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MERGERS & ACQUISITIONS DRIVERS AND FINANCIAL PERFORMANCE OF NON-FINANCIAL FIRMS LISTED AT THE NAIROBI SECURITIES EXCHANGE, KENYA

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ABSTRACT

The main objective of this study was to investigate mergers & acquisitions drivers and financial performance of non-financial firms listed at the Nairobi securities exchange, Kenya. The study specifically sought to determine the effect of market diversification, and financial synergy on financial performance of non-financial firms listed at the Nairobi securities exchange, Kenya. The study was anchored on the modern portfolio theory and financial synergies theory. With aim of achieving the aim of this study, descriptive design was employed that guided in establishing how non-financial firms' financial performance listed at the NSE in Kenya is affected by merger and acquisitions drivers. Population for this study was 5 non-financial institutions listed at the NSE in Kenya that underwent mergers and acquisitions during the period 2016 - 2021. Utilisation of collection sheet of secondary data involving review of documents were used containing available data on statements of finance that have been made available covering a period of 6 years. Nairobi securities exchange was the source of study's secondary data. Inferential analysis focused on use of analysis in multiple regressions as the study has more than two variables to be examined. The study found that that market diversification has positive and significant influence on financial performance of non-financial Firms listed at the Nairobi securities exchange, Kenya. Also, operating synergy was found to positively and significantly influence financial performance of non-financial Firms listed at the Nairobi securities exchange, Kenya due to reduced operating expense, consolidation of operations and synergies within the industry. The study therefore, recommends that the non-financial institutions listed on the NSE should concentrate on internal product or market development, acquisition of a firm, alliance with a complementary company, licensing of new technologies, and distributing or importing a product line manufactured by another firm. The study also recommends that these institutions should introduce new products that have technological or marketing synergies with existing product lines or industries while appealing to new customers, as well as introduce new products or services that are completely different from and unrelated to your core business.

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INTRODUCTION

Companies are becoming more aggressive in developing strategies to survive and grow in this globalization era. Every organization chooses the best strategy to win the competition and survive in the future (Bansal & Kumara, 2016). Mahmood, Aamir, Hussain and Sohail (2017) observe that with the global financial crises and the rapid advancement in technology has led to the increase on merger which has in turn made the organizations gain a large share of market, become competitive, increase their revenue earning and minimize risk and have a wide range of diversified products. Therefore, it can be argued that organization enters into a merger and acquisitions with the main objective being to gain access to unique assets that could take long in developing within the organization.

In the current market, financial performance improvement is paramount in the sustenance firm's capability, enthusiasm and worth. This is due the fact that the firm gains advantage in attracting managers with different talents and also able to increase their retention rate (Jovanovic & Peter, 2015). Appah and John (2016) observe that combining businesses using merger is now an international practice in achieving the economies of scale and high productivity. The demand for both financial as well as the non-financial institutions to undergo a merger is even very important in dealing with the global competition.

Ehrhardt and Brigham (2016) observe that a merger is a combination of two or more companies in which the resulting firm maintains a new identity different from the anticipated firms . A merger may be accomplished by one firm purchasing the other firms assets with cash or its securities or by purchasing the other shares or stock by issuing its stock to the other firms' shareholders in exchange for the shares of the acquired firm. Mergers and Acquisitions produce synergy, hence better use of complementary resources leading to geographical or other diversification (Gardiner, 2006). On other hand, Ehrhardt and Brigham (2016) define acquisition as taking over by one company of the share capital of another in exchange for cash, ordinary shares, loan stock or a combination of this. This results in the identity of the target being absorbed into that of the acquirer. An acquisition may be friendly or hostile. Whether a purchase is perceived as friendly or hostile depends on how its communicated and received by the target company's board of directors, employees and shareholders. It is quite normal though for M&A deal communications to take place in a so called 'confidentiality bubble' whereby information flows are restricted due to confidentiality agreements (Harwood, 2006). In the case of a friendly transaction, the companies cooperate in negotiations. In the case of a hostile deal, the takeover target is unwilling to be bought or the target's board has no prior knowledge of the offer. Hostile acquisitions can, and often do, turn friendly at the end, as the acquirer secures the endorsement of the transaction from the board of the acquire company which may require an improvement to the offer made. Mergers and acquisitions (M&A) perform a vital role in corporate finance by enabling firms achieve varied objectives and financial strategies.

Business combinations are always related to external business expansions, the reasons for business expansions include; obtaining acquiring new ways of facilities that are productive, productions knowledge, firms dealing with marketing, obtaining competent management, achievement of economies of scale and tax advantage (Zaneta & Lina, 2013). According to Sharma (2013) organizations merge on the basis of resource utilization of the already existing firm so as to improve its growth through increase in sales, reaching new markets and achievement of economies of scale.

According to Sudarsanam (2017) the main purpose of carrying out M&A is to increase the shareholders' value. Most firms seeking mergers and acquisitions seek to become the leading player in the product-market area of the strategic business unit. M&A are continuously occurring world over because they improve competition by gaining greater market share and reducing business risk. According to Kemal (2019) the performance of two firms that have merged or acquired improves due to the increase of shareholders value. The reasons that motivate M&A include economies of scale, revenue enhancement, tax reduction and others.

