ISSN 2278 – 0211 (Online)

Integration Strategy and Organizational Performance: A Case of Vertical Integration

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Abstract:
Vertical integration has been common as way of pulling resources for sustainability and synergy of the organization. The paper investigate vertical integration as mode of bringing resources and increasing economies of scale. General objective It was based on the following specific purposes; To evaluate the effect of human resources integration in mergers on organizational performance;organizational culture integration, leadership integrations and market integrations in mergers on organizational performance. The paper adopted the oligopolistic, free cash flow, and Size and Return to Scale Theories. The paper used descriptive research design. The study targeted population of 6 managers and 47 employees of Faulu Micro-Finance and Old Mutual Integration. Census was used in the research where structured questionnaire were used. Pilot study was conducted prior to the field data collection in order to determine the reliability of the research instruments used and content validity was also tested through passing the questionnaire to experts. Descriptive statistics was used where mean and standard deviation was interpreted appropriately. Regression analysis was also used to provide inferential statistics. The findings' indicated that HRM and marketing integration strategies provided positive significant improvement in performance. The organization and management provided positive improvement but not significant among the four integration strategies. The result also found positive correlation between integration strategies and performance of the organization.

Keywords: *Strategic Management, vertical integration, descriptive design, Kericho, Kenya*

1. Introduction

Many firm compete amongst themselves through taking customers, market share and turnover of sales. Globalization have brought dynamic changes in information system and new approach in management and strategies in order to survive the competition in their industry sector. Hence they are forced to look for strategies and make viable decision that increase the organization performance. The strategies that are common used include TQM, innovation and technology, marketing, integration, competitive advantage and corporate strategies. Integration through merger and acquisition are some of the strategies deployed no only to increase productivity but for the merging firm harvest core competence, economies of scale and increase market share.

Researcher and scholars have over decade investigate on the integration. Hence there are numerous view and ideology that combine to ensure successful integration. Integration has been mired by problem and challenges. This challenges includes human factors, government policies, economical factors, micro and macro economical dynamics, technological and managerial factors. Manzini and Gridley (1986) added that these challenges in merger and acquisition leads the organization no to achieve their objective, inadequate human resource, unprofitability, and poor performance of products in the market.

The organization need to learn do thorough research in the merger and acquisition before any course of action. They need to consider also which type of integration will suite the organization at the point in time, since factors of affecting integration change with time. Also if they would diversify their business or continue in one line of production. Vertical integration is most highly considered among the integration strategies. It has conveniences in ensuring that the right raw material are sourced with the right quality until the product or service is full developed or distributed. This strategy not only increase production levels but also ensures that the products are sourced cheaply by eliminating the suppliers, agents, hence reaping all the profit all through reducing the final cost. This gives room for advancement in technology and encourage the firm to produce variety of products based on technology as well as the scope of economies attained through integration. According to Besanko *et. al*,(2007) added that integration enable firms to improve the market share and business at a reduced cost which is attained as result of the economies of scale and scope. Diversification can also encourage region spread of the

organization as result of integration. The organization can transfer or increase in operation to a wider region or can even grow to global market. This leads to large market share that before in international diversification strategy (Hitt et. al, 1997).

Zollo and Singh (1998) argued that corporate acquisition are not frequent, with different characteristics and complex in nature which becomes a lesson after the process. Merger and acquisition of organization has numerous impact on the people. The perception needed when joining a different group leads to discontinuity of the original organization culture and identity therefore have a negative influence on employee performance and sense of belonging (Van Knippenberg et al. 2002).

The idea behind vertical integration as where two firms are vertically associated when one organization can use the output of another organization. Sudarsanam (2010) noted that it is rare to find vertical merger as related with one of horizontal and diversifying mergers empirically. Vertical and horizontal integration has shown that vertical merger has greater benefits than the horizontal merger.

Performance has been a problem to many organizations, many set targets they are not able to meet. Most organizations have been driven to costly undertakings like employing services of consultants. That is why in my topic I want to look at Integration as one of the strategies companies use to improve organizational performance.

