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THE IMPACT OF MERGERS AND ACQUISITIONS ON THE CORPORATE FINANCIAL PERFORMANCE OF GUINNESS GHANA BREWERIES LIMITED

BY

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A DISSERTATION SUBMITTED TO THE DEPARTMENT OF ACCOUNTING AND FINANCE OF THE SCHOOL OF BUSINESS OF THE UNIVERSITY OF CAPE COAST IN PARTIAL FULFILLMENT OF THE REQUIREMENTS FOR THE AWARD OF MASTER OF BUSINESS ADMINISTRATION

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DECLARATION

Candidate's declaration

I hereby declare that this dissertation is the result of my own original research and that no part of it has been submitted for another degree in this university or elsewhere.

Candidate's signature……………………… Date ……………………………

Name:

Supervisor's declaration

I hereby declare that the preparation and presentation of this dissertation were supervised in accordance with the guidelines on supervision of dissertations laid down by University of Cape Coast.

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ABSTRACT

Mergers and acquisitions are a relatively new but fast growing phenomenon in the Ghanaian economy as a response to increasing competition, emanating from the changing business environment. However, because they are relatively new in the country, mergers and acquisitions are not well understood in Ghana.

This study examines the impact of mergers and acquisitions on the acquiring company's corporate financial performance, within the Ghanaian economy, using Guinness Ghana Breweries Limited as case study. The issue was investigated using performance measure based on the company's annual reports.

The results of the study show that the accounting performance declined after the merger. There has being a downward fall in profitability performance. Sales growth declined sharply during the post-merger periods, although in absolute terms there were increases. Operating expense has being increasing while liquidity and financial leverage have both being on the decline. However, earnings per share and dividends per share were in continuous increase from the pre-merger period to the second post-merger year, due to the increases in absolute post-merger sales. But in the third post-merger year both of these indicators started to decline sharply.

To be able to attain the merger objectives of achieving synergy, reducing cost of operations and improving market performance and profitability of the joint

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operations and other performance benefits, the company should strengthen its business processes, restructure its capital base and improve its cash operation cycle.

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DEDICATION

To my parents, Mama Afua Daalon Seidu and the late Seidu Lienyuri Donyaga,, and also to my late aunt, the late Pogsaa Seidu

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Finally, the following organizations deserve mention and gratitude: Strategic African Securities (SAS), Merban Registrars (a division of Merchant Bank Limited), Ghana Stock Exchange (GSE) and Guinness Ghana Breweries Limited. Special mention must be made of Mrs. Harriet Antwi, head of Merban Registrars; Miss Angela, head of SAS Research Department and Mrs Woode , head of GSE Research Department.

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CHAPTER ONE

INTRODUCTION

Background

The changing economic, technological, social and political environment and new forms of competition, fueled by advances in Information Technology and Communication as well as Globalization, have combined to create new opportunities and threats for business firms. With globalization, a company no longer competes with only other companies within the same country, but also with companies in other countries around the world. In order to survive, firms must adjust to forces of competition from all directions.

Firms adopt various growth strategies to counter competitive challenges and or take advantage of opportunities emanating from the changing environment. Corporate growth is generally viewed as essential for the well being of a firm. Size and scale are obviously becoming critical as firms compete in today's market (Hoyle, Schaefer and Doupnik, 2001). For many companies, especially in brewery industry in Ghana, corporate growth has been a major survival strategy. Among other reasons, growth is needed by a firm to enable it compete for the best managerial talent by offering rapid promotions and broadened responsibilities. Without a continued inflow of competent executives, firms are likely to decline in efficiency and value.

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Firms can achieve growth through internal or external expansion. Internal growth involves investing internally to extend existing operations to provide new capacity, new product or to serve new markets. It occurs within the same corporate entity and under the same management. Normally, this form of growth is relatively gradual and predictable as the business identifies the natural growth available to it, in areas it has an established position. External growth, on the other hand, involves the acquisition of or merger with other firm(s). In the global economy, some firms operate tightly integrated partnership; while others have become their own global enterprises through mergers and acquisitions (Mcshane and Von Glinow, 2001).

Mergers and acquisitions thus represent one set of the many adjustment and expansion responses. This form of corporate growth produces relatively rapid expansion. For various reasons it is more visible, attracts a lot of attention and is more stimulating to investors, analysts and other interested parties, than internal growth. The media give considerable coverage to big merger and acquisition deals.

Mergers and acquisitions are forms of business combination, which involve events or transactions in which two or more businesses pool their resources to form a single entity. According to Hoyle et al (2001), the business community is clearly moving rapidly towards business combination as a strategy for growth and competitiveness. They posit that a merger is fundamentally a business combination involving two or more formerly independent and roughly equal firms on roughly equal terms under the joint ownership of the previous separate owners. Weston and Copeland (1989) consider a merger as any transaction that forms one economic unit from two or

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more previous ones. However, Van Horne (1998) considers a merger as a combination of two corporations in which only one survives.

An acquisition, on the other hand, occurs when one entity purchases another entity, with ownership of the combined entity remaining with owners of the purchaser. In this study however, the definition by Brealey, Myers and Marcus (2001) is adopted for both mergers and acquisitions and these two terms are used interchangeably throughout the work. They define a merger as the complete absorption of one company by another, where the acquiring firm retains its identity and the acquired firm ceases to exist. According to them the terminology of mergers and acquisitions are used loosely to refer to any kind of corporate combination or takeover. This is the basis of the decision to use these terms interchangeably in this work.

Firms merge to fulfill certain objectives, the over-riding goal being maximization of shareholders' wealth. As with any other business activity, mergers and acquisitions can be part of management's overall strategy to maximize shareholder value (Hoyle et al 2001). More specific merger motives may include synergy, tax consideration, growth or diversification, use of surplus funds, fund raising, increased managerial skill or technology, elimination of inefficiency, increased ownership, liquidity and defence against takeovers. Sometimes the underlining (hidden) motive is potential gains to management or other third parties, other than to owners. In some situations, a merger or an acquisition can be viewed as an essential phase in a firm's strategy of creating rapid growth. In other situations it can be a necessary prelude to rationalizing investments and reducing over capacity in the industry in the long run (Brealy and Myers, 2000). A merger or an acquisition may

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have a positive or negative effect depending on the reasons for undertaking it and how it is implemented.

In the Western economically advanced countries, corporate growth and restructuring through mergers and acquisitions have long been part of the business environment. According to "Mergerstart" (January 2001), the number of Mergers and Acquisitions in 2000 total 9602 with a total market value of $1.4trillion (as reported in Hoyle et al, 2001). However, in Ghana mergers and acquisitions have been rather unpopular due to her unique entrepreneurial culture and her business and political environment. Ghanaian business people prefer to work for themselves. Many Ghanaian companies are controlled by their founders or families who are usually the top largest shareholders and the top management. Besides, political and economic instability, in the past, hindered the growth of businesses in Ghana.

However since the last two decades, as Ghana embark on political democracy, economic liberalization and financial deregulation, corporate Ghana has come to face more intense competition and now seeks mergers and acquisitions as alternative strategy to internal growth. Hence there have been more frequent occurrences of merger and acquisition activities in Ghana in recent times. Recent mergers and acquisitions in Ghana include the mergers of La Palm Royal Beach Hotel, Berjaya Elmina Beach Hotel and Busua Beach Resort to form Golden Beach Hotels, National Savings and Credit Bank Limited and Social Security Bank Limited and subsequently the merged Social Security Bank Limited and Banc Societé Genérel to form S.G.- SSB Limited. Mobil Oil and Total oil also merged while Kumasi Brewery Limited and Ghana Brewery Limited merged and adopted the name Ghana Breweries

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Limited. The merged Ghana Breweries Limited subsequently merged with Guinness Ghana Limited to form Guinness Ghana Breweries Limited. The largest of the mergers, which attracted a great deal of publicity, was between Ashanti Gold Fields Company Limited and Anglo Gold South Africa Limited to form AngloGold Ashanti Limited. Prior to this merger, Ashanti Goldfields Limited had acquired a number of companies in Ghana and other African countries. Other recent acquisitions in Ghana include the Scancom Areeba deal, Areeba and MTN deal and the acquisition of Benso Oil Palm Plantation by Unilever Ghana Limited. However, inspite of this new trend, mergers and acquisitions are not well understood in Ghana, because they are relatively new in the country.

The study therefore attempts a review of the financial consequences of mergers and acquisitions in Ghana using Guinness Ghana Brewery Limited (GGBL) as a case study. It assesses the impact of the merger on the acquiring company's (GGL's) corporate financial performance and reveals whether the merger resulted in a better corporate financial performance or not. GGBL has being selected because it is listed in the Ghana stock exchange and the relevant data are available for the analysis. Also, it is a member of "Ghana club 100" (topmost one hundred companies in the country) and therefore a major player in the Ghanaian economy.

Problem statement

Mergers and acquisitions are relatively new but fast growing phenomenon in the Ghanaian economy. However, how mergers and acquisitions are done and what their effect is on corporate financial

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performance is not well understood in this country. In the western developed countries, especially the U.S and U.K., several researches have shown conflicting conclusions about the effects of mergers and acquisitions on corporate financial performance. Some of these studies include the works of Agrawal, Jaffe and Mandelker (1992) in U.S. and Limmack (1991) and Higson and Elliot (1993) in the U.K. However, these studies were done in environments that are quite different from that of Ghana.

So the question to answer is; what is the impact of mergers and acquisitions on corporate financial performance within the Ghanaian economy? Taking GGBL as case study, this study seeks to provide answers to this question using performance measures (accounting ratios) based on annual reports of the company. The study focuses on the long-run financial performance of the acquiring firm (Guinness Ghana Limited) after the merger. In accordance with the definition of mergers and acquisitions adopted in this work, GGL is considered as retaining its identity (as GGBL) while GBL ceases to exist, after the merger. Hence the study relates the trend in financial performance of GGL before the merger to the trend in financial performance of GGBL after the merger.

Objectives of the study

The main aim of this study is to assess the impact of mergers and acquisitions on the acquiring firm's corporate financial performance, as explained earlier. The specific objectives are to:

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Compute and compare accounting ratios (profitability, operational cost and sales growth among others) in the pre- and post-merger periods using the annual reports of the company for 2007.

Analyse and discuss the computed ratios to arrive at conclusions on the impact of the merger on corporate financial performance of the company and make appropriate recommendations for improvement.

Significance of the study

Mergers and acquisitions are very important events in corporate finance, both for the firm and the economy. Many research findings have shown that mergers and acquisitions provide benefits to the company and other stakeholders. However, a lot of businesses in Ghana are not fully aware of these huge benefits.

By highlighting the impact of mergers and acquisitions on the corporate financial performance of Guinness Ghana Breweries Limited, interested parties such as shareholders, investors, workers, speculators, analysts and the company itself may find this study useful. The University of Cape Coast may make the findings available to the public through the university library among other avenues. Shareholders and investors are normally interested in returns on their investment, which is achieved through capital gain and dividends payout. The analysis in the study will therefore provide a basis for them to make informed decisions. Additionally, the study will augment other research works on Mergers and Acquisitions and thus contribute to knowledge on the topic of Mergers and Acquisitions.

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Structure of the study

The study is divided into five chapters. Chapter one is the Introduction to the study. This covers the background information, problem statement, objectives and significance of the study. Chapter two covers a review of existing literature on Mergers and Acquisitions and evidence from previous studies. Chapter three is the study Methodology. It covers the background of the firm and the study design which comprises of the selection of company of study, data collection, and data analysis techniques. In chapter four, data on the acquiring company's financial performance, as obtained, are analysed and discussed. The summaries, conclusions and recommendations from the study constitute chapter five.

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CHAPTER TWO

LITERATURE REVIEW

Introduction

Business combinations involve events or transactions in which two or more businesses pool their resources to form a single entity. They occur in various forms including mergers and acquisitions. This chapter provides Literature on Mergers and Acquisitions.

Definitions

Mergers and acquisitions have been variously defined. In the view of Hunt et al. (1966), a merger is the combination of two or more formerly independent firms in which the acquiring firm takes over the assets of the target (acquired) and the acquired firm ceases to exist as a separate entity. Other terms such as consolidation, amalgamation and acquisition are used in a similar context and the lines of distinction are often unclear. Van Horne (1998) regards a merger as a combination of two corporations in which only one survives. According to Hoyle et al (2001), a merger is a business combination involving two or more formerly independent and roughly equal firms on roughly equal terms under the joint ownership of the previous separate owners. Thus, basically, a merger is said to have taken place when two or more companies come together, the shareholders of both companies

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continue to have interest in the combined entity and no material resources leave the combined company because of the combination. Obviously, when this happens the two companies surrender their separate identities and a new company is formed.

In Ghana, the Companies Code, 1963 (Act 179) Section 229(b) explains a merger as follows:

> "the expression 'amalgamation' means any merger of the undertakings or any part of the undertakings of two or more companies or of the undertakings or part of the undertakings of one or more companies and one or more bodies corporate".

This means a merger occurs when one firm buys or absorbs one or more other firm(s) and the acquired firm(s) thereby ceases to exist independently. The buying or acquiring firm may not change the name and operations of the acquired firm.