Statement of the Problem

The Deal Drivers Africa Report (2020) ranked Kenya as Africa's fourth most sought-after country for mergers and acquisitions mostly in consumer

and information technology. Activity in the Kenyanmarket is grow ing steadily and this can be attributed to the effici ency of regulations as well as the bodies tasked w ith implementing the regulations. Accordingto CA K(2018),150 merger notifications which are an im provement from the 130 notifications issued in the previous year(2017) noting that Ksh66 billion wa s added to the Kenyan economy by the merger tra nsactions conducted .Kenya has experienced a substantial increase in mergers and acquisition activity during the period 2013–2018(Kenya Financial stability report 2020) . On the other hand according to the recent Ease of Doing Business (2020) Report by the World Bank Group, Kenya improved by 5 places to position 56 globally out of 190 countries compared to position 61 in the 2018 report. The score improved by 2.2 points to 73.2 from 71.1 in the 2019 report.

However,
the 2019 Central Bank of Kenya (CBK) report sh ows that 25% of the financial institutions reported losses in the 2018/2019 financial year. This was an increase over the preceding five years where n ot more than 20% of the nonfinancial institutions had reported losses.In 2020, 14 NSE listed firms issued profit warnings compared to 11 and 17 in 2016 and 2019. Falling revenues and profitability, and furloughs of employees increases probability of defaulting on outstanding loans and reduces ability to borrow. The most recent release on Growth Domestic Product by the Kenya National Bureau of Statistics (KNBS) indicates that economic activity grew at the rate of 4.9 per cent in the first quarter of 2020 recording a drop from the 5.5 per cent growth rate recorded in the first quarter of 2019. This decline is attributable to the economic effects of the Covid-19 pandemic even as Kenya's major trading partners began facing the brunt of the virus within the first quarter of the year (CMA, 2019-2020).

A study by Ikpefan and Kazeem (2016) examined how the Nigerian Banking Industry performance was affected by merger and observed that synergy was created by merger because of statistical signi ficant financial performance of their post merger. However, convenience method of sampling was u sed which could lead to biasness in sampling.Che sang (2018) study investigated how commercial b anks' financial performance related with merger r estructuring show that the financial performance o f most of the institutions that had merged had no i mprovement due to introduction of merger restruc turing as evidenced by ratios on profitability and e arnings. Previous studies on mergers and acquisitions have focused on Financial firms mainly due to the streamline in the regulatory framework of their operations leaving a niche on non-financial firms .The continuous decline in financial performance in non-financial firms despite the recorded increase in M & A is what has challenged this study. These non-financial firms are regarded as icons of corporate financial stability and their collapse comes as a tremendous surprise to researchers and analysts .A study by Kimotho (2018) on effects of Mergers and acquisition financial performance of firms listed at the NSE show that The findings showed that there was a statistically significant effect of M&As on financial performance of firms listed in the NSE. This generalization of M& A on financial performance and left out an understanding of the drivers sought by mergers and acquisition .This study therefore seeks to examine drivers of mergers and acquisition and more specifically their effect on the financial performance of Non-financial firms listed at the NSE Kenya.

Objectives of the Study

The main objective of this study is to investigate Mergers & Acquisition drivers and the financial performance of non-financial firms listed at the NSE, Kenya. Specifically, the study sought to;

i. To examine the effect of Market diversification and the financial performance of non-financial firms listed at the Nairobi Securities Exchange, Kenya.
ii. To assess the effect of Operating synergy and the financial performance of non-financial firms listed at the Nairobi Securities Exchange Kenya.

LITERATURE REVIEW

Theoretical Review

Modern Portfolio Theory

The Modern Portfolio Theory (MPT) refers to an investment theory that allows investors to assemble an asset portfolio that maximizes expected return for a given level of risk. The theory assumes that

investors are risk-averse; for a given level of expected return, investors will always prefer the less risky portfolio. Hence, according to the Modern Portfolio Theory, an investor must be compensated for a higher level of risk through higher expected returns. MPT employs the core idea of diversification – owning a portfolio of assets from different classes is less risky than holding a portfolio of similar assets. Harry Markowitz published a paper on Modern Portfolio Theory in 1952. Markowitz proved that age-old adage "Don't put all your eggs in one basket" is true. Before the paper was issued, people had an intuitive sense that they should not put too much of their total wealth in a single investment or type of asset. Markowitz was therefore the first person to prove mathematically, that it was a question of how many eggs to put into which basket.. All these mathematical calculations are a way to structure and discipline your thinking as a portfolio manager – a way to reduce risk and improve overall return (Hudson-Wilson, 1990). HudsonWilson (1990), states, that the more advanced our thinking can become about the characteristics of each real estate investment and how it resembles and differs from others, the better the return we will be able to achieve. Portfolio Theory assumes an investor is both rational and risk averse and as such has a number of choices of investments to construct a portfolio. All investment opportunities involve risk and reward, an efficient frontier can be constructed where combinations of investments will have a given level of risk and return and at the efficient frontier will be the best possible risk reward combination. Markowitz (1952, 1959) showed that assets in a portfolio can be combined to provide an "efficient" portfolio that will give 19 the highest possible level of portfolio return for any level of portfolio risk as measured by the variance or standard deviation; these portfolios are thus connected to generate the "efficient frontier". Portfolios which have a combination below this efficient frontier will not be maximizing the efficient trade-off, according to the investors preferences. Having established an efficient frontier it is now necessary to decide where along the frontier the investor will choose a portfolio.