2. Literature Review

The literature based on the theoretical and conceptual review indicated variant results with wide view of vertical integration. The findings also showed different result based internal and external environment of the integrating firms.

2.1. Theoretical Review

Theoretical review relates to different concepts and postulate that build the foundation of major source of knowledge. The free cash flow theory, oligopoly theory and Size and Return to Scale Theory.

2.1.1. Free Cash Flow Theory

Free cash flow theory was developed by MC Jesen in the year 1987. Diverting excess funds from the shareholders assist organization from running to capital market which increase risk based on new equity motoring in stock market (Easterbrook, 1984). By doing so the organization are able to avert risk relating takeovers by increasing the size of the organization (Jensen, 1986).Manager may redirect free cash flows from misuse is by increasing the size of the company and enhancing power and abilities. There exist different expectation between shareholder and managers. One way the manager wants to divert besides dividends is issuing of debt and promising to pay future cash flow.

The theory relates to financial improvement as result of integration strategies. Shareholders benefit is affected by the diversification of free cash flow which affect the profitability of the firm. This is because ROE measure organization profitability by indicating how much profit was attained by the firm accordance with the funds contribution by shareholders. Hence profitability is determined by the level of sales.

2.1.2. Oligopolistic Theory

The theory of oligopoly was developed originally by Paul Sweezy in the U.S.A, Hall R. and Hitch C. in the U.K in 1939.Oligopolistic structure may arise as result of merger which was addressed as "oligopolistic reaction" (Knickerbocker, 1973). He defined oligopolistic structure as an organization behavior where large few rival organization compete with each other using similar strategies. Hence is two oligopolistic firms integrate others may react by integrating. The concept is inconsequential of will happen after merger to shareholder and other stakeholder. The merger can happen in continuous chain reaction and hence proof the studies conducted that integration happen in a waves. In the case of petroleum firms in Kenya, different firms has been merging in order to improve financial performance of the firms. Consequently, rival firms are engaging in mergers and acquisition deals as their competitors in order to realize these oligopolistic goals. Similar moves are possible in sales techniques, Market Share and output.

2.1.3. Size and Return to Scale Theory

The concept has been discussed by several scholars including Knut Eicksell, Wicksteed and Hicks from 1990s.Size increment is related to the organization "synergies". Merger and acquisition involve two or more companies joining forces to increase performance but it also increase the size of the industry both in financial capability and resources. The total gain or synergy of firm A and b of share equity is positive and more valuable than there separate organization. Hence synergy is given by Synergy= contribution of both firm A and B – (Firm A + Firm B). Benefit is obtain when the cash flow from the integration provide a positive synergy. The new integrated firm will remain the same if the synergy is zero and it becomes uneconomical is synergy is negative. In terms of large firms the average cost decline as result of integration leading to the high profitability. Efficiency is also attained through the merger and acquisition since the two firms support there weakness in resources. This mean integration that with improve economies of scale given by reduction of average production cost per unit product or service. If the unit cost reduce per product or service drop then the economics of scale benefit the organization. Due to the integration the operation cost due to merger of facilities, management, staff and resources will be reduced and the increase in productivity generated by economical of scale. Hence high performance is experience in the organization.

2.2. Integration Strategy

The integration strategies were given by human resource strategy, organization integration, management integration and marketing integration.

2.2.1. Human Resource Strategy

Integration of two or more organization involves human capital and relationship should be forged in so that efficiency and new culture is established (Walsh, 1989). It is important for the top management to enable the human resource undergo change so that they are able to transform the new integrated organization. Mergers and acquisition value addition highly depend on the integration process. Integration is a challenging experience since the organization will need to integrate all the function which include human resource integration. Failure in the process of integration are dependent on the management of the process. Mismanagement leads to failure hence it is important that human resource management be well established and integrated. Amiot *et al.* (2006) propose that there should be alignment of human resource strategies with the detail and process of the merger. According Papadakis (2005) he added that the communication is important and should be consistent and clear for efficient transition in the integration process. Buono and Bowditch (1990) also agreed that communication must be direct, consistent and certain. The knowledge from Hunt and Downing (1990) added that the communication should be clear, reliable and consistent in the integration process.