Thus in reality, there is ultimately an acquirer (victor) and an acquired (victim) in almost every merger. Management of the acquirer assumes more control over the direction and operations of the merged firm. Thus Brealey et al (2001) consider a merger as the complete absorption of one company by another, where the acquiring firm retains its identity and the acquired firm ceases to exist.

Many distinctions do exist between types of mergers and other business combinations. These distinctions can be of profound importance for legal, accounting and tax purposes. For instance, different accounting and tax treatments are permitted under the different situations (Sally and Rhoades-

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Catanach, 2002). Thus sometimes, attempts are made to differentiate between forms of mergers and acquisitions/takeovers.

A consolidation is a merger in which an entirely new firm is created and both the acquired and acquiring firms cease to exist. An acquisition on the other hand is a combination in which one entity purchases another entity and ownership of the combined entity remains with owners of the purchaser. Invariably, the acquired becomes a division of the acquirer. Sometimes the acquired is maintained as a subsidiary for a while, before the ultimate merger is consummated. An acquisition may be by either stocks or assets. According to Hoyle et al (2001), in a takeover one company buys all the shares of another company, maintains its own identity but brings to an end the separate identity of the purchased company. They assert that, however in reality the majority of situations do not fall into these clear-cut categories.

From the definitions and discussions above, it is clear that in any merger or acquisition, one economic unit is formed from two or more previously independent economic units and that one of the previous economic units survives and absorbs or takes over the assets of the other unit(s), which then cease(s) to exist. Hence, the definition for mergers and acquisitions by Brealey et al (2001) was adopted for the purpose of this work.

Classification of mergers

Mergers and acquisitions are usually classified into horizontal, vertical or conglomerate (Ross et al, 1999).

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Horizontal Mergers

These are mergers where both the target and acquiring firms are operating in the same line of business. Thus the merger is between competitors in the same industry. As a result of such a merger, top management of the acquired firm is likely to be replaced by a new management team (Brealey and Myers, 2000). The case under study was an example of horizontal mergers. Other horizontal mergers in Ghana within the last two decades include those of Ashanti Goldfields Limited and AngloGold S.A. Limited to form AngloGold Ashanti Limited (Annual Reports of AngloGold Ashanti Limited for 2004) and Ghana Brewery Limited (formerly ABC Limited) with Kumasi Brewery Limited (Annual Reports of Ghana Brewery Limited for 1998).

The advantages in horizontal mergers include economies of scale in purchasing and distribution, utilization of excess capacity and the sharing of skills and expertise. Achieving economies of scale is the natural goal of horizontal mergers (Brealey and Myers, 2000). They may however result in monopolies, which anti-trust laws and agencies fight against.

However, many mergers that seems to make such economic sense fail because managers cannot handle the complex task of integrating two firms with different production processes, accounting methods and corporate cultures (Keller J. J., 1995) and (Hirt and Block, 1999).

Vertical Mergers

These are mergers between companies specializing in different parts of a given production chain, which thereby consolidate into one firm. The target company is either a supplier of goods (materials) or a consumer of products of

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the acquirer. Vertical mergers seek economies in vertical integration (Brealey et al, 2001). An example is a cement distributing company merging with a blocks manufacturing company. The acquisition of Benso Oil Palm Plantation by Unilever Ghana Limited was an example in this regard.

A key advantage is that the production chain is brought under control by the combined firm so that, for instance, the producer is assured of constant supply of the raw materials and the supplier is also assured of ready market. Additionally there is reduction in costs of transactions including communication and negotiations costs, due to what is often termed the "internalization of operations". The disadvantage is that an unanticipated problem at any level, for example the supply (raw material) level, is likely to run through the other levels (Brealey and Myers, 2000). Failure to effectively integrate the operations and human assets of the two firms may hinder attainment of expected goal (Mark M., 1995).

Conglomerate Mergers

These are the merging of firms from unrelated industries or businesses. For example, a retail chain company merging with a mining company. Here, no operating economies are achieved, rather a portfolio of companies is held so that the total post-merger value should be at least equal to the sum of pre-merger values. However, in reality the post merger value is usually less than or at most equal to the sum of the pre- merger values. This is due to difficulties associated with meshing the different cultures and co-ordinating operations of the previous companies as well as the merger costs (Brealey and Myers, 2000) and (Hirt and Block, 1999). The case of Kaiser Industries, prior

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to its dissolution (as reported in Brealey and Myers, 2000) buttresses this view.

An argument in favour of conglomerate mergers is that they are less risky due to diversification. This is considered fallacious because investors can diversify their investment by simply buying shares of each of the companies and holding them as part of their portfolio (Brealey and Myers, 2000).

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Reasons for mergers (mergers versus internal growth)

In evaluating the reason for a merger, it is necessary to critically consider whether the particular reason given is consistent with the existence of an economic gain from the merger. In other words, the question is whether the merger is value enhancing so that the two firms are worth more together than apart. According to Brealey et al (2001) the question also needs to be considered whether the individual firms could not have embarked upon respective internal growth activities instead of external growth.

An explanation of the motivations for mergers and acquisitions will be helpful for the understanding and evaluation of the reasons for the merger under study, which is done in chapter four. Harpern (1983) identifies two classes of merger motivation theories. These are the non-value maximizing and value maximizing motivation theories.

Non Value Maximization Theory

This refers to non-value maximizing behavior of management of acquiring firms and third parties to mergers. Here, mergers are aimed at maximizing growth in sales or assets or at controlling 'large empires'. Third

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parties often lure management into merger activity because of perceived potential gains to the third parties, not necessarily to shareholders (Peter Dodd, 1980).

Mergers of this type have no economic gains, to be divided among the firms. In other words, the post merger value does not exceed the sum of the pre-merger values of the merging firms. Rather, there is likely to be an overall economic loss, given the potential managerial difficulties of coordinating activities of the expanding corporate empire and other reasons explained earlier, under conglomerate mergers. The cost of a merger is the premium paid by the acquirer, over and above the price of the target, as an inducement to the target's shareholders to sell their shares (Hirt and Block, 1999). This means that any gains obtained by the target's shareholders would be offset by a loss to shareholders of the acquiring firm.

The non-value maximizing behaviors are more likely to occur in acquiring firms that are engaged in conglomerate mergers and have active acquisition programmes (Brealey and Myers, 2000). These motives are classified under the two broad categories of managerial and third party motives.

Management's Personal Agenda (Agency Problem)

These are mergers undertaken because management of the acquiring firms pursues their own interest and not necessarily shareholders' interest of maximizing corporate wealth. Managerial motives include corporate empire building, the use of free cash flows, defense against takeover, diversification to reduce risk (as means of protecting jobs), increased liquidity and hubris.

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Sometimes Management's motivation is to build a corporate empire, for the sake of the power, status, prestige, higher remunerations and pensions and other perquisites (like luxurious offices, company cars, membership in clubs) that go with holding management (top) position in a huge company or with increase responsibilities. Sometimes it is just to satisfy management's ego and feeling of success and importance. In some cases, the motive of management is to use free cash flows for corporate expansion, rather than return it to shareholders (Jensen M.C., 1986 and 1989).

In other cases, the merger is a survival strategy, to protect the company from becoming a target for acquisition. It has been noticed by both casual observers and empiricists that mergers tend to take place between a larger acquirer and a smaller target (Brealey and Myers, 2000). Management of a potential target firm may therefore come to believe that the best way to protect their jobs and positions (to avoid being acquired and then replaced or dominated) is to grow their company and to do so quickly by external expansion. Defence strategies also include diversification to spread risk, and reverse acquisition whereby a potential target firm rather takes the lead to initiates action to acquire the potential acquirer. In any of these situations the acquiring company frequently overpays.

The hubris hypothesis for merger activities, spelt out by Richard Roll in 1986, is a managerial motive for mergers. It refers to mergers motivated by over confidence of management of acquiring firms in their own capabilities. This attitude sometimes amount to arrogance. As a result of their over wearing self-confidence and zeal to exhibit their 'superior managerial capabilities',

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such management frequently err, without realizing their errors, in assessing the efficiency of the management or future cash flows of the target firm.

Another non value maximizing motive for merger is often to increase liquidity. Owners of a tightly held company may have too much of their wealth tied up in the company. By merging with a publicly held company they can achieve higher liquidity of their stock, which enables them to sell some and diversify their investments.

In a modern corporation, ownership resides with shareholders while the running of the business is in the hands of management. Thus shareholders and management are in an agency relationship in which management is an "agent" of shareholders (the principal). An agent (the management) has fiduciary responsibility to act in the utmost interest of the principal (the stockholders), which in this case is the maximization of the company's wealth. However, in all such relationships, there is a possibility of conflict of interest between the principal and the agent. This is called an agency problem (Ross et al, 2001). Whenever management pursues its own interests at stockholders' expense, agency cost accrues to stockholders. Apart from stockholders and creditors there are other groups, stake holders, who potentially have claims on the firm's cash flows and therefore have interest in its decisions. They include employees (labour unions), customers, suppliers and government's tax and regulatory agencies. Such groups may also attempt to exert control over the firm, by pressuring management to act in their interest, perhaps to the detriment of the owners (Catherine, 2003).

Managerial behavior against shareholders' interest (agency problem) is thus a consequence of the separation between ownership and management. It

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happens also because the costs of monitoring management's activities, of writing and enforcing contracts to avoid principal-agent problems are very high. Brealey et al (2001) posits that no one shareholder would bear these costs given that the benefits would accrue to all shareholders, unless that shareholder holds a substantial proportion of the stocks. The recent Emergency General Meeting (EGM) of Cal Merchant Bank Limited, in Ghana buttresses this point. The EGM was sponsored by the largest individual shareholder (owning11% of the company's stocks) for shareholders to vote on resolutions concerning recapitalization of the bank, appointments of board members and dismissal of the chief executive officer. Whether management acts in the best interest of shareholders depends on:

- how closely management's interests are aligned to shareholders interests. This concerns management compensation and
- the ability to replace management if it does not pursue shareholders interest, an issue of the control of the firm.

The way management is compensated is therefore one factor that affects the agency problem. Thus in modern times, measures adopted to avoid the agency problem, particularly by large companies in which it is more pronounced, include creating and tying management's incentive compensation to corporate financial performance, often directly to share value (Ross et al, 2001). Such compensation packages include share options and bonuses. They provide economic incentives to management to increase share value. Another economic incentive to management is job prospect, both within the firm (promotion) and in the general labour market. Either of them means higher

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salaries for better performers. Managers who are successful in pursuing shareholders' interest can reap enormous rewards for themselves. For example, Stephen Case, CEO of America online, received $120milion in 1999, Oprah Winfrey got $150milion and Margaret Whitman of on-line auctioneer eBay received a total pay package (including the value of stock option and other items) of $1bilion as at March 2000 (as reported in Ross et al, 2001).

Control ultimately rests with shareholders. In smaller firms this is quite clear, because ownership and management are either the same or loosely separated. Even in large corporations where ownership can spread over a huge number of stockholders, arguably meaning that management effectively controls the firm; ultimate control still rests with shareholders. For instance unhappy shareholders can use the proxy fight mechanism to replace the board and management (Brealey et al, 2001), (Peter and Jerrold, 1985) and (Ross et al, 2001). Another way management can be replaced is by takeover. Firms that are poorly managed are more attractive as acquisition targets than well managed firms because a greater profit potential exist (Healy P., 1992). This means that market forces also influence managerial behaviour. Thus the treat of acquisition by another firm and consequence replacement or domination (Martin and McConnell, 1991) also provides management an incentive to act in stock holders' interest. The requirements of Ghana's company's code (Act 179, 1963) for an independent audit of the annual financial statements of public companies and for the full statements to be sent to shareholders, among other regulations also provides some incentives for management to act in shareholders interest (Catherine G., 2003).

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Third Party Motives

Third parties include professional advisers and intermediaries such as financial analysts, accountants, lawyers, financial journalists, investment bankers and stockbrokers and also creditors, customers and suppliers. Advisers gain in every merger event, through their fees, and the amount involved is sometimes enormous. For example the $25billion takeover of RJR Nabisco by KKR in 1988, the largest takeover in history then, "generated almost $1billion in fees for the banks and advisers", (reported by Brealey et al, 2001). Because of what they stand to gain themselves, bankers and other professional advisers sometimes lure their clients into merger transaction. Powerful customers, suppliers and creditors can also pressurize their clients or suppliers to merge with another company, in which they have interest.

Value Maximization Theory

This class of merger theories refers to the value maximization motivations by which a merger should meet the same criteria as any other investment decision. That is, there should be a positive expected economic gain from the merger. Mergers motives that are consistent with the goal of value maximization are classified into two groups: synergy and bargain buying. Synergic gains result from: increased market power, tax benefits, risk diversification, economies of scale, economies of scope, internalization of transactions, entry into new markets, ustiliation of excess capacity, information asymmetry, corporate control and monopoly (Brealey and Myers, 2000) and (Herzel and Shepro, 1990). Bargain buying on the other hand, is

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concerned with undervalued stocks of the target firm, the elimination of inefficient managements, and use of more efficient management.