Modern portfolio theory is used to explain diversification as a drive to mergers and acquisitions. Managers merge and acquire firms with the intention of expanding their market share, customer base, product line with the aim of reducing risk while increasing their returns. The weighted cost of capital should always be less than the expected return. By diversifying a portfolio, chances of increased financial performance are ensured,

Financial Synergies Theory

This study was based on financial synergies theory by Fluck and Lynch (1999) who argues that with asymmetric information in financial markets, a firm with insufficient liquid assets or financial slack may not undertake all valuable investment opportunities. In this case, the firm can increase its value by merging with a slack-rich firm if the information asymmetry between the two firms is smaller than that between the slack-poor firm and outside investors. Thus, takeover was an efficient means to alleviate information asymmetries and achieve financial synergies. This theory predicts that firms in financial distress but with good investment opportunities are more likely to be involved in M&A activities, either as targets or as acquirers.

Lewellen (2011) argues that merger may achieve financial synergy by combining of imperfectly correlated income stream, or practically, acquiring another firm from an unrelated industry. Basically, this is the Markowitz portfolio diversification at the corporate level. The bad outcomes in one business can be offset by good outcomes in another business that brings lower earnings volatilities to merger firm. Lower earnings volatilities lead to the lower risk of default because both firms (merger firm) jointly insure the debt of each merging firm, which is called as coinsurance of corporate debt. Lower risk of default leads lower expected default costs and thereby increases the debt capacity or borrowing ability of the combined firm. The merger firm can gain benefit by increasing its financial leverage in order to achieve tax deductibility on behalf of its shareholders.

This theory is relevant to the study because synergies are most often evaluated in the context of mergers and acquisitions. Acquisition of Yu mobile telecommunication company by Safaricom and Airtel companies have seen synergy in various aspects of the firm. Safaricom acquisition of it's Tele-communication network has seen an

operational synergy in its economies of scale hence wide spread subscription across the East Africa community. Airtel acquisition of the market subscribers is clearly visible by the synergy in market share after the post-merger. These types of synergies relate to improvement in the financial metric of a combined business such as revenue, debt capacity, cost of capital, profitability etc. In addition, financial synergies can result in increased debt capacity, greater cash flows, lower cost of capital, tax benefits etc.

Conceptual Framework

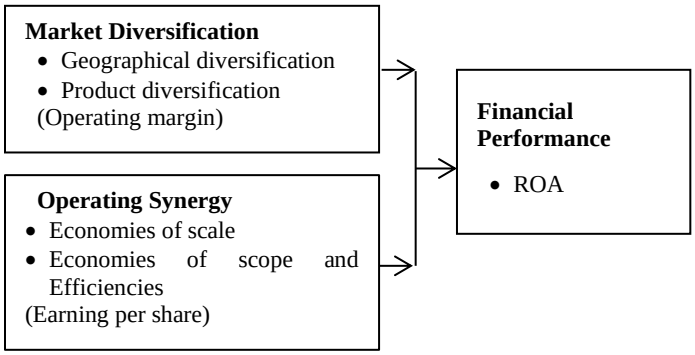

Figure 1: Conceptual Framework

Market Diversification

Firms merge to become more diverse, gain market share and penetrate new markets (Sekaran, 1992). Managers of firms often give diversification as a reason for entering into mergers and acquisitions. The explanation behind this is that the risk of earnings volatility is minimized when the activities of a firm are diversified. Thus when one aspect of operations is on the downside the loss can be compensated for or offset by increased or continued earnings in another aspect. This will then smoothen the earnings a company, which over time leads to smoothening of the stock price of a company; hence giving investors more confidence to invest in it. Market diversification is also seen as a risk reduction function of mergers;(Brealey et al, 2013), have though described this as dubious reason for mergers; this is so because though diversification in itself is a good thing there is need to analyze the cost associated with the venture as opposed to other options.

Market diversification ensures that there can be a smooth and efficient transition of the firm's knowledge to other business activities hence helping in the continuity of the firm (Campa and Kedia, 2002). Firms can achieve diversification either through internal growth or mergers. However, mergers are preferred because firms quite often lack internal growth opportunities due to lack of resources or when there is excess capacity in the industry.

