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THE EFFECTS OF THE MERGER OF UNITED NIGERIA TEXTILES PLC AND NICHEMTEX INDUSTRIES PLC ON PROFITABILITY

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ABSTRACT

Why do companies merge? Why are some mergers successful and others not? What is the effect of the 2001 merger of United Nigeria Textiles Ple and Nichemtex Industries Ple on the overall profitability of the group? In finding answers to these and other similar questions, the paper compares five (5) year pre-merger profitability (represented by Earning Per Share, EPS of hed Nigeria Textiles Ple with five (5) year post-merger profitability. Using paired sample test statistic on EPS before and after the merger, it was found that the mean EPS before the merger was 56.66 Kobo compared with a mere 450 Kobo after the merger. The difference of 51.86 Kobo loss is significant at 0.430, thus making it insignificant at 5 per cent. What this means in effect is that the merger has not resulted into an increased profitability at least in the short run. The finding here is quite in agreement with earlier research works on mergers which revealed that mergers, more of the time, do not result in improved profitability or capital appreciation of the acquirer organizations in the years immediately preceding such mergers.

Keywords: Merger, Profitability, Earning Per Share.

INTRODUCTION

Mergers and Acquisitions are methods of business combinations whereby one business gains control of one more businesses (Elumilade and Oladoyin, 2004). There are reasons for their occurrence but they are ally to enable advantages to be gained or disadvantages to be avoided.

The industrial set-up in the country, according to Sanni et al (2008), has been greatly affected by either stiff competition among local competitors or foreign companies that dump their goods into the economy. The present economic recession, according to them had also forced government to introduce some stringent measures in order to revamp the economy.

To really survive, companies do purposely undergo restructuring programmes. In order words, it is believed that mergers take place when the economy starts playing rough on companies, presenting a gloomy future. The first alternatives opened for the survival of firms, according to Sanni et al (2008), is to invest in new capacity. It can put resources into research and development, and it can spend on marketing its products. In each case, the firm acquires and organizes new factors of production. This is called internal growth.

Adereti and Sanni (2007) observe that takeovers are an important aspect of the corporate environment. Over the past three decades, United Kingdom's listed companies have spent billions of pounds on acquisitions. In most instances, the rationale of the acquirer is based on the promise of increasing shareholders' wealth from a variety of sources, ranging from greater synergy from the combined organizations to the replacement of under-performing managers. Regardless of the justification, the overriding argument put forward by managers is that takeovers result in greater corporate efficiency and, ultimately, in wealth increases for shareholders in the acquiring company.

In practice however, the promised gains to shareholders in acquiring companies are not easily identified. A stream of empirical researches has examined the post-acquisition performances of bidders and has generally failed to find consistent evidence of improvement in shareholders' wealth after acquisitions. These findings appear to hold in the short run and in the long run. From a management perspective, these findings are troublesome and raise important questions about the wisdom of takeover activities. Despite the disappointing evidence on bidder's performances, there is no evidence that past failures to generate positive shareholders returns has had an impact on the volume and acquisition activities.

The primary objective of this paper is to examine the effects of the merger of United Nigerian Textiles Plc with Nichemtex Industries Plc on the profitability of the group.

The rest of the paper is divided into five sections. Section two is on brief historical background of the case with Nichemtex Industries Ple on the profitability of the group. study. Section three reviews related literature on the topic. Section four is on research methodology and model specification. Section five focuses on findings and discussions while section six summarizes and concludes the paper, while at the same time bringing out the policy implications.

HISTORICAL BACKGROUND

Nichemtex Industries Plc. The company was incorporated on 3 August 1971 as a private limited company. It was later converted to a public company in May 1990. The principal activities of the company are the manufacture and marketing of textile materials such as real wax and polyester cotton blended fabrics. The shareholders' funds of the company stood at N2.9 billion when it merged with United Nigerian Textiles Ple in 2001.

United Nigerian Textiles Plc.

The company was incorporated on 7 May 1964. It is engaged in the manufacturing of textile materials. It major product lines consist mainly of real wax and superb prints textile materials. Fifty-seven percent (57%) of its issued share capital is held by overseas interests while the balance of forty-three per-cent (43%) is held by the Nigerian public. The company merged with Nichemtex Industries Plc (a company in the same business) on the 13 of November 2001 by the issue of 13 of its shares for every 5 shares to the shareholder of Nichemtex Industries Ple and the transfer of the assets, liabilities and undertakings including real property of the other company.