Harperm (1983) also identifies financial motivations as another class of motives for mergers that are also consistent with the value maximization theory. These motives are the redeployment of excess cash and diversification. Explanations of these value-maximizing motivations are provided in the following paragraphs.

Financial Motivations

Redeployment of Excess Cash: The argument presented under financial motivations is that a merger permits redeployment of excess cash held by either the acquirer or the target. Quite often, a company seeking access to funds may identify another company with excess liquidity (high liquid assets and low levels of current liabilities) as a merger partner. Merger with such a cash-rich company immediately increases the firm's borrowing power by decreasing its financial leverage (debt/equity ratio). However, sometimes it may be difficult to justify paying a premium to merge while the capital spent could provide funds at lower transaction costs (Brealey and Myers, 2000).

Diversification: Another argument regarding financial motivation is that the diversification benefits provided by a merger, particularly a conglomerate merger, can reduce the probability of default and thereby reduce expected bankruptcy cost, increase the debt capacity and reduce the cost of borrowing of the new entity.

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Synergy

This refers to a set of economic motivations in which the merger brings synergic benefits, making the combined entity to have a value that is greater than the sum of its parts. The synergic effects lead to increase in the expected cash flows in the combined entity over their sum as independent firms. Weston and Copeland (1989) identify three forms of synergy. These are operational synergy, financial synergy and strategic alignment to changing environment.

According to them, during the heydays of the conglomerate merger activities, in the late 1910s, exaggerated claims were made for synergy which came to be termed as the “2+2=5” effect. However while the claims for synergy achieved through asset deployment were exaggerated, there is a basis for achieving positive net present value investments by combining the operational activities of businesses (Healy et al, 1992).

Operating synergy: Operating synergy or operating economies may be involved in horizontal and vertical mergers. For horizontal mergers, the source of operating economies must represent some form of economies of scale. These economies, in turn, may reflect indivisibilities and better utilization of capacity after the merger. It may also come from organizational capabilities on the part of management that result in gains, which are not attainable from internal investments in the short run.

Synergistic benefits are realized in vertical integration, when firms at different stages of an industry achieve more efficient co-ordination of the different levels. The argument here is that the costs of communication, various forms of bargaining, negotiation, and opportunistic behaviour can be avoided

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by vertical integration. This is often termed as the internalization of transactions (Brealey and Myers, 2000).

Economies of scope may be achieved, in a conglomerate merger, through cost advantages or when output is increased by the post-merger entity not in one product but in vector products (Weston and Copeland, 1989).

Financial Synergy: Financial synergies arise when the cost of capital is lowered. If the cash flow streams of the combining companies are not perfectly correlated, bankruptcy probabilities may be lowered; and the result may be the same as with diversification, explained above (Weston and Copeland, 1989) and (Brealey and Myers, 2000).

Strategic Realignment to Changing Environments: The strategic planning approach to mergers appears to imply either the possibilities of economies of scale or utilization of some unused capacity in the current managerial or technological capabilities of one of the firms. The merger under study was expected to utilized the excess (under utilised) capacity of GBL. Another rationale is that by external growth, the firm acquires or is better able to attract needed management skills to augment its present capabilities (Weston and Copeland, 1989), (Brealey and Myers, 2000) and (Rose and Marquis, 2006).

In effect, the contention is that the combined firm can constitute a wider technological, managerial, marketing and financial base, which increases the potential for growth and profits (Brealey and Myers, 2000). It makes possible greater utilization of each firm's relative advantage. The other synergic motives for mergers are explained in the following paragraphs.

Increased Market Power: Merging with a company in the same industry may increase the market power of the combined company. This was one of the

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objectives of the GGBL merger. The increase in market power may enable the acquiring company to earn monopoly profits, provided there are significant barriers to entry into the industry. In 2000 Unilever PLC, the consumer product giant, made two acquisitions, both aimed at increasing its presence in the U.S. market. First, it acquired SlimFast Foods, Inc., a maker of diet products, which at the time commanded roughly 45% share of the U.S. market. Secondly, it acquired Ben & Jerry's Homemade, Inc., an ice cream chain (as reported by Ross et al, 2001).

However, Governments frequently legislate to prevent mergers that are considered likely to result in an excessive level of concentration in an industry or in monopoly, except mergers that are considered to be in the public interest.

Entry into New Market or Industry: Mergers are often a means of entry into a new market or industry. Sometimes the quickest way for a firm to establish itself in a new product or geographic market is to merge with an established player in that market. This approach eliminates the need to first develop the required technical knowhow and skills. It avoids the dangers of failure associated with the growth period of internal expansion, which is a common phenomenon. Additionally the price wars that frequently follow the entrance of a new competitor into a market are avoided. The merger of Banc Societé Genérel with Social Security Bank Limited to form S.G. - SSB was an example of market entry type of merger.

Tax Benefits: When a company merges with another company with accumulated losses, it can lead to a reduction in total tax payable by the combined entity. A firm with cumulative tax losses may have little prospect of earning enough in the future to utilize fully its tax-loss carry-forward, where

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this applies. By merging with a profitable company, it may be possible for the surviving company to utilize the carry-forward losses more effectively. However, there are restrictions limiting its utilization to a percentage of the fair value of the acquired company (Brealey and Myers, 2000) and (Jones and Catanach, 2002).

Nevertheless, Van Horne (1989) believes that even with these restrictions, there can still be an economic gain, at the expense of the government, that cannot be realized by either company separately. Another tax benefit is postponement of tax payment on merger proceeds, where the target's shares are paid for with the acquirer's shares (Sally and Catanach, 2002).

Diversification: Diversification is considered a synergic motive in line with portfolio theory where a company may merge with another one, in a different line of business, in order to reduce cyclical earnings instability. To the extent that investors are averse to risk and are concerned only with the total risk of a company, a reduction in a company's earnings instability would impact favourably on its share price.

Increase in Earnings per Share and Price Earnings Ratio Effects: Corporate financial objectives are often expressed in terms of growth in earnings per share (EPS) or price earnings ratio (P/E ratio). This may lead a company to evaluate the effect of a proposed merger on its EPS or P/E ratio. However Pierson et al (1990), argue that this approach is unreliable. They posit that although an economically viable merger should lead to an increased EPS for the acquiring firm, it is possible to design a merger which produces no economic benefits but nevertheless produces an immediate increase in EPS. This is often referred to as the "bootstrap effect" (Myers, 1976).

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Asymmetry Information: Management of the acquiring firm attempts to take advantage of information asymmetry. The information hypothesis postulates that the acquirer has information concerning the target firm that is not available to other participants in the stocks market and which does not reflect in the current share price of the target company. The information may be that the target shares are undervalued based on publicly available information or that there are more efficient operating strategies that could be used by the target's management and if the existing management knew these strategies, they could become more efficient and the stock price would increase (Nickolao Travos, 1987) and (Franks et al, 1991).

However, this information asymmetry should not be possible in an ideal strong form efficient capital market. Even in a weak or semi - strong form of efficient capital market, the announcement of a merger bid should be a signal to the market place and the asymmetry in information should be ameliorated. Besides, the rise in target's share price around the announcement date of a merger bid, (as competition for the target's stocks intensifies) may reach a level where the acquirer attains little or no gain, or even incurs loses (Hirt and Block, 1999).

Corporate Control: This is an attempt by the acquirer to obtain control of the target. The corporate control motive is linked closely to that of information asymmetry. In its most general form, the acquirer desires control of the target company to replace an incompetent management or to force existing management to follow a profit maximizing strategy. Under either case, shareholders of the target are expected to be earning below normal returns in some period preceding the merger (Brealey et al, 2001).

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The corporate control hypothesis, developed by Berle and Means (1932), postulates that managers, who control the firm (subject to general oversight by the board of directors) make decisions that do not maximize the market value of equity for shareholders. The value of a firm reflects a valuation by investors, taking into account the value of perquisites consumed by managers, agents of the shareholders (Jensen and Meckling, 1976). Under the hypothesis, a merger is facilitated by depressed stock price of the target firm and the acquirer is expected to gain through subsequent capital gains.

Bargain Buying: This has the same basis as corporate control. The acquiring firm perceives stocks of the target to be under priced or believes that the target can be bought at a price below the present value of its future cash flows under different management. This perception may be based on information and signaling or inefficient management of target (Brealey et al, 2001).

Information and Signaling: The idea is that the merger event provides information on underlying profitability that otherwise cannot be convincingly conveyed. It is generally asserted that value can occur if new information is conveyed to the market via the merger negotiations. A positive signal may occur via the merger announcement so long as a stock is believed to be undervalued, which then causes share price to rise (Hirt and Block, 1999).

The Target Company is Managed Inefficiently: Management of the acquiring company may identify an opportunity to use the target company's resources more efficiently. More efficient use of the resources may lead to an increase in the value of the target firm. Shareholders of the target are expected to be earning below normal returns in some period leading to the merger (Lichtenberg and Siegel, 1989) and (Martin and McConnell, 1991).

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Justification of mergers

According to financial theory of business combinations, a merger would be justified if: $PVxy = PVx + PVy + Gain$

Where: PVx = present value of firm X

PVy = present value of firm y and

$PVxy$ = present value of the combined firm, XY

Thus the present value of firm XY (PVxy) as a combination of firms X and Y should be greater than the sum of the present values of companies X and Y working independently. In the formula above, the Gain is the difference between the present value of the combined company (XY) and the sum of the present values of the individual companies (X and Y), working separately. Thus: $Gain = PVxy - (PVx + PVy)$

(Adopted from: Brealey and Myers, 2000)

Who gains in a merger?

The conclusion from the previous section is that there should be a potential gain in an economically justifiable merger. Many researchers have addressed the question of 'who benefits from the gain?' Samuel and Wilkes (1986) identify the following interested parties who could either gain or lose:

The Economy –A Social Gain

Although some mergers will result in some social gains, such as improved quality and or lower prices of products to the society, those benefits to society will to a larger extent depend upon whether a monopoly is created or not. If a monopoly is created and it exploits society, then the economy may

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lose. On a balanced scale, if a lower level of efficiency gains is realized relative to what could be expected, and potential social costs are generated by increased market power and absence of other benefits, then the argument may be against the merger (Samuel and Wilkes, 1986).

In 1969 The Monopolies Commission of the United Kingdom concluded that based on evidence they had seen, the effect of mergers on the economy was at best neutral. A study by Hong et al (from1954 to 1964) also concluded that on a balance it is very unlikely that the reshuffling of economic resources, which takes place as a result of a merger, leads to more profitable utilization of these resources. Richard Roll in his Hubris hypothesis (1986) argues that takeover gains may have been overestimated if they existed at all. The weight of evidence indicates that overall, the merger process is at best neutral in terms of its impact on the economy.

Shareholders of the Two Firms

Researches in both the U.S and U.K. have shown that shareholders of the target firms do gain from successful merger bids. They earn significantly from all mergers (Hirt and Block, 1999). This is not surprising given that target firms' shareholders require a premium to induce them to sell their shares. Often times increased demand by market participants, particularly speculators, for the target's shares following merger bid announcement, and inside trading prior to the merger bid announcement date push up share price of the merger candidate. Most important is the competition among bidders and the defense activities by management of the target. Brealey and Myers (2000)

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contend that every time one suitor tops another suitor's bid, more of the merger gains slides towards the target.

Several studies in the U.S., which have been summarized by Jensen and Ruback (1983), show that on the average, above normal percentage share price gains of 30% are realized by target shareholders in a successful merger bid, whereas the gains to the bidding company shareholders are only 4%. Around the date of announcement of a tender, the target firms' shares price increase from 6 percent to 30 percent. A study by Oppenheimer and Block (1980) indicates that an average premium paid in recent time period was approximately 60 percent, and that there was an associated upwards price movement of similar magnitude

In general, acquiring firms' shareholders earn little or no abnormal returns from tender offers. Jarrell and Poulsen (1989) report that the announcement returns to acquiring firms dropped from a statistically significant five percent to an insignificant one percent loss in the 1880s. However, according to Weston and Copeland (1989), whether or not the shareholders of acquiring companies gain depends in part on the intensity of competition in the market for mergers and in part on the market's view of what will be achieved by the combined companies.

The evidence of gains or losses is usually based on returns computed over a pre-merger period starting immediately before the announcement date and ending on or before the effective date of merger. This assumes that prices will adjust to the likely efficiency gains from the mergers.

Some studies also examine the assumption of market efficiency by measuring abnormal returns after the effective date of the merger. These

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studies give mixed findings. Frank, Harris, and Titman (1991) find no evidence of significant abnormal returns over a three-year period after the last bid date. However, Agrawal, Jaffe, and Mandelker (1992) find that merger tender offers are followed by insignificant abnormal returns to acquirers, whereas the mergers are followed by significant abnormal returns of negative ten percent (-10%) over a five-year period after the effective merger date.

Management of the Acquiring Firm

Generally, the management of an acquiring company gains from a successful merger policy. They receive increased status, prestige and power from running a larger business. There is evidence that at the same time they receive increased financial rewards. There are thus financial and other incentives to the managers, who have little or no ownership interest in a company, to pursue growth at the expense of profitability. This explains the desire of managers to merge rather than increase efficiency (Meeks, 1981).