Market diversification is achieved through merger by expanding geographically and by taking on different products or developing new ones using newly-acquired capability. Through taking over products in an industry , firms increase their market share and beat unnecessary competition .Mergers enable firms reduce competition to manage interdependence with sources of input/output Pfeffer (1972). Both firms no longer compete but now compete more effectively with other firms (Yash, 2005). Acquiring firms in very competitive product markets experience increased profitability, higher sales growth, and positive abnormal stock returns when they buy firms that increase their product differentiation. Market competitive is an advantage over other competitors gained by offering consumers greater value, either by means of levering prices or by providing greater benefits and services that justify higher prices. Hill (2001) identifies four building blocks of market competitive as efficiency, quality, innovation and customer responsiveness. Competitive is the single and most powerful weapon needed by firms to win and prosper in today's hyper-competitive world (Dulo,2006) .As a lethal weapon , competitive advantage enables firms enjoy unassailable position in the market (Robert ,2000) .Porter (1985) argues that market competitive can help firms erect entry barriers through economies of scale, proprietary products ,synergistic alliances and expected retaliation

The need for diversification is one of the reasons that firms make decisions to undertake mergers and acquisitions. Market diversification enables firms reduce risks as combined firms risks is less than the weighted average of the risks of the two firms prior to the merger.

Operating Synergy

Wealth creation for the shareholders is linked to operational synergy (Dennis & McConnel, 1986; Andrade et al., 2001). This strength happens in three major ways : economies of scale , cost synergy , and efficiency. Operating synergy refers to gains derived from operating economies gained from economies of scale, economies of scope and

reduction in administrative costs. The sources of these gains include economies of scale that are a result of increase in size of operations, increase in specialized management and efficient use of capital equipment which result in lower cost per unit (Gaughan, 2002).Economies of scale and scope are sources for synergetic gains from M&As (Weber et al., 2013). Economies of scale is the idea of spreading fixed costs, such as infrastructure, machinery and administrative costs, across a greater number of units produced. It is achieved when the output of a firm can increase with decreasing, or without the proportionate increase in, per unit cost of production. (Clark, 1988; The Economist, 2008)

A second source is the economy of scope which comes from reduction on average total costs as it is cheaper producing the same product from one firm than from two different firms (Depamhilis,2013). Example of cost savings is when the same set of skills for example marketing are used to sell products or services. To gain competitive edge in market, companies often merge to obtain economies of scale and scope (Hitt et al., 2001). If the transaction parties operate in the same market, integration can create economies of scale (Hitt, Ireland and Hoskisson, 2003). Economies of scale arise when the (output) generated by the combined entity is higher than the sum of the outputs when the two companies operate individually (Lambrecht, 2004).Economies of scope exist if the total cost for joint production of a certain product mix is less than independent production of each product (Clark, 1988). Examples of when economies of scope are obtained is when a business can share centralized functions (e.g. marketing economies of scope), when one product can be cross-sold alongside another or when output or residuals from one product or business can be used as input for another. Cross-selling of different products using the same processes for marketing and distribution is a good example of a driver in several of the conglomerate mergers that occurred in the 1990s (The Economist, 2008).

A third source is the value creation is acquired through efficient workflow processes (Cooper & Finkelstein, 2013). . Synergies most commonly result from cost reductions, as the integration of two companies enables the elimination of duplicate costs (Gardiner, 2006). These cost reductions lead to improved efficiency (Daniel, 2001; Clougherty, 2006). Efficiency can also be increased through better utilization of previously underutilized resources (Sherman, 2005).

Empirical Review

Market diversification and Financial Performance

M &A is one of the ways a firm can diversify into new markets. Mergers and acquisitions have also been used as an opportunity to grow existing business (Anslinger & Jenk, 2004). Firms benefit in access to new markets by tapping into segments that they would have been unable to reach individually due to geographical limitations or any other limitations that may exist.

Njoki Irene (2015) studied Competitive advantage gained by mergers and acquisitions. The research was a study which is British-American Investments Company Limited subject being limited to the employees located at the Upperhill in the month of October 2015. According to the study, mergers and acquisition can be used as a means to diversify into new markets and hasten the pace of market entry and increase product lines. They also enable firms to penetrate foreign markets that have barriers to entry. Mergers and acquisitions enable firms to curb regulatory bodies by merging with firms that already have the prerequisite license and thus speed up the process of market entry .Market dynamics especially in technology businesses force firms to react quickly. Organizations undertake acquisitions and mergers to react to the market conditions faster and thus gain competitive advantage especially where time is critical. Mergers and acquisitions provide an avenue for firms to adjust capabilities in order to meet the dynamic market demand. Firms will therefore determine how alliances will assist in developing new products that are deviate from existing market demand.

Ward Wolters (2012) research on The influence of Diversification and M&A examines the Accounting effect on Firm Value on Firms. Using a sample of 45,283 firm year observations between 1993–2012, Wards recognized that firms diversify from two dimensions namely industry and geographical. Over time the discount decreases for geographical diversification. A clear trend for the discount of domestic industrially diversified firms is observed. For later periods, M&A accounting

implications result in an increasing bias for multinationals. Including firm fixed effects does not lead to significant results, which indicates that unobserved firm characteristics explain for earlier document discounts. Examination of the value effects of diversification and M&A accounting across industries finds evidence that for low-goodwill industries the bias resulting from M&A accounting implications is lower. In addition it is evidence that the value consequences of diversification differ between industries. Firms that are operating in the Mining and Construction industry are valued at a premium relative to both domestic single-segment firms and diversified firms in other industries.