The market share price of the company, which was 291 Kobo in 2001 (year of merger), increased marginally to 326 Kobo in 2002 but plunged downwards to 91 Kobo in 2006.

REVIEW OF RELATED LITERATURE

There are many studies on the effects of Mergers and Acquisitions (M&A) on employment structure of the organizations and financial performances of the acquirer organizations (Sanni and Akinpelu, 2006:4).

The study of Conyon et al (2002) indicates that M&A significantly reduce the demand for labour in the UK in the years following the acquisition. Licttenberg and Siegel (1990), using comprehensive analysis of thousands of US manufacturing plants conclude that the job losses after merger are largely confined to central office staff. McGuckm et al (1995), as cited by Sanni and Akinpelu (2006) find increased employment in acquired plant and insignificant effects in firms' level of regression for the US.

It was confirmed by the studies of Shliefer and Summers (1998) that M&A often go hand in hand with substantial restructuring and even closure of divisions within the combined entity.

There are many studies on the effects of M&A on financial performances of merged organizations. Singh (1971), in a sample covering the period 1955-1960 found that two-thirds of the seventy-seven companies which acquired other companies in the same industry had lower profits in the year after merger than in the earlier years. Utton (1974) selected a sample of thirty-nine frequent acquirers in the period 1966-1970, For both periods, the average profitability of the sample was lower than that of the control group. Utton (1974) concluded first that companies which had relied heavily on external expansion had a lower profitability in a subsequent period of internal expansions and second, that the profitability could be maintained more readily in companies which demonstrate a slower growth rate, but rely on internal rather than external expansion.

The study of Meck (1977) was based on a sample of 233 large listed companies in the UK, which merged between 1964 and 1974. The merger profitability (the average of the three years profitability prior to the merger) was estimated for the merging companies and was compared with after the merger, having 'standardized the profitability in relation to the average profitability of the appropriate industrial sector. The outcome of the study shows that apart from the merger year itself, profitability declined on an average and between one-half and two-thirds of the companies experienced a decline in profitability in each year after merger.

Management and Administration, Volume 4, Number 3, 2009 Newbould (1970) revealed that after two years, seventeen out of thirty-eight companies in the sample reported no benefits were anticipated within the next five years. Thirty per cent of UK acquisitions were failures, concluded kitching (1974)

Why do companies merge?

Ogunbi and Ogunseye (2004) listed some of the reasons why companies merge. These are: The desire to achieve economies of scale through increased purchasing power by way of discount.

The desire to obtain access to effective research and development resources thereby providing a sustainable ability to compete in the future and enhance further growth.

The desire to diversify. If two risky assets, which have less than perfect positive correlation, combine, then, the total risk of the combination will be less than the weighted average of the total risk of the two assets. The greatest benefit from diversification can be obtained by combining companies, which are in different industries (that is, conglomerates).

The desire to use surplus cash. If a company has a large amount of surplus cash, which it cannot invest profitably, it may attract take-over bid from a company in dare need of cash.

The desire to achieve greater financial stability by large organizations is likely to command better credit ratings for easy attraction of new finances.

The desire to enter a new industry within a short time.

The desire to achieve market dominance.

The desire to safeguard sources of raw materials.

Ability to contract competition from new areas or products.

The desire to claim all outstanding tax allowances.

WHY SOME MERGERS FAIL

In a major study of post-acquisition performance of acquired companies, Elumilade and Oladoyin (2004) observed that many companies were acquired and, on average, their profits and market shares declined following acquisition. Some of the reasons advanced by them include but not limited to the following:

Difficulty with post-acquisition integration. Evidence has shown that having made an acquisition, the acquiring company has to integrate the acquired business into its own organizational structure. This may not be easy to achieve.

Overstating Economic Benefits. Quite often the strategic advantages that can be derived from a merger may be overstated, thus making the acquirer to pay more for the target company than it is probably worth.

The expense of acquisition. It has been observed that acquisitions of companies whose stock is publicly traded tend to be very expensive. When a company bids to acquire the stock of another enterprise, the stock frequently gets bidded up in the acquisition process. This is particularly likely to occur in the case of contested bids, in which two or more companies simultaneously bid for control of the target company. Thus, the acquiring company must often pay a premium over the current market value of the target.