Management of the Target Firm

The general impression is that management of the acquired company loses. They are frequently replaced, because either they are judged to be inefficient, or they resisted the merger thereby raising the cost of the acquirer substantially (Martin and Mc Connell, 1991). Although this is the general view, there have however been instances where top executives of large firms attained their positions as results of been managers of acquired firms.

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Employees

In many instances, a number of the employees of the acquired firm lose. After the merger certain parts of the acquired firm might well be closed down, resulting in redundancies (Brealey et al, 2001). Sometimes assurances are given during the negotiations that there will not be redundancies. However, if the situation is reviewed after the excitement of the battle is over, it will often be found that despite the assurances, redundancies have being carried out. In fact, in many cases, it is employees of the target firm who are anxious to fight the merger bid, as they realize that they stand to lose much.

Nevertheless, it must be appreciated that in order for a merger to be a financial success it may be necessary to create redundancies, as a result of the ensuing restructuring. Often, the acquired company had more employees than was necessary, and the resulting inefficiency contributed to make it an acquisition target. Besides, there may be duplication of functions and processes among the combined businesses (Brealey and Myers 2000).

Financial Institutions and Professional Advisers (Third Parties)

Financial institutions and professional advisers are groups that certainly benefit from mergers. They are the merchant bankers, financial analysts, lawyers, stockbrokers, public relation firms, financial press and all other institutions and professionals, outside the merging companies, that are involved in the merger negotiations and resulting battles. They are used by both the bidding and the target firms. Their expertise is critical and there is no hope of being successful either in bidding or in defending without good advice from them (Brealey and Myers 2000).

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Whatever the case their fees must be paid by the merging companies, whether or not their advice leads to success and the costs involve are often considerable (Myers S.C., 1976). In every merger battle one group of advisors wins and another group loses. One banker might be advising an acquiring firm in one merger battle and at the same time advising a target firm in another battle. They all win some and lose others.

Generally therefore, it has been identified that three groups gain from successful mergers and two groups lose. The winners are the acquirer's management, victim's shareholders, and third parties. Management and employees of the acquired firm are the losers. The position of society and the bidding company's shareholders on the balance seems to be neutral. They win in some mergers and lose in others. These are, of course, generalizations but they do indicate the complexity of the motives involved in mergers (Brealey and Myers, 2000).

The procedures of mergers

A Merger may be initiated by either of the parties to the merger or by a third party, such as an investment-banking firm, which recognizes in the merger some direct or indirect advantage to itself. Negotiations may be conducted between the top managements of the companies concerned, as was the case in the Ghana Breweries Limited merger, or directly with owners of the target. Sometimes, management of the target firm is deliberately by passed, where it is expected to be antagonistic to the merger proposal (Brealey and Myers, 2000). Where the target is a listed company, the acquiring company may choose to make a public offer to buy all or a good percentage of

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the target's stock, usually at a price that is above the prevailing market price. The higher offer price is meant to induce the shareholders to sell their shares. Where an outright merger is not achieved the aim may be to gradually establish a parent subsidiary relationship and then proceed to achieve ultimate merger. The legal procedures that one firm can use to acquire another firm are either acquisition of the target firm's stock or its assets (Hunt et al, 1966).

However, these often spark unhealthy takeover battles and tactics between the potential acquirer and potential target, as happened between Mesa Petroleum and Cities Service (Ruback, 1983) or between potential acquirers, as happened in RJR Nabisco's acquisition (Burrough and Helyar, 1990). In such situations, the target is mostly over valued and the acquirer losses value after the merger.

Acquiring Target Firm's Stock

The most frequently used procedure for bringing ownership and management together is for one company to acquire ownership of all or substantial proportion of the voting stock of the other. In the initial stages therefore, the target company is likely to retain its identity, and the two companies are in a parent-subsidiary relationship. This relationship may last for a brief period or sometimes for years before actual merger takes place (Brealey and Myers, 2000) and (Jensen and Ruback, 1983).

Where the acquiring company gains less than100 percent ownership in the initial transaction, it may find it necessary or desirable to increase its ownership level before initiating merger proceedings. Even where the acquirer/parent has majority shares necessary to vote approval of the merger, it

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may wish to reduce further the minority interest, which will have to be reimbursed in cash at an arbitrated price (Litwin, 1995).

Payment for the voting stock of the target may be made in cash or with shares of the acquirers or other securities or a combination of these. Acquisition of stock by cash may be obtained in a private negotiation between the acquiring company and a single owner or a small group of owners. In the case of a publicly owned company, the stock may be purchased gradually on the open market at the prevailing market price. It may also be purchased through a public offer. This offer may be made with or without the knowledge and blessing of the management of the target company (Brealey and Myers, 2000). Payment by cash will require payment of tax on any capital gains realized as a result of the merger (Sally. and Rhoades-Catanach)

Under acquisition by Shares the acquiring company offers its own stock in exchange at a ratio, usually expected to be attractive to the target's shareholders. This way shareholders of the acquired firm become shareholders of the surviving company, together with the acquirer's shareholders. Apart from the possible advantages of the exchange itself, there may be considerable attraction in becoming part of a larger and more diversified company (Brealey and Myers, 2000). In addition, tax payment on any capital gains is postponed when acquisition is by shares. Postponement of tax payment may be a positive attraction in the long term, but the prospect of being a member of a larger and more diversified firm may not be positive in the long run. This is because of difficulties in managing larger and diversified firms and the fallacy that risk is reduced in diversified firms, as discussed above.

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Buying of the Target Firm's Assets

The alternative to acquisition of the stock of a going concern is to purchase its assets. This might appear to be a more direct and therefore a more satisfactory procedure for the acquiring company, since the ultimate purpose in acquiring stock is to have the use of these assets. Instead of the shareholders receiving the payment directly, the acquired company receives it and ultimately disburses it to the stockholders as a liquidating dividend when they dissolve the company. The acquiring company is thus relieved of the formal merger proceedings and the costs and problems of minority interests (Nickolasos Travos, 1987).

In practice the purchase-of-stock route often proves to be a quicker and more effective procedure, as evidenced by its use in majority of cases. Where there is an established market price for the stock, the key problem of valuation is greatly simplified. Often, the purchase of stock is a way of by passing antagonistic management, and it may be done with a minimum publicity, through the impersonal medium of the stock market (Brealey et al 2001).

When a company is acquired through the purchase of its stock, the acquiring company indirectly takes on responsibility for its liabilities, as well as its assets, since it assumes ownership. However with a direct purchase of its assets, there is no necessity for the acquiring company to assume the liabilities, although this is often part of the deal, especially where the acquired company is in a weakened financial condition. Otherwise, the target company concerned is simply converting earning assets into cash; it retains responsibility for discharging its own obligations Hong et al (1978).

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Determination of the value of a firm

Analyzing a potential merger target firm involves placing a value on it. There is no company for which a single dollar value exists because the value of a firm depends not only on its cash flows generation capabilities, or value of asserts it owns, but also on its operating and financial characteristics (Petty et al, 1993). Therefore in valuing a target company, a range of values is determined that would be economically justifiable to the prospective acquirer. The final price is then negotiated within this price range, between the two managements.

To determine an acceptable price for a firm several factors are carefully evaluated. However, quantifying the relevant variables for this purpose is difficult at best. For instance, the primary reason for a merger might be to acquire managerial talents, excess capacity or to complement a strong sales staff with an excellent production unit (Brealey and Myers, 2000). The synergistic effects are difficult to measure using historical data of the companies involved. Even so, several quantitative variables are frequently used in an effort to estimate a firm's value (McConnell and Muscarella, 1985). These factors include:

Book Value

The book value of a firm's net worth is the balance sheet amount of the assets less its outstanding liabilities, or its owners' equity. Book value does not measure the market value of a company's net worth because it is based on the historical cost of the firm's assets. Seldom do such costs bear true relationship to the organization's ability to produce earnings.

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Although the book value of an enterprise is not the most important factor, it can be used as a starting point for comparing with other analyses. The book values could provide critical information, especially where plant and equipment are relatively new, (Brealey and Myers, 2000).

Appraisal Value

An appraisal value of a company may be secured from an independent appraisal firm. The techniques used by appraisers vary widely. This method is closely tied to the replacement cost method. The deficiency of this method is that the value of the individual assets may have little relationship to the overall ability of the company to generate earnings, and thus the going concern value of the firm (Mc Connell and Muscarella, 1985).

Stock Market Value

The stock market value, as expressed by stock market quotations is another approach to estimating the net worth of a business. If the stock is listed on a major stock market, and is widely traded, an approximate value can be established on the basis of the market price (McConnell and Muscarella, 1985). The justification is based on the fact that market quotations indicate the consensus of investors on a firm's future cash flows and corresponding risks (Hirt and Block, 1999).

Cash Flow Value

Under this method, valuation of the target requires an estimation of the incremental net cash flows available to the bidding firm. The present value

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of these cash flows will then be determined, and this will be the maximum amount that should be paid for the target (McConnell and Muscarella, 1985).

Terms of mergers

Merger negotiations may break off if it comes out that the companies' operations are incompatible or when the parties are unable to agree on the merger terms. Empirical evidence shows that, a number of potentially attractive combinations fail during negotiations. The question then is on what terms do merger partners negotiate? Weston and Copeland (1989) identify the price to be paid by the acquirer as the most important of merger terms.

Quantitative Factors Affecting Merger Terms

Much emphasis is given to Earnings and Growth Rates, Dividends, Market Values, Net Current Assets Per Share and Book Value Per Share as factors influencing the terms of a merger. An analysis will be based on the per-share values of each of the above factors. However, the relative importance of each factor and the circumstances under which each is likely to be the most influential variable will vary among mergers (Myers, 1976). The natures of these factors are explained in the following paragraphs.

Earnings and Growth Rates: Expected earnings and capitalization rates which are reflected in Price-Earnings (P/E) ratios are important in determining the values that will be established in a merger. The bidder should value the target company by first making an estimate of the future earnings per share (EPS) of the target. The EPS figure is then multiplied by an "appropriate" P/E ratio to obtain an implied price (value) of the target (Myers, 1976).

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Dividends: Dividends do influence the terms of a merge in the sense that dividends represent the actual income received by shareholders. Weston and Copeland (1989) suggest that where a company which does not pay dividends seeks to acquire a firm whose stockholders are accustomed to receiving dividends, the exchange of shares can be on a "convertibles for common stock" basis. This will enable shareholders of the acquired firm to continue receiving income.

Market Values: The current market values are always expected to have a significant influence on the terms of a merger since the price of a firm's stock is a reflection of the expectations about its future earnings (Hirt and Block, 1999). The following reasons could be attributed to a situation where the value placed on a firm exceeds its current market price:-

- The prospective purchaser may be interested in the company for the contribution that it will make to the purchaser's company. Thus the acquiring firm may view the target company as worth more than it is valued by the market (Brealey and Myers, 2000).
- The stockholders of the target are offered premium as an inducement for them to sell their shares (Hirt and Block, 1999).
- As posit by Lease et al (1983), the value of control or ability to realize tax advantages is considered as additional to the current market value.

According to Weston and Copeland (1989), the offer price is historically 10% to 20% higher than the market price before the merger announcement, due to the reasons above. However, provisions of 5% have been observed.

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Book Value per Share: Although book values have generally been considered to be relatively unimportant in determining the value of a firm, in certain instances it has an impact on the merger term especially when it substantially exceeds the market value. The book value represents an index of the amount of physical facilities made available in the merger. It however, does not capture intangible assets. Because of the potential contribution of physical properties to improved future earnings, book value may have an important influence on actual merger terms (Hiiggin and Schall, 1975).

Net Current Assets per Share: The Net current assets per share can have an influence on merger terms as they represent the amount of liquidity that can be obtained from a company in a merger. Again, Weston and Copeland (1989) posit that if an acquired company is debt-free, the acquiring firm may be able to borrow the funds required for the purchase, using the acquired firm's assets and earning power to pay off the loan after the merger or to provide security for renewing or even increasing the borrowing. They further state that by the same token, a firm seeking to avoid being acquired may reduce its liquid position and use up its borrowing potential.

Merger waves

Merger waves are periods of unusually intense mergers activity (Gaughan, 1999). They have all occurred in the western economically advanced countries especially the U.S and U.K where mergers have long been prevalent.

Merger waves tend to occur during economic expansions, and they end when the economy and the market slow down. This is so because economic

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expansion leads to increasing demand, which causes companies to endeavour to grow, in order to meet the demand. When the economy slows down companies are less concerned about expansion and so mergers play a lesser role in corporate plan. Additionally, during economic down turn, deals that could be financed by stock may become more expensive (Gaughan, 1999).

The first three merger waves occurred at the start of the twentieth century, during the boom of the 1920s, and at the end of the 1960s. Each was distinct. The first merger wave occurred between 1897 and 1904 and featured the transformation of the American economy from one of many small companies to larger, sometimes monopolistic firms dominating an industry. This period of consolidating mergers and acquisitions was ironic in the light of the passage of the Sherman Antitrust Act in 1880. The difficulty the courts had in interpreting the broad provisions of the law and the fact that the Justice Department lacked the resources and probably the mindset to fight this first great merger wave were some of the many reasons for the lack of antitrust enforcement. The situation however changed with the passage of the Clayton Act in 1914 and the establishment of the Federal Trade Commission in the same year which, along with the Justice Department, enforced antitrust laws.