Caroline Wanjiru (2011) studied Mergers and acquisition as a competitive advantage on firms in the oil industry in Kenya. The research design was a case study of Total Kenya Limited data collection tool being an interview guide in the period 2009-2010 .The results indicated that there need for diversification is one of the reasons that firms make decisions to undertake mergers and acquisitions. Diversification enables firms reduce risks as combined firms risks is less than the weighted average of the risks of the two firms prior to the merger. Firms merge to become more diverse, gain market share and penetrate new markets. Mergers enable firms reduce competition to manage interdependence with sources of input/output. Both firms no longer compete but now compete more effectively with other firms. A market power effect occurs automatically as a merger calls for a higher market share making the new firm the market leaders

Operating Synergy and Financial Performance

Synergy has three main benefits which include the operating, financial and managerial synergies. According to Chesang (2002) for synergy to be achieved the costs from the combined firms have to be less than the total of each firm accrediting the reduction in economies of scale and scope Operating synergy is successfully employed by enhancing revenue while financial synergy is regarded as the impact to which a corporate merger has on the overall cost of capital to the acquiring organization thus the firms carry the possibility of having access to cheaper capital.

A study by Ochoki George 2016 investigated the effect of synergy on financial performance of merged institutions in the financial services sector in Kenya. The paper adopted a mixed research design, pre and post-merger secondary data was collected from 40 (forty) institutions in the Kenyan financial services industry that had concluded their merger processes by 31 December 2013.Financial synergy was proxy using the liquidity ratio while operating synergy was measured using growth in sales. Primary data was used to explain the results of the secondary data while regression analysis was used to determine the relationship between synergy and profitability. Results show that there is a positive relationship between performance, operating synergy and financial synergy, and that there was significant improvement in performance post-merger.

Junge (2014) studied the changes in operating performance brought by the synergy types after the merger. The sample consisted of 420 mergers which occurred from 1988 to 2008. The results indicated an improvement in overall operating performance. Mergers which aimed at achieving efficiency synergy portrayed a steady performance improvement compared to those that aimed at synergy from complementary resources. A study by Ogada, Njuguna, and Achoki (2016) was conducted to determine the effect synergy had on financial performance of merged institutions within Kenya's financial service sector. A mixed research design was used and data was obtained from forty firms which had already done their merger processes by 2013. Study findings showed there existed a firm correlation between performance, operating synergy and financial synergy as well as a performance post-merger improvement.

A research on the effects of Mergers and Acquisitions when attaining synergy for commercial banks in Kenya was conducted by Misigah (2013). The study's population consisted of 15 banks which from the year 2000-2010 had successfully completed their merger and acquisition transactions. The ratios were analysed so as to provide a comparison of the effects mergers have on growth in assets, profitability and shareholders' value at both pre and post-merger periods. The outcomes implied that the banks undertook mergers due to the rise in stakeholders' value and profitability growth. Therefore, mergers were significantly contributed to rise in profitability

and synergy. Fatima and Shehzad (2014) further conducted a research to determine the effects of M&As of insurance firms' financial performance within Pakistan from which analysis was conducted on only six financial ratios. The study sample consisted of ten firms which from2007 to 2010 were already into mergers. A three-year pre and post-merger data points obtained from the firms after which their averages were compared. The findings found no relationship between synergy and financial performance.

RESEARCH METHODOLOGY

This study employed a descriptive research design. According to Dulock (2014) descriptive research design is a scientific method which involves observing and describing the behavior of a subject without influencing it in any way.

Mugenda and Mugenda (2003) observe that population is composed of a total number of individuals in a group whereby a representable size of a sample can be obtained. Population for this study was 5 Non-financial Firms listed at the NSE Kenya that have undergone merging and acquisition in the period 2016-2021.

Utilization of collection sheet of secondary data involving review of documents was used containing available data on statements of finance that have been made available covering a period of 6 years from 2016 to 2021.

The main reports of interest included; Statement of Financial Position, Income Statement, and Cash Flow Statement. Nairobi securities exchange was the source of study's secondary data. Measurement of non-financial institutions' financial performance mainly focused on return on assets (ROA).

The data was collected from annual audited and published financial statements for all ten (5) non-financial firms for the six year period under study (2016 to 2021) using secondary data collecting sheet. The financial statements were obtained from Nairobi Stock Exchange

The extracted data was input to pre-structured work sheet which involved analysis per company.

Quantitative data was analyzed descriptively in terms of mean and standard deviation.

Statistical Package for Social Sciences (SPSS) version 20 was use to analyzed quantitative data. Inferential analysis focused on use of analysis in multiple regressions as the study has more than two variables to be examined.