The best bench mark of judging the success or otherwise of a merger, according to Adereti and Sanni (2007). might consist of a financial performance index based on a set of matched firms in the same industry that did not go through a merger event. Pautler (2003), referring to several consulting firms' commissioned surveys concerning the outcomes of recent mergers since mid-90s identified three questions the surveys were used to examine: first, did the mergers tend to achieve the goals and objectives of the executives involved in the deals? Second, on a more objective basis, did the deals enhance shareholders' value relative to industry benchmarks? Third, and perhaps the most important to the consultants, what were the characteristics of the more successful deals compared to those of the less successful deals?

Why mergers succeed

Adereti and Sanni (2007) listed some factors that help in achieving successes in mergers. Some of them are listed below:

Mergers that retain the main focus of the firm result in better outcomes. Bower (2001) opined that better outcomes of mergers in the same or related industries might be due to the possibility of scale or procurement gains.

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Mergers of equal-sized firms work less often than others Ravenscraft and Scherer (1987) found mergers of equals worked better than less equal deals. In their sample, the mergers of equals tended to be conglomerate in nature.

Early planning for the integration of the new physical and human assets improves the chances of success.

Fast-paced integration and early pursuit of available cost savings improves outcomes.

Managers must designate the merger integration leader and provide appropriate incentives.

Managers must be cognizant of the cultural differences between organizations and avoid conflicts in part, via frequent tailored communications with employees, customers and other stakeholders.

Particularly in mergers involving technology and human capital, manager must retain the talent that resides in the acquired firm.

Customers and sales force attrition must be minimized.

The degree of autonomy given to the acquired organization's management team. Weber (1996) found that the removal of management autonomy was positively related to post-acquisition performances in manufacturing firms but negatively related for takeovers involving banks. He argued that the negative effects of autonomy removal are felt most strongly in human-capital-intensive industries whereas the benefits of synergies may dominate in manufacturing outfits.

Industrial relatedness of the bidder and the target. According to Tuch and O'Sullivan (2007), an important motivation for takeover activity is the potential for synergies between the bidder and the target that are expected to result in efficiencies which should ultimately provide positive returns for the shareholders. The potential for such efficiencies is less easily identified in the case of takeovers where different industrial sectors are involved.

After taking cognizance of the factors that determine financial success of mergers and acquisitions, Pautler (2003) observed that a merger can be a financial failure, but a success in a societal sense, if it reduces the use of real resources in producing output or if it results in better products or more diverse choices for consumers. For the most part, one would expect financial results and social outcomes to coincide but if a firm over-pays for the assets or if rivals quickly copy and surpass a merging firms' innovation, the merger might be socially successful but a financial failure.

RESEARCH METHODOLOGY AND MODEL SPECIFICATION

Research methodology

The paper made of secondary data obtained from the Annual Report and Accounts of the companies used as case studies. The data obtained are mainly EPS before and after the merger.

The statistical method employed for test of the hypothesis is paired sample t-test. This is because among other uses, the t-test is a statistical tool used to test the significance of the difference between two sample means observed at two points in time (Carver and Nash, 2000).

The paper tested only one hypothesis in its effort to make the research objective achievable. This is:

Ho: The merger of United Nigeria Textiles Plc and Nichemtex Industries Plc has no positive effect on their profitability. Hi: The merger of United Nigeria Textiles Ple and Nichemtex Industries Plc has positive effect on their profitability.

Model Specification

As earlier stated, the test of significant difference between two means carried out with calculated t-value

$$t_{cal} = \frac{Ma - Mb}{\sqrt{\frac{Va}{Na} - \frac{Vb}{Nb}}}$$

Where:

Ma = Mean of EPS after the merger.

Mb - Mean of EPS before the merger.

Va=Variance of EPS after the merger.

Vb =Variance of EPS before the merger.

Na Number of

Nb Number of after the merger before the merger The calculated P-value (significance level) is compared with 0.05 level of significance

Decision Rule Accept Ho if

Calculated Pavale >0.05

Reject Ho if Calculated P-value 0.05

FINDINGS AND DISCUSSIONS

As can be observed from Table 1, the mean EPS of United Textiles Pie is 4.40 Kobo alter the merge This it far less than 56.66 Kobo before the merger. The correlation of the paired samples (Table 3) is 0018 at 0.977 significant level, meaning that the negative correlation between the paired samples is not signi 59% significant level. The mean of the paired sample test (Table 3) is 51 86 Kelso (loss) with 0.87 value. It is significant at 0.430, thus making it insignificant at 54 significant level. Thus, we refine to reject He and therefore conclude that the merger of United Nigeria Textiles Tie and Nichemtex Industries Pie has no positive effect on the profitability of the combined entity.

Table 1: t-test.