The second merger wave began in 1916 and continued until the economic downturn in 1929. This wave featured many of the same types of horizontal transactions as the first wave, but also had a good proportion of vertical transactions. While the first merger wave can be said to be mergers towards monopoly period, the second wave can be said to be of mergers towards an oligopoly period.

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The third merger wave took place between 1965 and 1969. This featured conglomerate mergers. In many of the deals, the acquiring companies acquired targets across industries. In many of the cases these measures would not be considered in any way as strategically fit by current standards. Many of the companies paid a price for these non-strategic deals, when they later sold off those diversifications in the 1970s and 1980s.

The fourth merger wave occurred between 1983 and 1989. While it was largely confined to the United States, large-scale mergers and acquisitions finally made their way to Europe in the mid-1990s (Gaughan, 1999). These include even hostile takeovers, which had long been considered as exclusively an America phenomenon. This is evident by the fact that the Vodafone-Mannesmann $183 billion deal, then the biggest deal of all time was a hostile takeover. The fourth merger wave was characterized by mega-mergers and many high-leveraged transactions. Many of these transactions were financed by the junk bond market that grew dramatically in the 1980's, but collapse at the end of the decade.

In recent years, cross-border deals within Europe have become common. In addition to deals within Europe, trans-Atlantic deals, with European buyers of U.S. companies and vice versa, started to become commonplace. With the establishment of the European Union, a unified market structure, a common currency and erosion of national barriers in the continent, companies see their market as all of Europe and more.

The fifth merger wave began in around 1993 as the economy began to recover from the 1990-1991 recession. As the economy expanded, firms sought to meet the growing demand in the economy by merging with other

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companies. A distinctive characteristic of fifth waver was that in a way it closely followed the fourth merger wave which ended around 1989.

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CHAPTER THREE

METHODOLOGY

Introduction

This chapter provides explanation of the techniques used in data collection and data analysis in the study. It also provides background information of the firm under study and other firms in the brewery industry in Ghana.

Background of the companies

The production of beer in Ghana began in the 1930s, initially by four companies namely Accra Brewery Limited (ABL), Guinness Ghana Limited (GGL), Kumasi Brewery Limited (KBL) and Achimota Brewery Company Limited (ABC). This was in response to increasing demand for both alcoholic and non-alcoholic beverages and the need for low production cost. Prior to the establishment of the breweries such beverages were imported from renowned brewery firms overseas which established distribution centers in the country. ABC later changed its name to Ghana Brewery Limited (GBL) and shortly afterwards, in 1998, GBL and KBL merged. The number of companies in the brewery industry then reduced to three namely ABL, GGL and GBL (Dewotor, 1998). The number reduced further to two, namely ABL and Guinness Ghana Breweries Limited (GGBL), in 2005 following the merger under study.

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Prior to the merger between GGL and GBL Heineken Plc had restructured GBL and injected capital into GBL to improve capacity and operating efficiency making GBL the largest brewer in the country (Dewotor,1998). Similarly, Guinness Plc's keen interest in GGL had allowed for the investment of $17.4 million worth of internal funds in capacity expansion and technological improvement that had made GGL the most technologically advanced brewer in West Africa. South African Breweries (SAB) had also restructured ABL making it more competitive, having acquired indirect controlling interest in ABL in 1997. These developments placed the sector in an environment of intense competition (Dewotor, 1998).

The Former Guinness Ghana Limited (GGL)-The Acquiring Firm

GGL was incorporated in Ghana in August 1960 as a private company engaged in the distribution of imported Guinness Foreign Extra Stout. Initially it was owned by Guinness Overseas Limited (63.75%) and Atalantal Limited (36.25%). The Government of Ghana later secured 45% equity stake in the firm while 15% of the equity was issued to the Ghanaian public (Dewotor, 1998). The share holding of GGL then underwent some restructuring resulting in the position, prior to the merger, whereby out of a total of 117,480,000 shares outstanding, Guinness Overseas Limited held 60%, Ghana Government 1%, Ghanaian public 28%, foreign portfolio investors 10% and GGL’s Employees 1% (Annual Reports of GGL, 2004).

In 1970, the company set up a brewing and bottling plant in Kumasi, for local production. The brewing, packaging and marketing of Guinness extra stout started in 1971 while Malta Guinness was introduced in 1989 and

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followed much later by Maxi-Malt (with a number of flavours) in 1996. Maxi-Malt was however withdrawn from the market and replaced with a canned variant of Malta Guinness. Thus prior to the merger, GGL was producing only Guinness Stout and Malta Guinness, and had the least diversified product line in the brewery industry. This notwithstanding, the company continuously led the stout and malt markets in terms of market share value, controlling around 90% and 80% respectively (Annual Reports of GG L, 2004).

From an initial plant capacity of 60,000 hectoliters, GGL in 1998 utilized almost 100% of its installed capacity of 350,000 hectoliters causing it to increase its capacity to the level of 800,000 hectoliters with the installation of a 40 billion cedis plant. This investment enabled GGL to enjoy a modern state-of the-art brewing process, offer world class product quality and significantly uplift its capacity and operational efficiency. Additional facilities provided by this investment included a fully automated brewing process, a new refrigeration plant, a new water treatment plant to deliver superior water quality, de-aerated liquor plant to enhance capacity and a 300 KVA generator set, to ensure uninterrupted power supply. GGL was thus well positioned to meet the growing demand for its products and enhance revenue growth, improve profit margins at least in the medium-term. This was the result of the expanded capacity and improved technology, continuous product innovation and creative marketing initiatives and enhanced operating efficiency (Annual Reports of GGL, 1998-2001).

GGL’s main threat was in the stout market segment where ABL had recently introduced a lower priced stout, Castle Milk Stout. GGL had 100% nation-wide coverage with a well-knitted network of distributors, dealers,

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wholesalers and retailers. About 60% of the company's sales were made in the more urban and populated southern part of the country (Dewotor, 1998).

The Former Ghana Brewery Limited (GBL) -The Target Firm

Ghana Brewery Limited was formed out of a merger between KBL and GBL (former ABC) which was conducted under Section 230 (7) of the Companies Code 1963 (Act 179). The combined company assumed the name 'GBL' and continued with the businesses of KBL and ABC without any change in objectives of operations. Ghana Breweries Limited was subsequently listed on the Ghana Stock Exchange on 17th July 1998.

Before the merger, KBL was fully under the management of Heineken N.V., as a result of the latter's controlling equity stake in the former. Heineken N.V. also took over the management of ABC, upon acquiring 90% equity stake in the local company. Having secured control of the management of these two brewing companies, Heineken sought to avoid unnecessary duplication of activities, reduce operational cost and capture synergies as well as increase market share and thereby improve profitability. For these reasons and for ease of administration the board of directors of KBL and GBL decided to merge. KBL became the survivor (acquirer) and GBL the acquired (victim). The objects of incorporation of ABC however remained the same, so as to maintain its identity (Ghana Breweries Limited Annual Reports, 1997).

The merged company was expected to be more efficient and to benefit from KBL and Heineken's tradition of excellent management as well as technical and financial resources from Heineken. It was also expected to increase the capacity utilization of ABL'S plant and machinery and at the

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same time relieve the pressure on the aging equipment of KBL. KBL had been expected to reach its full capacity in the near future. This would have resulted in the loss of market share and profitability. Without the merger KBL would have had to acquire approximately $30 billion loan to replace its aging equipment. The resultant high interest payment would have led to losses and KBL would have been unable to pay dividends within the foreseeable future (Dewotor, 1998).

ABC had a relatively modern bottling line with brewing capacity of one million hectoliters which was enough to supply the total Ghanaian market of approximately 900,000 hectoliters. However, its capacity utilization was less than 50% (300,000 hectoliters). The excess capacity was to be exploited efficiently by KBL after the merger to enable the merged company make positive gains in the lager beer market in Ghana. The merger was therefore expected to result in improve profitability of the joint operations through enhancement of market share and reduction in cost of operation. On the other hand, ABC had substantial negative balance in its income surplus account, meaning it would also not have been able to pay dividend to its shareholders within the foreseeable future (Dewotor, 1998).

Therefore the objective of Heineken and the management team to restructure ABC within a given period was to enable the merged entity to generate enough profit to maintain consistent dividend payout to shareholders in the medium to long-term. In addition, the shareholders were to benefit from having shares in the largest brewing company in the country (Dewotor, 1998).

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However, these expectations were not met after the merger and this led to the GBL and GGL merger in 2004. At the time of the GGBL merger, GBL's equity shares outstanding totaled 334,220,000 (Appendix).

Guinness Ghana Breweries Limited (GBL) -The Merged Company

Guinness Ghana Breweries Limited was formed in December 2004 out of the merger between the former GGL and the former GBL, in which GGL acquired the shares of GBL. Prior to the merger, GGL had continuously achieved significant levels and growth ahead of the market in corporate performance in all its brands and had consistently increased dividend payment. The performance indicators can be seen clearly in figures 1 to 6 and tables 1and 2, all in chapter 4. These achievements were the results of continuous huge investments in capacity, research and creative marketing initiatives and of effective distributing network. These in turn, resulted in quality management, high efficiency in production and operating practices and quality products that met consumers taste. In 1998 and 2004 for instance, investments in capacity amounted to Gh¢4m and Gh¢16.64m respectively.

On the other hand, the objectives and expected benefits from the combined firm from the merger between KBL and GBL were not being realized. Profitability and sales growth declined from the pre-merger to post-merger periods while there was a downward fall in liquidity after the merger. Additionally, operating expense increased considerably and earnings per share reduced significantly. As a result no dividends were paid after the merger.

Shareholders of the company were not satisfied with this poor corporate performance. Heineken N.V., parent company of GBL was unhappy

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with the low level of return on its investment in GBL because it was far below Heineken's expected rate of return. Initially, Heineken intended to move its investment out of the country. However it considered the view that as a multinational company, it was good to maintain its investment in Ghana as a component of its portfolio diversification. Thus the merger with GGL was sought. As two giant multinational companies, Heineken and Guinness saw the need to join their efforts to reap synergic benefits rather than competing against each other, considering in particular that the Ghanaian market is relatively small. The terms of the merger were cash payment for the minority shares of GBL. In the process GGL's outstanding shares were increased by 47,191,475 shares to 164,671,475 shares in the combined company (GGBL Annual Report, 2005).

After the merger in 2004, Heineken N.V. received 20.56% (representing 33,851,463 shares) of total outstanding shares of GGBL, this reduced to 20% (32,934,295 shares) by 2007. Diageo Highlands BV, parent of GGL shareholding reduced from 60.37% (70,921,228 shares) of total outstanding shares in GGL to 50.44% (83,065,284 shares) of the total shares of the combined firm. This increased to 51% (83,982,452 shares) by 2007. Thus Diageo Highlands BV and Heineken N.V. became the majority and minority share holders respectively in control of the combined company. The share holding structure of the acquiring firm, GGL, before and after the merger are shown in tables 1 in chapter four (Annual Reports of GGL, 1998-2004 and Annual Reports of GGBL, 2005-2007).

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Other Current and Former Participants in the Brewery Industry

Accra Brewery Limited (ABL)

ABL was established in 1931 as Overseas Breweries Limited, a wholly-owned subsidiary of OBL of Switzerland, to brew beer and produce carbonated drinks in the country. It was the first brewery to be established in the West African sub-region. The name of the company was subsequently changed to ABL while in 1997 South African Breweries (SAB) acquired a majority stake in Overseas Breweries Limited and currently owns 51.12% equity stake in ABL. SAB has therefore technically become the controlling shareholder of ABL (Dewotor, 1998).

ABL began operations with the production of Club Lager Beer, the company's flagship and a host of soft drinks. A non-alcoholic malt drink, Vita malt previously imported from Denmark was later introduced. ABL also distributes Castle Lager Beer and Castle Milk Stout, from South African Breweries. In addition, the company increased the range of its line by introducing the canned Club Beer (Dewotor, 1998).

Former Kumasi Brewery Limited (KBL)

KBL was established as a private limited liability company in 1960 by a group of foreign investors led by Unilіver Plc and Heineken to manufacture, sell and deal in beer, stout, mineral waters and other ancillary products. It was also to invest its funds in acquisition, by purchase, lease or otherwise of interests of land and building as deemed fit by the directors.

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KBL was converted into a public liability company in 1976, allocating 55% of its shares to Ghanaians, in compliance with Ghana's Indigenisation Policy. Subsequently in 1990, the company was listed on the Ghana Stock Exchange. In August 1995, Unilever divested its shareholding of 25.2% in KBL and this was acquired by Limba Ghana Limited, a wholly owned subsidiary of Heineken Plc. This acquisition, together with Heineken's own shareholding, placed Heineken in a controlling position with 50.26% shareholding in KBL (Dewotor, 1998).