Qureshi et al. (2011) noted that performance in organization that has merged of acquired is dependent on the HRM management. Human resource is view a perspective since with poor management of HRM in a merger or acquisition leads to poor performance.

Many scholars including Schuler (1992) have argued that integration provides a large range of intervention to complex firm's challenges; this where all functional structure from finance, HR and technology are assessed so that the desired output in the integration process is attained and; HR provide positive influence to management decision (Lengnick-Hall and Lengnick-Hall, 1988). The degree of integration has often been measured in terms of HR managers' representation on BOD, involvement of HR manager in business strategy development, and the existence of mission statement and business strategy (Budhwar, 2000; Chung and Huang, 2005; Schuler, 1992). Similarly, evidence suggests that in order to integrate HR strategy with business strategy and to achieve organizational performance, there must be an explicit or implicit form of HR strategy, translation of HR strategy in clear set of work programs and clear policies on a range of HRM practices (Cook and Armstrong, 1990; Delery and Doty, 1996; Dietz et al., 2004; Mills, 1985). There is consensus in the literature that there are advantages to be gained from the integration of HRM with business strategy

Schuler and MacMillan (1984) believe that an effective HRM increase firm's profitability. They proposed that strategic integration has direct impact on HR outcomes, followed by organizational, financial and capital market outcomes. Huselid (1995) had found that those organizations that link HRM practice to strategy reported higher financial performance outcomes. Youndt et al. (1996) support this type of fit, more particularly with respect to the fit between HRM practices and a quality strategy. Arthur (1994) compared two HRM strategies and found that the commitment approach resulted in greater labor efficiency and lower scrap rates. Literature concludes that HRM practices can help to create a source of sustainable competitive advantage for companies, especially when such practices are aligned with the firm's business strategy (Jackson and Schuler, 1995; Porter, 1985; Schuler, 1992; Wright and McMahan, 1992). It is possible that the close integration of HRM with business strategy leads to heavy emphasis on cost reduction (Brewster, 1999). Firms that achieve a tight vertical fit between strategy and HR management perform better than their counterparts who have a disjointed linkage (Truss and Gratton, 1994).

2.2.2. Organizational Integration

Dr Porter (1985) created a framework on value chain this linked the buyers and suppliers and the functional unit of the organization. The integration of organization do impact on the organization structure and hence the value chain. Hence the supply chain of the organization need to be overhauled to capture all the needs integrated organization.Lawrence and Lorch (1968), referred integration as the state interrelationship among various department in order to enforce unity in the organization through collaboration. It narrowed internal integration but Porter referred it to go beyond the boundaries of the organizations. Porter looked not only to the buyer influence to integration but also other stakeholders including suppliers in the supply chain (Vickery et al., 2004; Swink et al., 2007; Frohlich & Westbrook, 2001).

According to other scholars (Koufteros et al., 2005), also supported the Porter's ideology that it both internal and external orientation of organizational integration with the as noted by Lawrence and Lorch (1968) and Porter (1985). The Lorch and Porter noted that concept and strategic are crucial in merger and acquisition. As it note that organization integration is more of networking and collaboration among organization functionality and partnership between buyers and suppliers.

Many scholars done relate the integration and organizations' performance (Paulraj & Chen, 2007; and Koufteros et al., 2005). They argued that firm with more internal and external integration are able to review on the performance since there exist a network between the internal and external collaboration between each other than the counterpart of which have not integrated. Suppliers involved with process integration has assisted that cooperation, innovation and solving problem (Frohlich & Westbrook, 2001), which has enable the organization to complement knowledge resource (Koufteros et al., 2007).

These studies argued that with lack of internal and external supply chain integration assist in performance (Flynn, Schroeder, & Flynn, 1999; Clark 1996).

