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Effect Of Mergers And Acquisition On Returns To Shareholders Of Conglomerates In Nigeria

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Abstract
This study analyzed the investment returns to shareholders of conglomerate companies that have carried out mergers and acquisitions and their performances. Panel data for the study was collected on four sample companies for the period of fifteen years. Conglomerates companies were purposively selected for this study because they are the only sector on the Nigeria stock exchange list that has carried out merger and acquisition which covered the period of study (1990-2005). Our findings show that the relationship of net total assets in relation to the turnover, profit tax and profit margin portend a positive relationship. On the other hand the relationship between net total assets in relation to profit after tax, earnings per share and return on capital employed shows otherwise. It is recommended that companies should translate the improved performance into benefit for the shareholders.
Key words: Mergers, Acquisition, Returns, Shareholders

1. Introduction

Contemporary business organization seek to grow for business survival and such an assertion can be supported by Freier's (1990) empirical observation that "over the past twenty (20) years, the minimum company size required to compete successfully in most industry segments has been steadily increasing". Under the premise that growth is a vital element for business survival, a firm can grow and develop core competences either internally by investing in and nurturing within-firm resources or externally by acquiring another firm. Corporate organizations need to expand in today's increasingly competitive and international business environment so as to achieve economies of scale in production, promotion and distribution. Mergers and acquisition is no doubt one way in which to obtain such drastic expansion or growth.

Albert and Joel (1986) opined that "One of the key stones of a free enterprises and prices determined economy (i.e. capitalism) is the strategy for entry". Every corporate entity in such an economy is faced with a problem of growth whether in output or profitability. In today's global business environment companies may have to grow to survive and one of the best ways to grow is by merging with another company or acquiring other companies. Growth may be achieved through internal or external entry into a new industry or market. While internal entry involves -increasing unit sales consistently and developing new products through research and development; External entry includes - Mergers and Acquisitions and strategic alliance.

A merger occurs when one firm assumes all the assets and all the liabilities of another firm. The acquiring firm retains its identify, while the acquired firm ceases to exist. A majority vote of shareholders is generally required to approve a merger. A merger is just one types of acquisition. One company can acquire another company in several other ways, including purchasing some or all of the company's assets or buying up its outstanding shares of "stock.

In general, mergers and acquisitions are performed in the hopes of realizing an economic gain. For such a transaction to be justified, the two firms involved must be worth more together than they were apart. Some of the potential advantages of mergers and acquisition include achieving economics of scale, combining complementary resources, garnering tax advantages and eliminating inefficiencies. Other reasons for considering growth through mergers and acquisitions include obtaining proprietary rights to products or services, increasing market power by purchasing competitors, shoring up weaknesses in key business areas, penetrating new geographic regions or providing managers with new opportunities for career growth and advancement.

When a small business owner chooses to merge with or sells out to another company, it is sometimes called "harvesting", the small business. In this situation, the transaction is intended to release the value locked up in the small business for the benefit of its owner and investors. The impetus for a small business owner to pursue a sale or merger may involve a need to diversify his or her investment, an inability to finance growth independently, or a simple need for change. In addition, some small businesses find that the best way to grow and compete against larger firms is to merge with or acquire other small businesses.

In general, acquisitions can be horizontal, vertical or conglomerate. A horizontal acquisition takes place between two firms in the same line of business. For example the acquisition of the Nigerian Soft Drinks Company us. Limited (NSDC)- bottlers of the Schweppes range of soft drinks by the Nigeria of Bottling company- bottlers of

the coca-cola soft-drink. In contrast, a vertical merger entails expanding forward or backward in the chain of distribution, to towards the source of raw materials or towards the ultimate consumers. For example, an Auto parts manufacturer might purchase a retail auto part store. A conglomerate is formed through the combination of unrelated business.

Other types of combination of two companies are a consolidation. In consolidation, an entirely new firm is created, and two previous entities cease to exist. Consolidated financial statement are prepared under the assumptions that two or more corporate entities are in actuality only one. Another way to acquire a firm is to buy the voting stock. This can be done by agreement of management or by tender offer. In a tender offer, the acquiring firm makes the offer to buy stock directly to the shareholders thereby by-passing management. In contrast to a merger, a stock acquisition requires no stockholder voting.