	Mean	**N**	**Std Dev**	**Std Error**
Pair After	4.8000	5	80.6424	36.0644
Before	56.6560	5	103.4001	46.2419

Source: Computations from SPSS

Table 2: Paired sample statistics.

	N	Correlation	Significance
Pair 1: After and Before	5	-0.018	0.977

Source: Computations from SPSS

Table 3: Paired Sample Test

	Mean	Std Dev	Std Error	t	df	Significance
Pair 1: After - Before	-51.8560	132.2655	59.1509	-0.877	4	0.430

SUMMARY AND CONCLUSION

The paper looks at the effects of the merger of United Nigeria Textiles Plc and Nichemtex Industries Pie on profitability of the combined entity. Merger, it was seen, takes place when business plays rough. It is entered into because of the advantages to be gained or the disadvantages to be avoided his sad however to ste that not all mergers are success stories. Some mergers fail, among other reasons due to wrong choice of merger partners or over-estimation of benefits that will accrue. Mergers of equal partners particularly in the same industry lead to improved profitability.

As for the companies used as case study, the pre-merger mean LPS of United Nigeria Textiles Plc declined from 56.66 Kobo to a mere 4.80-post merger EPS. The paired sample test mean of 51.86 Kobo (loss which is significant at 0.430, is not significant at 5%. This means that the merger did not revolt into increased profitability, at least in the short run. The finding here is quite in agreement with earlier research works which revealed that mergers more of the time do not result in improved profitability or capital appreciation of the acquirer organizations in the years immediately preceding such mergers (Singh, 1971, Utton, 1977, Ravenscraft and Scherer, 1966, Bekiar et al, 2001, Sanni and Akinpelu, 2006 Sanni, 2007 and Sanni et al, 2007)

POLICY IMPLICATIONS

The merger of United Nigeria Textiles Ple with Nichemtex Industries Plc, like other mergers was done with high expectations. It turned sour due to a number of factors. First was the problem of over-valuation. For every five (5) ordinary shares of Nichemtex Industries Plc, thirteen (13) shares of United Nigeria Textiles Ple were issued. For a company not listed in the Nigerian Stock exchange to be so valued might have been due to the fact that the same person holds the bulk of the shares in both companies.

Then, a lot of macro-economic and political factors beyond the power of the two companies cropped in. The textile industry as a whole fared badly from 2002. According to Cha (2002), many textile mills closed down as a result of high manufacturing costs due to increased wages, unreliable and unstable electricity supply, scarcity and escalating prices of black oil/diesel, as well as, cotton lint. United Nigeria Textiles Plc particularly suffered from myriads of problems affecting the textile industry. Its performance was not only undermined by the smuggled cheap textiles from Asia, but also by the problems of unfair competition from products using the company's brand- name, resulting in confusion regarding quality and prices of the company's goods in the market place (Cha, 2002). The outlook of the textile sector is not promising as rightly pointed out by Yusufu (2006).

The problem in the industry was highlighted in a release jointly issued by Esele and Kolawole (2008) of the Trade Union Congress of Nigeria (TUC). According to them, the textile sector faces extinction due to lack of black oil to power its plants, coupled with poor and erratic power supply by the Power Holding Company of Nigeria (PHCN). They also identified government's refusal to disburse the N70 billion textile revival funds to ailing factories as one of the major problems militating against the revival of the sector. They lamented the spate of smuggling and dumping of banned substandard textile materials in the country and called on the men and officials of the Nigerian Customs to be alive to their responsibilities and halt this menace.

The policy implication is that this company may be liquidated due to circumstances beyond its control. And if this happens, the 8,845 workers in its fold as at December 2006 (10,222 in 2005) may join the already saturated labour market. For this not to happen, the Federal Government should address some of the problems identified in this paper. It should also implement the projects under the Textile Development Fund as rightly suggested by Yusufu (2006).

But very worrisome is the view of Isueli (2008) on the release of the Fund. According to him, the revival fund is commendable but the funds may not revive the sector as the sector is faced with infrastructure problems. The sector, according to him, had over 20 moribund companies and in the past had sent over 200,000 people into the labour market. Inconsistency in government policies was also identified as one the basic issues that need to revive the sector (Imhonlele, 2008). To Hunsu (2008), the problem of inconsistency in government policies is one basic issue that needs to be resolved, especially policies concerning the textile industry. The problem has gone beyond money, he said.

One of the limitations to this work, which must be pointed out is the fact that the paper did not take into consideration the effect of inflation/time value of money.

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