KBL primarily produced and distributed Gulder and Star Lager beer as its main brands. The growing demand for non-alcoholic beverages particularly, with the successful introduction of Malta Guinness by GGL encouraged KBL to add Maltina, to its product line in 1990. Unfortunately, Maltina performed poorly. KBL then launched Amstel Malta, another brand of non- alcoholic malt beverage in July 1996. In February 1997, the company commissioned a 90 thousand Ghana cedis kegging line for the production of

Star Beer in draught

Over the years KBL had consistently increased the production volumes of its brands despite heavy reliance on an aging brewery house and a single bottling line. KBL's products were distributed throughout the country via several distributors, wholesalers and retailers. It's location in Kumasi enabled it to dominate the beer market in the northern sector, though 53 % of its products were sold in the southern sector (Dewotor, 1998).

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Former ABC Brewery Limited (ABC)

This company was incorporated in April 1992 as a limited liability company by a consortium of investors led by SSNIT to acquire the then Achimota Brewery Company from the Ghana Government. The late J.K. Siaw, a renowned Ghanaian entrepreneur, had founded the company in 1969 with the objective of carrying on business as brewers, distillers and manufactures of, and merchants and dealers in beer, ale, porter, shout, wines spirits, soft drinks, aerated waters and liquors of every description. Another objective was to market, distribute and sell beer and other alcoholic and non-alcoholic beverages and to act as wholesalers and retailers of such drinkables and related merchandise.

ABC was owned and managed by its founder until it was nationalized in 1979 by the then military regime and thereafter, the Government of Ghana became the sole shareholder. In 1997, Heineken N. V. acquired 90% of the total equity shares of ABC. The remaining 10% shareholdings were held by SSNIT. SSNIT, the minority shareholder and, Heineken N.V the majority shareholder of ABC, thus assumed fill management control over its operations.

The company was the first brewery to introduce draught beer (ABC Bubra) in the country. The company further diversified its operations to include the production of soft drinks made up of Afri cola, Bluna Tropic, Bluna Orange and Bluna Zit, in response to the growing demand for these products. The company's plant capacity was increased with the installation of a new carbon dioxide plant and a new bottling line to cope with the expected increase in production volume. Unfortunately the company was unable to

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increase its capacity-utilization to any appreciable level and this contributed to its merger with KBL. Before the merger, ABC changed its name to GBL (Dewotor, 1998 and ABL Annual Reports 1997 and 1998).

Study design

Selection of Company of Study

The study mainly concerned with acquiring firms. The merger between GGL and GBL to form GGBL is being selected as a case for study based on consideration that this merger is a recent one listed on the Ghana Stock Exchange (GSE), and the financial data available is sufficient for the analysis period. This period covers the three years immediately before and the three years immediately after the merger. Another reason is that the merger under study followed, quite closely, the merger between the former KBL and GBL (former ABC Ltd) which adopted the name GBL. Both KBL and GBL were listed on the GSE. The selection of this sample is also intended to broaden the period and scope of study of the issues concerned with Mergers.

Data Collection

The study used mainly Secondary data. Several visits were made by the author to the company, its registrars (Merchant Registrars, the investment division of Merchant Bank), the lead brokers for the merger (Strategic African Securities-SAS) and Ghana Stock Exchange, to obtain financial data on the company, for the purpose of this work. From these visits mainly annual reports of the company and some extracts thereof were obtained. Interviews were also held with some officials (past and present) of the above organizations during which additional qualitative information were obtained

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Data Analysis

Extracts of the data obtained are analysed and discussed, with the aid of selected financial ratios and corresponding graphs computed using the data. The selected financial ratios were computed for the three years immediately before and three years immediately after the merger. The calculation of the ratios and their corresponding graphs for periods surrounding the merger date helped in identifying and comparing the trends in corporate financial performance of the acquiring company before the merger and of the merged company after the merger.

Seven performance indicators (classes of ratios) were computed to measure the company's profitability, growth, liquidity, financial leverage, efficiency and expense ratios as in the study of Tsung-Ming and Hoshino, (2000). The earnings per share and dividend per share were also computed. These indicators were calculated as follows:

Profitability

Gross Operating Margin (GOM) = Gross Profit/Turnover

Net operating Margin (NOM) = Profit before tax/turnover

Return On Assets (ROA) = Profit before tax /Total Assets

Return On equity (ROE) =Profit before tax/net worth

Expenses Ratios

Operating Expense Ratio (OER) = Operating Expense/Turnover $\times 100\%$

General, Selling & Admin. Expense Ratio (GSDER) = GSDER/Turnover $\times 100\%$

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Net Interest Charge Ratio (NICR) = Net Interest Charge/Turnover ×100%

Liquidity

Current Ratio (CR) = current assets/current liabilities

Quick Ratio (QR) = (current assets-inventories)/current liabilities

Acid Test Ratio (ATR) = Cash and Bank + cash equivalent/current liabilities

Financial Leverage

Long Term Liabilities to Total Assets (LLTA) = long term liabilities/total assets

Debt Equity Ratio (DE) = Total liabilities/Equity.

Growth

Sales Growth (SG) = (Sales of current year/sales of previous year) -1

Total Assets Growth = (Total Assets of current year/Total Assets of Previous year) -1

Earnings per Share and Dividends Per Share

Earnings per share (EPS) = profit after tax/number of shares outstanding.

Dividends per share (DPS) = dividends paid/number of shares outstanding.

Tables 1 and 2 in chapter four show the financial data and the computed financial performance indicators respectively.

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CHAPTER FOUR

ANALYSIS AND DISCUSSION

Introduction

The strand of literature on the methodology of assessing the impact of Mergers and Acquisitions on corporate financial performance is from industrial economists. Industrial economists concentrate on the efficiency aspects by comparing profits, sales, operating efficiency, liquidity and other indicators in pre-and post-merger periods. They generally use accounting data generated internally by the merging firms. Several studies in the US use this approach. In these studies there is no consensus regarding what happens to the firm's profitability after the merger (Mueller, 1980), (Ravenscraft and Scherer, 1987), (Healy et al, 1992), (Lichtenberg, 1990), (Dickerson et al, 1997) and (Calomiris and Karceski, 1998). The findings of different studies may be due to different measurement methodologies employed and the different sample selections.

In this study, accounting data are used to examine GGBL, a merged Ghanaian firm. This approach has been adopted by several studies such as Healy et al (1992) and Cornett and Tehranian (1992). During visits to the company and other organizations concerned with the merger (mentioned earlier) annual reports and other relevant documents of the company were provided for study. Additional information was gathered from interviews, mentioned under Methodology. The financial data of the company covered the

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three years before the merger was announced and three years after the merger (see table 1).

Table 1: Selected income statements, income surplus statement and balance sheet figures in thousands of Ghana cedis (GH¢000) for GGBL (2005-2007) and GGL (2001-2003).

	GGBL			GGL		
	2007	2006	2005	2003	2002	2001
	Year + 3	Year+ 2	Year+1	Year -1	Year-2	Year-3
Turnover	122,411	104,760	79,945	36,208	25692	19,064
Cost of Sales	80,115	60226	32,958	21,481	14,348	10,428
Gross Profit	42,295	44,534	32,958	14,727	11,344	8,637
Gen., Selling &						
Admin. Exp.	20,701	22,651	17,396	8,569	6,634	4,940
Net Int. charges	5,119	3,600	2,161	3	25	1,081
Operating Exp.	105,935	86,477	66,544	30,053	21,007	16449
Profit before tax	15,119	19,053	13,580	6,519	4,817	2639
Profit after tax	14,011	15,006	10,802	5,063	3,519	1836
Dividen Proposed	7064	6883	5939	2937	2056	1057
Fixed assets	83929	75103	62748	15020	8129	6846
Current assets	48118	8595	30877	12393	7809	5702
Stock	24424	18645	14334	5777	3640	2691
Debtors	18684	15443	8029	1946	2019	1035
Cash & Bank	5010	4507	8514	4670	2150	1649
Total Assets	132047	120271	100198	27748	16273	12882

Source: Author’s calculation.

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Table 1: selected income statements, income surplus statement and balance sheet figures in thousands of Ghana cedis (GH¢000) for GGBL (2005-2007) and GGL (2001-2003). (cont.)

	GGBL			GGL		
	2007	2006	2005	2003	2002	2001
	Year +3	Year+2	Year +1	Year -1	year-2	year-3
Current liabilities	47001	64787	46337	5821	6715	4743
Creditors	17744	23903	17374	6796	3488	1944
Short term loans	2367	6243	4320	-	-	-
Net Current Assets/ (Liabilities)	1117	(26192)	(15459)	(3427)	1094	958
Medium term liabilities	27000	545	6788	-	-	-
Total Liabilities	74982	68333	56389	17098	7750	5822
Net Assets	57065	51938	43809	10650	8524	7060
Stated Capital	26252	26252	26252	769	769	769
Income Surplus	30518	25391	17268	9586	7460	5997
Shareholders' Fund	57,065	51,938	43809	10650	8524	7060
No.of shares issued (in thousands)	164671	164671	164671	117480	117480	11740

Source: Author's calculation.

Data analysis

In order to examine the medium-to long term effect of mergers and acquisitions, the acquiring firm's financial data include three years before the

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acquisition is completed (year-3, year -2, and year -1), and three years after the acquisition (year+1, year+2 and year+ 3). The year in which the merger was consummated, 2004 (year zero), is not included in the data because varying accounting practices may bias the financial measurements in the year of consolidation. Exclusion of data for year zero can minimize the effect of such ‘noise’. Comparing the post-merger performance with pre-merger performance provides a measure of the change in corporate performance.

The table below shows the financial data for each performance indicator for each of the three years immediately before and the three years immediately after the merger. Below the table are graphical presentations of the data (ratios) and the discussions.

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Table 2 financial performance indicators for the acquiring firm (GGL) for each of the 3 years before and the three years after the merger.

Indicator	Ratio	Year+ 3	Year+ 2	Year+1	Year- 1	Year- 2	Year- 3
Profitability	GOM	34.55	42.51	41.26	40.67	44.15	45.31
Rates	NOM	12.35	18.19	17.00	18.00	18.75	13.84
(%)	ROA	11.45	15.84	13.55	23.50	29.60	20.49
	ROE	26.50	36.68	31.00	61.21	56.51	37.38
Expenses	OER	86.54	82.55	83.24	83.00	81.77	86.28
Ratio (%)	NICR	4.18	3.44	2.7	0.01	0.1	5.67
	GSAER	16.91	21.62	21.76	23.67	25.82	25.91
Liquidity	CR	1.02	0.60	0.67	0.78	1.16	1.20
Ratios	QR	0.50	0.31	0.36	0.42	0.62	0.64
	ATR	0.11	0.07	0.18	0.30	0.32	0.35
Financial	LLTA	0.21	0.03	0.10	0.05	0.06	0.84
Leverage	DE	1.31	1.32	1.39	1.61	0.91	0.83
Growth	Turnover	16.85	31.04	51.64	40.93	34.77	52.08
Rates (%)	Assets	9.79	20.03	117.93	70.52	26.32	-19.40
Investment	EPS	0.0851	0.0911	0.0656	0.0431	0.0300	0.0225
Returns	(Gh¢)						
	DPS	0.0428	0.0419	0.0300	0.0186	0.0130	0.0090
	(Gh¢)						

Source: Author’s calculation.

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Discussion of results

Growth

Figure 1 depicts growth rates of turnover and total assets. There were continuous sharp increases in GGL's total assets growth rates from the second pre- merger year till the year of the merger. A similar sharp increase occurred in the first post-merger year. This was however followed by a continuous steep drop in the growth rates during the next two post-merger years. From the second pre-merger year the turnover growth rate, though with lower values till the second post-merger year, generally changes along with changes of the total assets growth rate.

As can be seen from figure 1 the pre-merger turnover growth rate for GGL has out-performed the post-merger growth rate of GGBL, although there was a sharp increase in the first post-merger year. The decreasing post-merger turnover growth rate means the merger has not brought about any superior market performance, because it has not resulted in any monopolistic or superior market power for the combined firm. Monopolistic or superior market power is the natural goal of horizontal mergers (Brealey and Myers 2000).

The situation is partly due to difficulties in coordinating activities of the two previous firms. Brealey and Myers (2000) assert that it is easier to buy another business than to integrate it with yours afterwards. They also posit that many mergers that seem to make economic sense fail because managers cannot handle the complex task of integrating two firms with different production processes, accounting methods and cooperate cultures. Other contributing factors are lack of corresponding increases in prices of products to match inflation and exchange rate changes and the intensification of

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competition in the beer industry during the study period (GGBL's Annual Reports, 2005 and 2006). Nevertheless, as the growth rates are positive, it means that in absolute terms the increases in turnover are significant.

The continuous sharp increases in total assets growth rate from -19% value in the third pre-merger year (year-3) to 118% in the first post-merger year (year +1), resulted from huge assets acquisition through both internal investments and the merger. GGL installed a 40 billion cedis plant after the company attained 100 % utilization of installed capacity in 1998 (Dewoto, 1998). A lot of assets were disposed off after the merger without commensurate replacement. There was also alignment of operations including utilization of GBL's excess capacity. These result in the sharp drop in post-merger total asset growth rate.