In principles, the decision to merge with or acquire another firm is a capital budgeting decision much like any other investment decisions. But mergers and acquisition differ from ordinary investment decisions in at least five ways. First, the value of a merger and acquisition may depend on such things as strategies fits that are different to measure. Second, the accounting, tax and legal aspects of a merger can be complex. Third, mergers often involve issues of corporate control and are a means of replacing existing management. Fourth, mergers obviously affect the value of the firm, but they also affect the relative value of the stocks and bonds. Finally, mergers are often unfriendly (Averbach, 1988).

Prior to 1980's, Mergers and Acquisitions was an alien concept to the Nigeria business environment but not so anymore-Mergers and acquisitions have made their debut in some Nigerian business. Nigeria's economic has been in recession for a number of years. Some companies have had significant reduction in capacity utilization due to the combine effect of lowering aggregate demand and the problems of supplies to meet production requirement (Akamiokahor, 1992). Inflation has been on double digits numbers and interest rate on borrowed funds has increased only of recent reduced to eleven (11%) percent officially. Production cost have consequently been escalating due to the depreciation of Naira now officially at N140 to a Dollar (July 2006) as compared to N1.35k to a Dollar 2000,(N1) One Naira to the Dollar in 1986 and (N1.50R) One Naira Fifty Kobo to a Dollar 1988.

Profit margins of the companies have also come under severe pressure. The deregulation of the economy is the best thing that has ever happened in this country since independence but it now means that companies have to compete for an increasing share of a decline market through pricing, improved product quality, improved services and other marketing mix (Giwa, 1989). The high cost of capital and the replacement cost of existing assets in the face of cash squeeze, towering profit margins and fierce competition means that the winners shall be companies with very able and efficient management with the right products portfolio and who recognizes all the dynamics in their business and the environment and must be capable of putting their fingers on all the critical Issues of today.

These changes in the Nigerian business environment demand that adoption of Mergers and Acquisitions as growth for business organization. While firm seeks the external mode, the Mergers and Acquisitions transaction. The most critical concern will be whether the Merger and Acquisition transaction will create economic gains. This might relate to the type of business and corresponding performance to be purchased by a firm. That is the type of diversification should a firm choose in implementing a growth strategy. The type of diversification refers to the degree of business relatedness or fit between the acquiring and acquired firms. In addition to the above issues, merger and acquisition professionals have pointed out that the magnitude of economic gains will depend largely upon the cultural fit between two combining firms. Further, they have argued that management of acquired firms should be retained after the completion of Merger and Acquisitions transaction because acquiring firms tend to regard knowledge of the management as a valuable asset. This study therefore attempts to document and analyze the investment returns to shareholders of conglomerate companies that have carried out mergers and acquisitions and their performances.

2. Literature Review

Mergers and acquisitions are a global business terms used in achieving business growth and survival. Merger entails the coming together of two or more firms to become one big firm while acquisition is the takeover or purchase of a small firm by a big firm; which are both pursuing similar motives (Katty, 2005). Accordingly, Soludo (2004) opined that mergers and acquisitions are aimed at achieving cost efficiency through economies of scale, and to diversity and expand on the range of business activities for improved performance. Numerous studies have empirically examined whether mergers and acquisitions are solutions to bank problems. The studies of Cabral et al. (2002), provided the foundation for a research on the linkage between banks mergers and acquisitions and profitability. Evidence as provided by De-Nicolo (2003), suggested that mergers and acquisitions in the financial system could impact positively on the efficiency of most banks. Surprisingly, the available empirical evidence suggests that mergers and acquisitions operations in the United States banking industry have not had a positive influence on performance in term of efficiency (DeLong and Deyoung, 2007). Overall of these studies provide mixed evidence and many fail to show a clear relationship between mergers and

acquisitions and performance. Some of the previous literature has examined the impact of mergers and acquisitions operation on cost efficiency as measured by simple accounting cost ratios (DeLong and DeYoung, 2007). Also, evidence supporting mergers and acquisitions to achieve cost saving and efficiency gain is sparse (Kwan and Elsenbeis, 1999). Akhavein et al. (1997) analysed changes in profitability experienced in the same set of large mergers as examined by Berger and Humphrey (1992). They found that banking organizations significantly improved their profit efficiency ranking after mergers.