2.2.3. Management Integration

Management participation and role is very critical in the process of integration. Management integration is defined by the activities to the right constitution the right personnel and management strategies in order to finish the task. Hence is provide strategic management concept that enable decision making and the right management team is necessary for it success. According Buono and Bowditch (1990) argued that team spirit is needed rather than autocratic leadership style in management integration. This more like change management process and the more there is friction the unsuccessful the integration is. Participatory leadership would ensure integration of decision. Marks and Mirvis (2012) defined the role of leadership as to provide direction in human, cultural and organizational to the integration process by gathering all of them to work cooperatively on tough combined leadership. Working together between the two or more integrating groups allow quick integration process. Also quality would also improve besides quick integration process (Homburg and Bucerius, 2006).

Sudarsanam (2010) gave an account on vertical merger and acquisition combines successive tasks in vertical chain to form as single organization. According to Besanko et.al, (2007) vertical integration deals with task that organization within its boundaries, compared to the purchase from independent organization in the market. It means that one organization is formed from two or more independent organization rather than sourcing process from other firms or contractual deals or lengthy market based transactions. It then internalize most of the process without sourcing reducing cost formed by distance, time wastage, capital synergy and cost factors that would have existed between the two firms before vertical merger.

According to Besanko *et al*, (2007) iterated that vertical integration has been more frequent rather than the use of independent suppliers or agent. This is enable the organization to control the choice or source of raw materials and control production distribution at the same time as the market demands. New technology in the production unit provide new opportunity to scope economy these ensure that numerous variety and in larger quantity can be produced compared to be produced separately, which enable them to horizontally to integrate. Besanko *et al* further suggested that diversification can be vertical or horizontal depending on the need and aim of the benefactor or the integrating firms. Horizontal just like vertical reduces production cost, improve market effectiveness through the development of both economic of scale and scope.

2.2.4. Market Integration

Marketing integration is customer oriented where the customer are involved in the integration process through information sharing and knowledge on the products changes, quality, cost, delivery time, product performance. Customer integration as other scholars puts like (Swink & Song, 2007; Vickery et al., 2003; Frohlich & Westbrook, 2001), and agree that customer integration is the external and vertical network to the organization where the customer is end user in the vertical chain. It is then very crucial to maintain a close linkage and collaborative connection between the integrating organization and the customer so that both organization main customer are maintained (Stank et al., 2001), this ensure larger market share (Swink & Song, 2007), and provide greater innovation from feedback from the customer on the changes made and products (Urban & von Hippel, 1988; Koufteros et al., 2005;).

Positive relationship between communications on integration process has been found in major studies like (Gupta, Raj, & Wilemon, 1985). It is then important to ensure harmony between functions generated through inter-functional integration (Souder, 1988). Coordination is found to be important in the integration strategy (Gupta & Wilemon, 1990) that will ensure market orientation integration.

3. Research Objective

The paper investigated integration strategy on organizational performance. It was provided by the following specific objective which were to investigate;

- Human resources integration strategy on organizational performance
- Organizational integration strategy on organizational performance.
- Management integrations strategy on organizational performance
- Market integrations strategy on organizational performance

4. Methodology

This study was conducted using Descriptive and exploratory research designs. A case study of Faulu Micro Finance Bank-Old Mutual was used. The research used primary data obtained from the Faulu Microfince found in Kericho County. The study targeted a population of 6 Managers and 47 junior staff of Faulu Micro-Finance Bank (management records, 2016). Census was used based on the fact that population was small. Questionnaires were appropriate based on the study concerned could not be observed but characteristics, opinion, feeling and perception could be inquired from the respondents. These enable the researcher to collect both quantitative and descriptive data the described the influence of mergers and acquisition on organization performance. Reliability was ensured by the use of pilot test method. Data analysis was done quantitatively.

Descriptive statistics were used to where mean, mode and standard deviation were obtained. Regression model was then used to obtain the solution for the entire research questions.

The most ethical factors that was highly considered are the privacy of the respondents' information, all the responses treated with confidentiality and great assurance accorded to them. After permission is granted the researcher proceeded to collect data from the 53 respondents.