RESEARCH FINDINGS AND DISCUSSIONS

Descriptive Statistics

Table 4.1: Descriptive Statistics

Variables	N	Min.	Max.	Mean	Std. Dev.
Market Diversification	30	0.71802	0.1049	0.0933	0.1362
Operating Synergy	30	1.2923	2.7166	1.8793	2.5969
Financial Performance	30	1.0438	2.0558	1.5655	1.7902

ROA

From the findings in Table 1, the average ROA for the sample of 5 companies between 2016 and 2021 is 1.5655, with a minimum of -0.6442 and a maximum of 5.7705. ROA is a measure of a company's financial performance and indicates its ability to generate profits from its assets. The mean value suggests that on average, the companies made profit but the negative minimum value suggests that there are companies that made losses. There was however small deviations in data points from the mean value as indicated by a standard deviation of 1.7902. The trend in ROA of the companies over the 6-year period is as shown in figure 4.1 below. From the figure, it is seen that the average data points were not far from the mean. Also, on average, the companies were profitable since they all had positive ROA. A higher ROA indicates that the company is more efficient in generating profits from its assets.

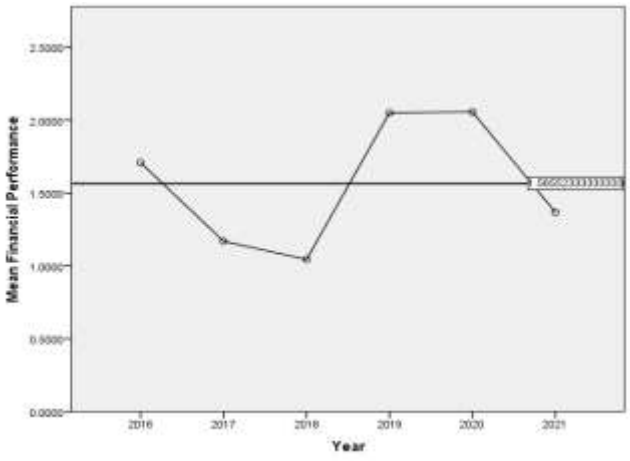

Figure 1: Trend Analysis in ROA

Market Diversification

Market diversification was measured using operating margin. The average operating margin for the five companies in 6 years is 0.0933, with a minimum of -0.2294 and a maximum of 0.4061. This suggests that the companies studied had different levels of market diversification. This is shown by Figure 2 which shows that between 2016 and 2021, the level of market diversification fluctuated. Operating margin is a measure of a company's profitability and efficiency in generating revenue from its operations. The standard deviation of operating margin is 0.1362. This means that the data points for operating margin are relatively spread out, with some companies having much higher operating margins and some companies having much lower operating margins compared to the average. A higher operating margin indicates that the company is more efficient in controlling its costs and generating profits from its core operations.

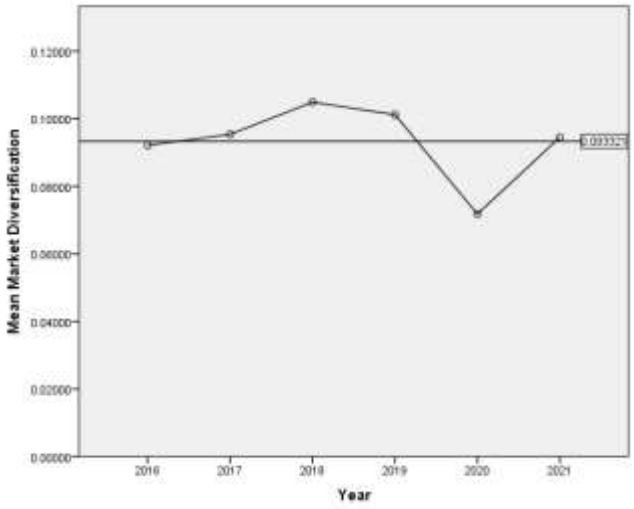

Figure 2: Trend Analysis in Market diversification
Source: Research Data (2022)

Operating Synergy

In this study, operating synergy was measures using EPS. From the findings in Table 1, the average Operating synergy level by non-financial Firms listed at the Nairobi securities exchange was 1.879333. There was however different levels of operating synergy recorded by the companies with minimum being 1.2923 and maximum being 2.7166. From the variance level of 5.27587, the findings show that the the data set was highly spread and the large standard deviation of 2.2969268 suggests that the data points had a huge deviation from the mean. This is seen in Figure 4.3 which shows that between 2016 and 2021, the companies recorded on average fluctuating synergy levels. There was no clear trend in synergy levels recorded by the companies.

This shows that the operating synergy in companies varied. This is because synergy is likely caused by the Earning per Share (EPS) of the Non-financial Firms listed at the NSE Kenya.