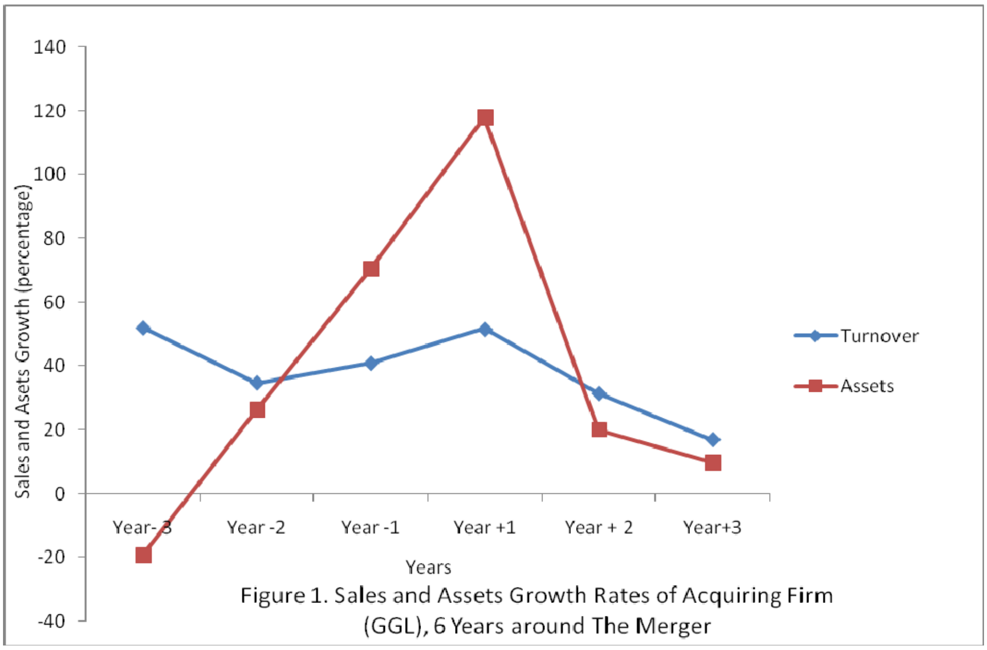

Figure 1. Sales and Assets Growth Rates of Acquiring Firm (GGL), 6 Years around The Merger

Source: Author's calculation.

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Profitability

In order to evaluate the impact of the merger on the profitability of GGL, four ratios: ROA, ROE, GOM and NOM were used. From figure 2 it can be seen that there is a steep decrease in ROE and ROA in the post-merger period relative to pre-merger period. The decline in ROA started a year prior to the merger and deteriorated further in the first post-merger year, along with the ROE. An improvement in both ROA and ROE in the second post-merger year, over the previous year, was followed by decreases in these ratios in the third post- merger year. A similar decreasing trend occurred in NOM and GOM, starting from the pre- merger period, though at a lower degree. In the third post-merger year, all the four ratios decreased. The decrease in ROE and ROA after the merger is an indication that the degree of effectiveness of management of the combined company has decreased relative to the pre-merger situation of the acquirer. Management were finding it difficult integrating and coordinating operations of the two previous firms, This buttresses the assertion that it is easier to buy another business than to integrate it with yourself (Brealy and Myers, 2000). The lower values of GOM and NOM in the post-merger period means the firm's overall performance is reducing relative to the pre-merger performance of GGL. The situation buttresses the Hubris Hypothesis by Richard Roll (1986).

Generally, the merger has brought about no improvement in corporate profitability, three years after the merger, despite the strong performances at turnover. The payment of high interests on overdrafts and loans (table 1 above), used to finance the merger and to fund working capital, and the high general operating expenses are contributory factors for the decreasing post-

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merger profitability. In absolute terms however, post- merger profits are higher, as these ratios and turnover growth rates are all in positive values. This decreasing post-merger accounting performance buttresses the results of the studies by Ravenscarft and Scherer (1987) and Herman and Lowenstein (1988).

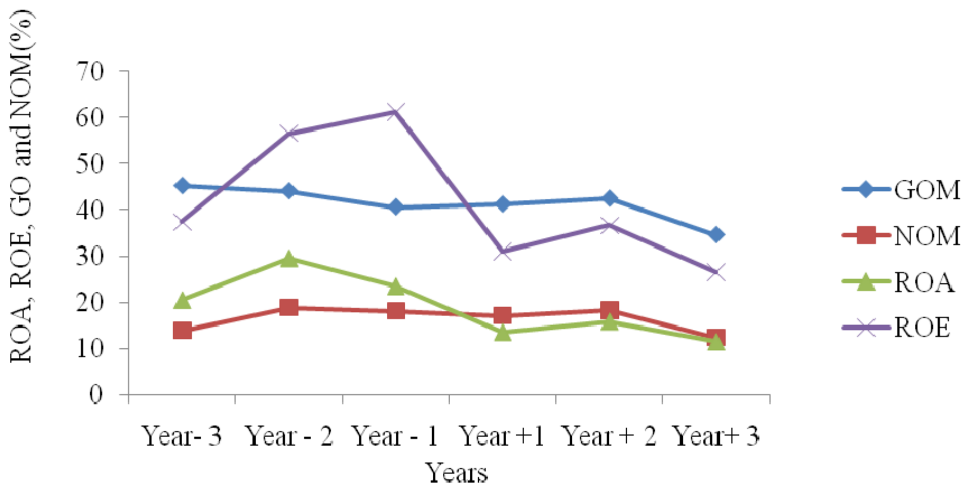

Figure 2. ROA, ROE, GOM and NOM of Acquiring Firm (GGL), 6 Years around the Merger.

Source: Author’s calculation.

Expenses

As can be seen in figure 3 below, there has been a continuous decline in General, Selling and Administrative Expenditure. Though this trend started during the pre-merger period, the decrease was more pronounced in the third year after the merger (year+3). This may means that the combined company has started to achieve operational and strategic synergies, as explained by

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Weston and Copeland (1989), an indication that the objective of achieving reduction in operational cost, through the merger, could be achieved.

Net interest charges as a percentage of turnovers (NICR) on the other hand, after achieving a significant decrease during the second pre-merger year increased continuously after the merger. This was due to the servicing of loans and overdrafts which rose sharply after the merger. These were relied upon for financing the working capital and the merger itself. Both short loans and medium term liabilities were non- existent during the period before the merger (table 1 above). The increasing net interest rates contributed to the high and increasing operational expenses and the decreasing profitability.

Generally, the overall operating expense ratio (OER) has being in ascendency after the merger, though a marginal decrease occurred in the second post-merger year. The increase was more pronounced in the third post-merger year. As shown in figure 3, there was a significant decrease in the OER before the merger was completed (in year-2). This trend may reflect a high level of efficiency of GGL, following heavy internal investment in modern equipment and technology, before the merger and conversely, a decreasing level of overall efficiency after the merger. This in turn contributes to the deceasing profitability of the combined firm, after the merger. The situation buttresses the Corporate Control Hubris Hypothesis by Richard Roll (1986) and the findings of Lichtenberg and Siegel (1989).

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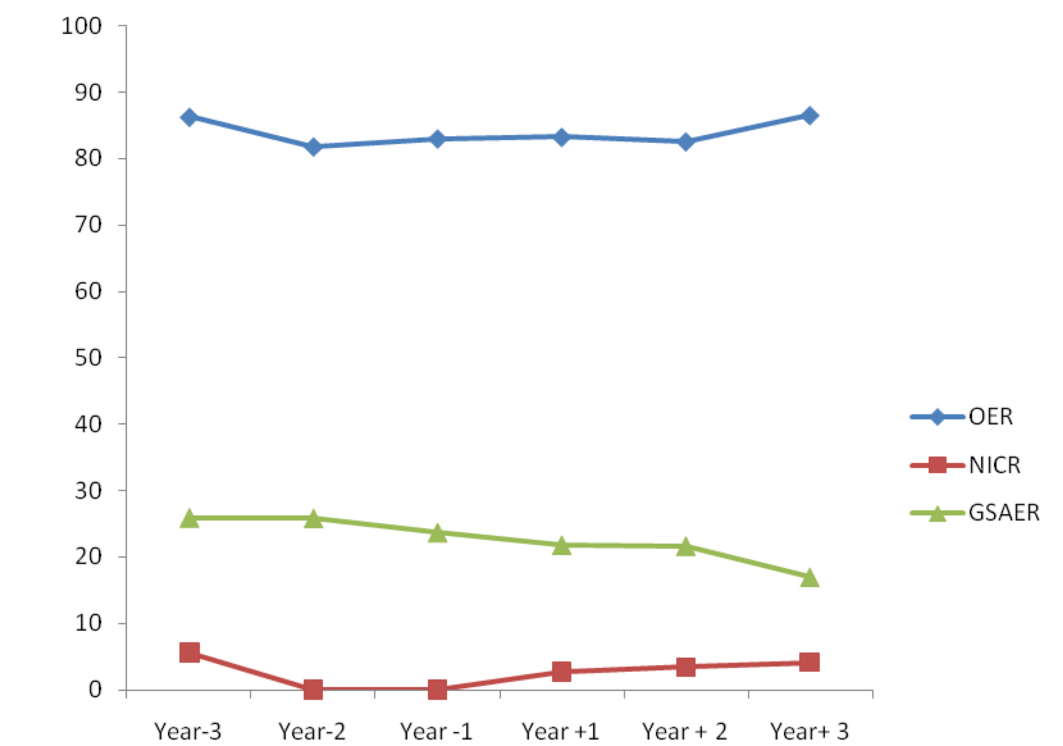

Figure 3. OER, NICR and GSAER for aquiring firm (GGL), 6 years surrounding the mergerChart

Source: Author's calculation.

Liquidity Indicators

There was significant deterioration in liquidity, beginning from the start of the pre-merger period under study, as CR, QR and ATR all continuously declined deeply into the post-merger period, reaching lowest levels in the second post-merger year. As can be seen in table 1 above, this is accounted for by 72% deep decline in current assets (from Gh□30,877,000.00 to Gh□8,595,000.00) and 40% increase in current liabilities (from Gh□46,337,000.00 to Gh□64,787,000.00), all in second post- merger year. Liquidity however started to increase in the third post- merger year as current assets rose by 41.5% while current liabilities decreased by 27.5%, as depicted

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in figure 4 below. Net assets figures over the study period attest further to this trend of liquidity.

The decreasing liquidity is mainly a result of the company's resort to short-term borrowing to finance the merger and working capital. Table 1 shows that short term borrowings were undertaken in the post-merger period but were non-existent in the pre-merger period. This buttresses the findings of Lewellen (1971). The decreasing liquidity means the company may be finding it difficult to meet its current obligations, which could pose a serious challenge to its operations. However, if the significant reversal of this trend that occurred in the third post-merger year is sustained, this threat may be eliminated and the company's operations strengthened as in the findings of Lichtenberg and Siegel (1989).

Finally as can be seen in Figure 4, in the third post-merger year the increase in ATR was less significant compared to the increases in CR and QR. This means that the improvement in liquidity may have resulted mainly from relative increases in stocks and debtors. This is confirmed by higher values and sharper increases in stocks and debtors during the post-merger period relative to pre-merger period, as shown in table 1. It is therefore necessary to improve the company's cash operation cycle, especially debts collection, sales and distribution and production so as to strengthen the company's ability to meet its short term obligations.

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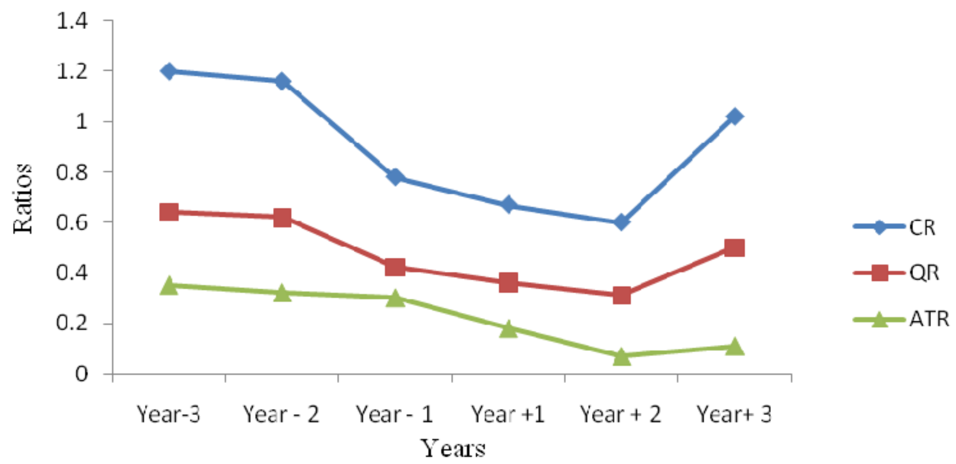

Figure 4. Liquidity (CR,QR and ATR) ratios of Aquiring Firm (GGL) for 6 Years around the Merger

Source: Author's calculation.