De Young (1993) find that when both the acquirer and target were poor performers, mergers resulted in improved cost efficiency. Healy et al. (1992) examined all commercial banks and bank holding company mergers and acquisitions occurring between 1982 and 1986. They found that mergers and acquisitions did not reduce non-interest expenses that could have led to improved efficiency. According to Pilloff and Santomero (1997), there is little empirical evidence of mergers achieving growth or other important performance gains. Their findings undermine a major rationale for mergers and consequently raised doubt about other benefits mergers and acquisitions may provide to businesses. However, Cornett and Tehranian (1992) and Kay (1993) find some evidence of superior post merger period because of the merged firms' enhanced ability to attract loans. They also show increased employee productivity and net asset growth. Also, this is evident in the Nigeria's banking industry (Okpanachi, 2006).

Walter and Uche (2005) posited that mergers and acquisitions made Nigerian banks more efficient. They used table to present their data which was analyzed using simple percentage. Akpan (2007), using chi square to test his stated hypothesis found that the policy of consolidation and capitalization has ensured customers' confidence in the Nigerian banking industry in term of high profit. But, for Sobowale (2004) and Osho (2004), it is expected that the value of the companies that participated in mergers and acquisitions activities would be higher than before because future dividends and earning streams are expected to rise and subsequently improves efficiency. Similarly, Uchendu (2005) and Kama (2007) opined that, the bank consolidation which took place in Malaysia facilitated banks expansion which led to growth. In a related study of the Chilean banking industry, Kwan (2002) found that the high rate of economic activities experienced in Chile was mainly from productivity's improvement from the large banks formed as a result of mergers and acquisitions.

The studies by Berger and Mester (1997) and Stiroh (2002) using data on United States banks suggested that, there may be more substantial scale efficiency from larger sizes of banks as a result of mergers and acquisitions. But for Straub (2007), mergers and acquisitions have often failed to add significantly to the performance of the banking sector. Surprisingly, the majority of studies comparing pre and post mergers performance found that, these potential efficiency derived from mergers and acquisitions rarely materialize. Towards this end, Beitel et al. (2003) found no gain effect due to mergers and acquisitions, but for Yener and David (2004), mergers and acquisitions played an important role in improving after merger financial performance which is a stimulus for efficiency. Most of the studies examined found that mergers and acquisitions add significantly to the profits of the banking sector, except for Straub (2007) and Rhoades (1993) that have contrary views.

3. Methodology

Data for the study was collected on four sample companies for the period of 15 years. Data were obtained from annual reports and statement of accounts of the sample companies. Conglomerates companies were purposively selected for this study because they are the only sector on the stock exchange list that has carried out merger and acquisition which covered the period of study (1990-2005). Variables used in this study include profitability performance measure by sales/turnovers, net profit, earnings per share, returns on capital employed, and market adjusted returns of securities.

4. Results

Table 1 reveals that the relationship of net total assets in relation to the turnover, profit tax and profit margin portend a positive relationship of 0.721 (72.1%), 0.758(75.8%) and 0.779(77.9%) respectively. The p-value further collaborate the result of the correlation co-efficient that the relationship is significant and t-value greater than 2. On the other hand the relationship between net total assets in relation to profit after tax, earnings per share and return on capital employed shows otherwise as correlation coefficient is 0.026(2.6%), 0.342 (34.2%) and 0.271(27.1%) respectively and t-value less than 1.5.

5. Conclusion

This study analyzed the investment returns to shareholders of conglomerate companies that have carried out mergers and acquisitions and their performances. Panel data for the study was collected on four sample companies for the period of fifteen years. Conglomerates companies were purposively selected for this study because they are the only sector on the Nigeria stock exchange list that has carried out merger and acquisition which covered the period of study (1990-2005). Our findings show that the relationship of net total assets in

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Table 1

Variables	R	T	P-value	Decision
NTA and turnover	0.721	4.025	0.000	Significant
NTA and profit	0.758	4.504	0.000	Significant
NTA and profit margin	0.779	4.817	0.000	Significant
NTA and profit after tax	0.026	-0.099	0.923	Not significant
NTA and EPS	0.342	1.408	0.179	Not significant
NTA and ROCE	0.241	1.090	0.297	Not significant

Source: Data analysis, 2011

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