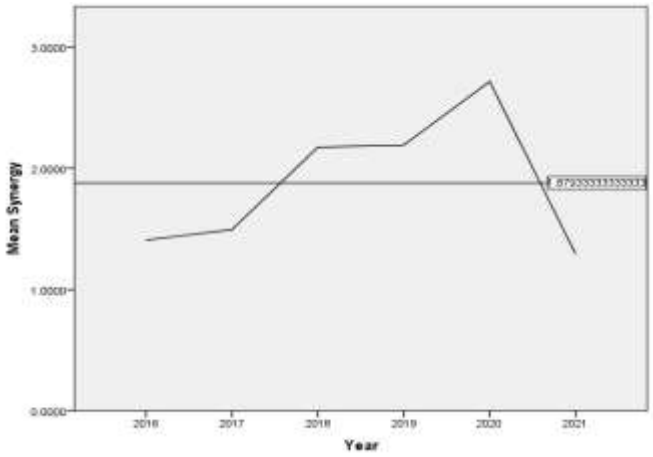

Figure 4.3: Trend Analysis in Operating Synergy
Source: Research Data (2022)

Operating synergy can be defined as the degree to which the operations of different businesses within a company complement and enhance each other. Earnings per share (EPS), which is calculated by dividing net income by the number of outstanding shares of stock, is a widely used metric to evaluate a company's profitability and financial performance.

The study used EPS to measure operating synergy among the companies under investigation. Our trend analysis in Figure 4.3 revealed that the minimum EPS value was 1.292 in 2021, while the maximum value was 2.716 in 2020.

Therefore, the EPS was at its peak in 2020 and then decreased sharply in 2021. This trend could be attributed to various factors such as changes in revenue, cost-cutting measures, or expansion of the business.

Inferential Statistics

Inferential statistics were conducted to determine the relationship between the study variables. The study computed correlation analysis and multiple

regression analysis.

Correlation Analysis

Correlation Analysis between market diversification and financial performance of non-financial firms listed in the NSE

The Pearson's correlation was checked to ascertain whether or not there is a statistical relationship between market diversification and financial performance of the firms. Table 4.8 show the Pearson's correlation coefficient between the market diversification and financial performance being .856, $p<0.05$, two tailed, tested at 95% confidence level. The results showed that there is positive and significant relationship between market diversification and financial performance of the firms.

Table 2: Pearson Correlation Coefficient between market diversification and financial performance of non-financial firms

		financial performance	market diversification
financial performance	Pearson Correlation	1	
	Sig. (2-tailed)		
	N	30	
market diversification	Pearson Correlation	.856**	1
	Sig. (2-tailed)	.000	
	N	30	30

**. Correlation is significant at the 0.01 level (2-tailed).

With these results, improved market diversification in non-financial firms listed in the NSE leads to an improvement in financial performance of strongly.

Correlation Analysis between operating synergy and financial performance of non-financial firms listed in the NSE

The Pearson's correlation was checked to ascertain whether or not there is a statistical relationship between operating synergy and financial performance of the firms. Table 3 show the Pearson's correlation coefficient between the operating synergy and financial performance being $r=0.705$, $p<0.05$, two tailed, tested at 95% confidence level. The results showed that there is positive and significant relationship between operating synergy and financial performance of the firms. This shows that operating synergy influences financial performance of the non-financial firms listed in the NSE.

Table 3: Pearson Correlation Coefficient between operating synergy and financial performance of non-financial firms

		financial performance	operating synergy
financial performance	Pearson Correlation	1	.705**
	Sig. (2-tailed)		.000
	N	30	30
operating synergy	Pearson Correlation	.705**	1
	Sig. (2-tailed)	.000	
	N	30	30

**. Correlation is significant at the 0.01 level (2-tailed).

With these results, it implies that improved operating synergy in non-financial firms listed in the NSE leads to an improvement in financial performance moderately.

Regression Analysis

The effect of one variable on the other was determined using regression analysis. This was realized by regressing market diversification, operating synergy, financial capacity expansion, and assets acquisition on financial performance of non-financial firms listed in the NSE.

Table 4: Model Summary

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.891[a]	.793	.786	.08745

a. Predictors: (Constant)operating synergy, market diversification

A summary of the model is shown in Table 4, which includes information about the retrospective linear narrative capability for the full range of dependent variables. R is the ratio of the strength of the relationship between dependent and independent variables and is represented by a factor of 0.891. The correlation coefficient (r) indicates that the predictor variables of this study therefore have a strong relationship with the financial performance of non financial firms.

The coefficient of determination, also known as R^2, is a mathematical estimate that depicts variations in the response variable that is brought about by the variation in predictor variables. The coefficient of determination for this study was 0.793. This implies that market diversification, operating synergy, financial capacity expansion and assets acquisition explain 79.3 percent of the variation in financial performance of non-financial firms listed in the Nairobi securities exchange (NSE). Other variables not included in this model explain 21.7 percent of the variations in financial performance.

Analysis of Variance Summary (ANOVA)

Table 5: Analysis of Variance

Model		Sum of Squares	Df	Mean Square	F	Sig.
1	Regression	3.404	4	.851	111.323	.000[b]
	Residual	0.2	25	.008		
	Total	3.604	29			

a. Dependent Variable: financial performance
b. Predictors: (Constant)operating synergy, market diversification

Analysis of variance was done in order to determine if market diversification, operating synergy, financial capacity expansion and assets acquisition were significant contributors of financial performance of non-financial firms listed in the NSE. The F statistics listed in the table was 111.323 with a corresponding P value of 0.000. Since the P value was less than the standard P value of 0.05, it implies that the four variables jointly had significant influence on the financial performance. The model is therefore statistically significant in predicting how market diversification, operating synergy, financial capacity expansion and assets acquisition affects financial performance of non financial firms listed at the NSE, Kenya.