Financial Leverage

Figure 5 shows the financial leverage measures, LLTA and DE. LLTA was much lower in the post-merger period relative to the pre-merger period. It decreased deeply, reaching almost negligible values, in the second and first pre-merger years. This was due to sharp increases in total assets following the huge internal investment in equipment and technology, without recourse to debt financing, before the merger. It is worthy of note that during these years there were zero medium term liabilities and short term loans while overdrafts were relatively minimal. The company started securing short term loans, medium term liabilities and higher overdrafts in the year in which the merger was completed, to help finance the merger and fund the resulting increased working capital (table 1 above).

As depicted in the figure below, LLTA increased and decreased slightly in the first and second post-merger years respectively and then increased significantly in the third post-merger year. The values however still

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remained lower, relative to the period before year -2. These changes resulted from the increases in debt funding and in assets acquisition through the merger as well as the subsequent disposal of some of the assets. The low LLTA levels strengthen the credit capacity of the combined firm. This buttresses findings of Nicolas Travos (1987).

The DE has being in continuous decrease over the post-merger period under study but the values have being higher relative to those of the pre-merger period. This, in addition to the sharp increase in DE in the last year before the merger (year-1) confirm that the merger was debt financed. The result is that share holders' wealth has not being diluted by the merger. The post-merger decreasing trend of the DE corresponds with the increasing loans, overdrafts and other liabilities that follow the merger (table 1).

Finally, it can be seen from figure 5 that the DE and LLTA were equal in value in the third pre-merger year. In the subsequent years, while the DE increased the LLTA on the other hand decreased. This was due to the debt financing of the merger, increased post- merger working capital and probably other investments, leading to the high financial leverage of the combined firm.

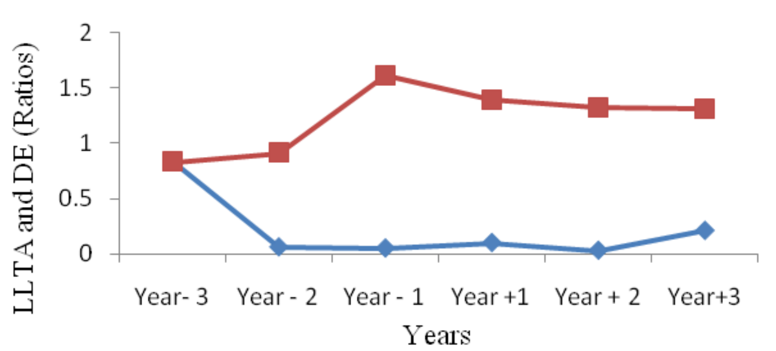

Figure 5 Financial Leverage Indicators for Aquiring Firm (GGL) for 6 Years around the Merger

Source: Author's calculation.

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Earnings per Share and Dividend per Share

Figure 6 shows the plots of earning per share (EPS) and dividend per share (DPS) against the period of study. The post-merger EPS and DPS values are higher than the pre-merger values. Both of these values rose significantly throughout the study period, with the exception of the last year. In the third post-merger year however, there was a drop in the EPS and so the DPS was increased only marginally. These trends confirm the assertion by Hoyle et al (2001) that increases in scale can produce larger profits from enhanced sales volume despite smaller (more competitive) profit margin. The company could pay increasing dividend because profits have being increasing in absolute terms, albeit at reducing rates. The aim may be to sustain shareholders and investors interest in the company and their support for management, which confirms Pierson et al (1990). These notwithstanding, the company's share price, after rising by 342% to Gh¢1.20 in the year of merger, rose by only 113% over the three year post merger period, to Gh¢2.55. Nevertheless the levels of EPS and DPS may be unsustainable if the decreasing post- merger profitability and other accounting performance, after the sharp initial increases and sharp decline in EPS in the third post-merger year, as discussed above, continue.

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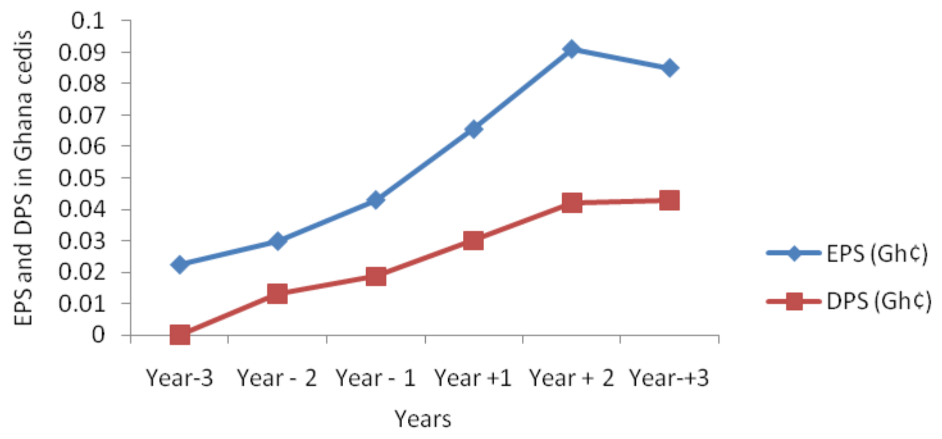

Figure 6 EPSand DPS for Aquiring Firm (GGL) for 6 Years around the Merger

Source: Author’s calculation.

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CHAPTER FIVE

SUMMARY, CONCLUSIONS AND RECCOMMANDATIONS

Summary

In this study, the impact of mergers and acquisitions on corporate financial performance has been examined using GGBL as a case study. In investigating these issues the pre-merger and post-merger behaviour of GGL/GGBL is examined using performance measures based on the annual reports of the company for 2004 to 2007. The three consecutive years immediately before and the three consecutive years immediately after the merger are considered in the study as the pre-merger period and post-merger period respectively. Performance measures examined were: growth rates, profitability ratios, expense ratios, liquidity ratios, financial leverage, earning per share and dividend per share. It was found out that:

- There has been a downward fall in the acquiring firm's profitability performance in the post-merger periods as compared to the pre-merger period.
- Growths in both turnover and assets have been in continuous sharp decrease since the merger. The reverse was the situation during the pre-merger period except in the second pre-merger year when turnover decreased significantly.

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- Liquidity has been in continuous decrease since the pre-merger period, the decline being deeper during the first two years after the merger. However in the third post-merger year liquidity started to improve, with a significant rise.
- Financial leverage was higher after the merger than it was before the merger. At the same time the company's credit potential was higher during the post- merger period, as the ratio of total liabilities to total assets fell.
- While general, selling and administrative expenditure has experienced a downward fall, interest charges has increased significantly and total operating expense started to increase significantly in the third post-merger year.
- Earnings per share increased significantly throughout the study period except in the third post-merger year when it started to decrease. The increases were sharper in the first and second post-merger years. Dividends per share were increased continuously throughout the period. However the increase in the third post-merger year was marginal. These increases occur in the face of declining profitability and turnover growth rate.

Conclusions

Generally, the merger has not brought about the expected improvement in corporate profitability and other financial performances, except the increases in EPS and DPS, three years after the merger. Factors contributing to the declining accounting performance after the merger were the poor financial

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performance of the acquired firm (former GBL) prior to the merger, intense competition in the brewery industry and worldwide rising cost of cereals (raw material for malt), energy and water. The recent power crises in Ghana and water shortages, particularly in Accra, readily come to mind in this regard. Other contributory factors were high interest payments on overdrafts and loans, used to finance working capital and the merger itself. All these led to the high operation expenses and financial leverage. Additionally, management of the acquiring firm was encountering difficulties integrating and coordinating operations of the two previous entities.

It is however important to note that since the profits margins and sales growth rates are positive, it means that in absolute terms the post- merger profits levels of the merged company are higher than the pre-merger levels of the acquiring company (though the rate of increase is in continuous decline). Hence the post- merger increases in earnings per share, which may have been the basis for the higher post-merger dividends. These dividends may have been meant to sustain the interest of shareholders and investors in the company and to engender their support for management. However the share price increase is relatively less in the post-merger period than in the pre-merger era. Evidently, the EPS and DPS are likely to be unsustainable, if the decreasing trend in profitability and other accounting performances continue.

The increasing EPS and DPS in a situation of deep declining profitability and sales growth rates may confirm the argument by Pierson et al (1990), that expressing the effects of corporate financial objectives in terms of growth in earnings per share (EPS) or price earnings ratio (P/E ratio) is unreliable. They argue that although an economically viable merger should

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lead to an increased EPS for the acquiring firm, it is possible to design a merger which produces no economic benefits but which nevertheless produces an immediate increase in EPS.

These results suggest that the accounting performance of GGBL confirms the general expectation of future improvements in the operations of the acquiring firm (GGL). As suggested by Kitching (1967), the mere existence of potential synergism is no guarantee that the combined operation will realize the potential. Thus although the objectives of the merger were to reduce cost of operations and enhance market power and profitability of the joint operations, the attainment of these objectives is still in a balance. Thus the overall conclusion is that the expected financial performance benefits of the merged company so far remain elusive.

Recommendations

Guinness Ghana Breweries Limited should strengthen its business processes to enhance productivity and turnover, reduce cost and improve efficiency of operations. The company should restructure its capital base and improve its cash operation cycle to help improve cash flow, reduce the level of short-term borrowing and yet meet working capital requirements. Specifically, it should:

- issues more shares and possibly long term debt securities, to improve cash flow, eliminate or reduce overdrafts and medium term loans so as to reduce interest and loans payments (at least in the short term). These will lead to operation cost reduction and improvement in profitability.

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- improve debts collection and sales and distribution to improve cash flow and reduce borrowing and level of interest payment. For instance, the company could negotiate with distributors (customers) and suppliers (creditors) to reduce debtor's collection period and extend creditor's payment period respectively. Similarly, marketing, sales and distribution activities could be intensified.
- ensure more effective integration of operations and cultures of the two previous firms to improve operational efficiency and productivity.
- review business and production processes to identify and rectify possible bottle-necks.

The above recommendations should be implemented with the aim of putting the company in a stronger position to meet future competitive challenges, reduce operation cost, improve liquidity, profitability and general business performance and at least sustain shareholder earnings and value.

Limitations and direction for further research

The findings in this study may not stand the test of being truly representative due to the fact that only one merger event has been investigated. Studies of this nature normally use a sample size of not less than ten (10) companies. The results obtained from this study are therefore limited. The study is also limited due to the fact that the time available for this study was too short to do thorough work. Additionally, the results could be influenced by some possible extraneous variables like sudden changes in the socio-economic and or business environment that the research did not cover.

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For instance some of the differences between pre-merger and post-merger performances may result from the effects of economy-wide and industry factors. It is therefore necessary that the firm's performance measurements be adjusted by the industry averages. The absence of industry averages for the brewery industry in Ghana is therefore a limitation to this study. Future studies of the impact of mergers on corporate financial performance should therefore take the industry averages into consideration. In future studies, the industry-adjusted performance measures should be computed by subtracting the industry average from the sample firm's values.

These weaknesses notwithstanding however, the findings will be useful to any researcher who will use them as a starting point for further research, and to shareholders, investors and other stakeholders of the sample company in their decision making.

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APPENDIX A

INTERVIEW GUIDE ON THE GGL AND GBL MERGER

UNIVERSITY OF CAPE COAST

SCHOOL OF BUSINESS

DEPARTMENT OF ACCOUNTING AND FINANCE

Introduction: This interview seeks to gather relevant data on the impact of the merger on the corporate performance of Guinness Ghana Breweries Limited, in partial fulfillment of the requirement for the award of MBA. Please feel free to me as objective and truthful answers as you can. The interview is for academic purpose only and your response will be treated with the utmost confidentiality.

1. Please when was the merger completed?

....

2. Who were the major shareholders of GGL and of GBL before the merger?

GGL……………………………………………………………………….

…………………………………………………………………………..

GBL…………………………………………………………………………..

…………………………………………………………………………..

3. What were the major reasons/ objectives for the merger?

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4. Would you say that the objectives as stated above have been achieved?

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a) Objectives have been achieved

b) b) Objectives not been achieved

c) Others ………………………………………………………

………………………………………………………………

5. Could you please explain to me the reason(s) why you think the merger objective(s) have been/have not been achieved?

…………………………………………………………………..

……………………………………………………………………

…………………………………………………………………...

…………………………………………………………………...

6. Which of the merging companies was the acquirer and which was the target (acquired)?

a) Acquirer ……………………………

b) Acquired ……………………………

7. What were the terms on which the merger was negotiated?

……………………………………………………………………

……………………………………………………………………

8. To the best of your knowledge what were the terms of payment to

a. Cash payment?

b. Payment with shares of the acquirer?

c. A combination of cash and shares of the acquirer? or

d. Some other term you could explain to me?

……………………………………………………………………

…………………………………………………………....................

9. Did the merger have any effect on the size of the workforce of the

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company? Yes No

10. If yes to (9) above then, please what is the nature of the effect?

………………………………………………………………………………..

………………………………………………………………………………..

11. Was there any resistance to the merger? Yes No

12. If yes to (11) above, then by whom? and what was the reason(s)

……………………………………………………………………………….

……………………………………………………………………………….

………………………………………………………………………………

13. Did the exchange of shares (if it happened) cause any change in shareholders rights?

Yes No

14. If yes to (13) above, then please what were the changes?

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15. In your view why are mergers and acquisitions not common in Ghana?

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