5. Results and Discussion

The regression analysis was given by correlation of determinant, correlation coefficient, ANOVA table and regression model table. These was used to test the significantly on the integration strategy on the performance of the organizations.

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate
1	.714[a]	.510	.452	.47886
a. Predictors: (Constant), Marketing Integration, Management Integration, HRM Integration, Organization Integration.				

Table 1: Correlation coefficient using SPSS Version 21
Source: Research data (2017)

The table 1 indicated that there was strong positive correlation between integration of organization and performance (R = 0.714). The data used to determine the relationship was 51.0% between independent and dependent variable and 49.0% can be attributed to other factors as represented (R square = 0.510).

Model		Sum of Squares	df	Mean Square	F	Sig.
1	Regression	8.101	4	2.025	8.832	.000[b]
	Residual	7.796	34	.229		
	Total	15.897	38			
a. Dependent Variable: Performance						
b. Predictors: (Constant), Marketing Integration, Management Integration, HRM Integration Affect Performance, Organization Integration						

Table 2: ANOVA using for regression analysis SPSS Version 21
Source: Research data (2017)

The ANOVA results indicated (table 2) there was significant relationship between the integration strategies used to the performance of the organization (P < 0.05).

Model		Unstandardized Coefficients		Standardized Coefficients	T	Sig.
		B	Std. Error	Beta		
1	(Constant)	-.261	.891		-.293	.771
	HRM Integration	.266	.088	.391	3.019	.005
	Organization Integration	.011	.084	.018	.136	.893
	Management Integration	.235	.120	.244	1.963	.058
	Marketing Integration	.541	.161	.462	3.359	.002
a. Dependent Variable: Performance						

Table 3: Regression model (SPSS Version 21)
Source: Research data (2017)

The research findings indicated that HRM integration and marketing integration was significant for performance of the organization (P<0.05). On the other hand organization and management integration was not significant to the performance (P>0.05).

- Objective 1: The finding indicated HRM integration strategy was significant (P=0.005) predictor to performance of the organization (P<0.05). HRM integration brought second highest positive effect on the performance per unit (Beta =0.391).
- Objective 2: Organization integration was noted that it is not significant (P=0.893) predictor to the performance of the organization (P>0.05). Organization integration brought little positive contribution per unit performance (Beta = 0.018).
- Objective 3: Management integration was not significant (P=0.058) predictor to the performance of the organization. There was positive improvement of performance per unit of management integration applied (Beta = 0.244).
- Objective 4: On the performance as result of the marketing integration was noted to be significant (P=0.002) since (P<0.05). Marketing integration provided the highest unit contribution in performance (Beta = 0.462).

6. Conclusion and Recommendation

The study concluded that there was significant of the integration to the performance of the organization. Despite the organization and management integration producing insignificant positive effect to the performance of the organization. The organization did improve performance due to integration. The performance was high contributed positively by human resource management integration and the integration of marketing.

The integration strategy that was highest predictor to performance come from marketing integration. It improve both market share and sales which provides important variable in performance of the companies. The second positive and significant contributor to the performance was HRM integration, since through the period of integration there high number of employed staff and mainly had degree as the highest academic level. This can give a view point of why there was significant improvement of performance as result of HRM integration. Management integration was a positive predictor of performance but was not significant as the other first and second predictor (marketing and HRM integration). Marketing produce positive was positive predictor but it was not significant to the performance.

The study noted that there was a need to improve on management and organization integration. The two always dependent on why and how the organization integrated. It means that if it was a forced takeover the management and the structure might be on shaky grounds. Human resource management can still produce negative result if the integration were done in hurry. The orientation of the integration could still play significant effected on the performance of the new organization.

The research found weakness in organization and management integration. It is then important that a good organization integration which can be made through assessment of the organization goal, vision, mission and the organization structure. The other important are is the improvement of management style and management planning in the organization. The HRM integration and marketing integration provided positive and significant improvement to performance, to improve more on these service industries more need to be done on the two.

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