Beta Coefficients Summary

Table 6: Beta Coefficients of study variables

Model	Unstandardized Coefficients		Standardized Coefficients	t	Sig.
	B	Std. Error	Beta		
(Constant)	.164	.025		6.545	.000
market diversification	.291	.094	.377	3.090	.003
operating synergy	.116	.058	.192	2.003	.048

a. Dependent Variable: financial performance

An increase in market diversification by 1 unit would lead to 0.291 unit increase in financial performance of the non-financial firms. An increase in operating synergy by 1 unit would lead to 0.116 unit increase in financial performance of the non-financial firms.

$$\mathbf{Y = 0.164 + 0.291X_1 + 0.116X_2}$$

Whereby **Y** = Financial Performance (ROA)

$\mathbf{X_1}$= Market Diversification

$\mathbf{X_2}$= Operating Synergy

The study established that market diversification as indicated by beta value ($\beta = 0.291$, $p < 0.05$), had a positive and significant influence on the financial performance of non-financial firms. This is in line with a study conducted by Ward Wolters (2012) that examined the influence of Diversification and M&A examines the Accounting effect on Firm Value on Firms. Using a sample of 45,283 firm year observations between1993–2012 and recognized that firms diversify from two dimensions namely industry and geographical.

The study revealed that operating synergy as indicated by the beta value ($\beta = 0.116$, $p < 0.05$), had a positive and significant influence on the financial performance of non-financial firms. . This is in line with the findings of a study by Ochoki (2016) that investigated the effect of synergy on financial performance of merged institutions in the financial services sector in Kenya and found that there is a positive relationship between performance, operating synergy and financial synergy, and that there was significant improvement in performance post-merger.

Conclusion

The study concludes that market diversification has positive and significant influence on financial performance of non-financial Firms listed at the Nairobi securities exchange, Kenya. This is because market diversification enables non-financial institutions to spread risk across various types of investments, with the goal of increasing their chances of investment success. Because markets can be volatile and unpredictable, market diversification is essential in investing. As a result, when non-financial institutions diversify their markets, they reduce the risk of loss to their overall portfolio, expose themselves to more opportunities for return, protect themselves against adverse market cycles and reduce volatility.

The study concludes Operating Synergy positively and significantly influences financial performance of non-financial Firms listed at the Nairobi securities exchange, Kenya due to reduced operating expenses, , consolidation of operations and synergies within the industry. There is improved financial performance in terms of profitability for the non-financial firms. This has enhanced the stability and effectiveness of operations of the non-financial institutions. The financing cost of the institutions decreased after a merger and acquisition, and this eventually led to better financial performance of the firms. This has improved the firm's operational stability and effectiveness. Following a merger and acquisition, the financing costs decreased, resulting in improved financial performance. In exchange,

benefits might ascend in the short and medium term, while the firms' odds of long haul development and extension improve.

Recommendations

The study recommends that firm's investors ought to basically assess the blending foundations' general business and functional similarity and spotlight on catching long haul functional collaborations. They ought to widen their extension to fabricate high-performing supply chains with huge long haul potential gain that convey long haul worth to clients and partners. The study also recommends the critically evaluating of merging overall business and financial compatibility, with a focus on capturing long-term synergies.

The study recommends that the management should invest in a diverse range of assets, including bonds, stocks, and real estate etc. so as to reduce the volatility and risk to their portfolio by holding investments that have a low correlation to one another. The firms should distribute capital in a manner that diminishes openness to any one resource or hazard, decreasing danger or unpredictability by putting resources into a different scope of resources.

Non-financial firm contribute tremendously to the economy of our county Kenya. Through quantitative analysis of the financial statements publicly published at the Nse on financial firms takes over 50 % representation of companies registered at the exchange .The study recommend that the government and regulators should create favorable business environment for the operations of these firms. Through continuous policy making the process of M& A should be encouraged and made seamless.

Suggestions for Further Studies

Previous scholars have dwelt on the discussions of financial firms and how mergers and acquisition affected their financial performance. To make our study unique we chose to focus on non-financial firms and more specifically drivers that motivate managers choose M& A as turnaround tactic to financial improvement.

The Kenyan Nairobi stock exchange had seven recognized non-financial industries .The study therefore suggests that further studies should give in-depth and analysis on specific sectors in the non-financial industry and how M& A drivers affect their financial performance. Aimed at gaining insights into the drivers of acquisition activity, focus on comparing the characteristics of different acquisition and mergers activity i.e. either hostile or friendly would give an understanding of other possible drivers of Mergers and acquisition in specific industries.

The study r- squared in our study was 0.793.This Means that other drivers rather than markets diversification, operating synergy, financial capacity expansion and assets acquisitions impacted the financial performance of non-financial firms at 20.7% .So as to gain insightful knowledge on non-financial firms financial performance ,the study recommends for researchers to perform further studies on these factors.

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