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Influence Of Vertical Integration Strategy On Sales Performance Of Soft Drink Manufacturing Companies In Nairobi County, Kenya

By

[1]Sylvia Nyamoita Morumbwa, [2]Prof. Constantine Nyamboga, [3]Dr. Charles Mwambela
Corresponding author email address: sylvia.morumbwa@gmail.com

[1]Masters student, School of Business and Economics, Lukenya University.
[2]Prof. of Library and Information Science, School of Business and Economics, Lukenya University, cnyamboga@yahoo.com

[3]Lecturer, School of Education and Social Sciences, Lukenya University, Kenya, charlesmwambela@gmail.com

Abstract

The primary objective of this study was to examine the influence of vertical integration strategy on the sales performance of soft drink manufacturing firms in Nairobi County, Kenya. In today's dynamic and increasingly competitive business landscape, firms must implement effective strategies to sustain their relevance and improve performance. Vertical integration, as a corporate growth strategy, allows organizations to control multiple stages of production and distribution processes, potentially enhancing operational efficiency and boosting sales outcomes. However, despite its growing adoption, the direct impact of vertical integration on sales performance, particularly within the soft drink sector, remains uncertain. This study sought to bridge this gap by exploring the extent to which vertical integration affects sales performance. Utilizing a survey research design, data were collected from 141 respondents within the soft drink manufacturing sector. SPSS software version 24.0 was employed for data analysis. The results are expected to offer practical recommendations for soft drink manufacturing companies, further contributing to the growing body of knowledge on vertical integration's role in enhancing competitive advantage.

Key words: Kenya, Nairobi County, Competitive business landscape; Operational efficiency; The soft drink manufacturing; Vertical integration strategy

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Introduction

Background of the Study

In recent years, businesses worldwide, including those in Kenya, have faced increasing pressure to rationalize their operations and adopt innovative strategies to remain competitive in the face of rapidly changing market dynamics. Firms are now contending with global competition as well as local market challenges driven by evolving business environments, technological advancements, and regulatory policies (Ali, Namusonge, & Sakwa, 2016). One of the frameworks that help firms understand and respond to macro-environmental factors affecting their performance is the PESTEL model, which categorizes these factors into political, economic, social, technological, ecological, and legal dimensions (Johnson, Scholes, & Whittington, 2008).

In a world becoming increasingly globalized, firms are compelled to adapt and innovate, particularly in terms of form, structure, and scope, as new technologies provide them with the means to lower production costs and improve operational efficiency (Selen, 2011). Within this evolving business landscape, vertical integration has emerged as a key strategy for improving sales performance and gaining competitive advantages. Vertical integration involves a firm extending its control over different stages of its production or distribution processes, either by acquiring or establishing operations at earlier (backward) or later (forward) stages of the value chain. This strategy allows firms to internalize certain operations, which can lead to reduced transaction costs, improved coordination, and increased control over quality and supply chain processes (Williamson, 1985). In the context of soft drink manufacturing companies in Nairobi County, Kenya, vertical integration offers potential benefits, particularly as these firms face challenges such as unreliable suppliers, fluctuating raw material prices, and distribution inefficiencies. By controlling key aspects of their production and distribution processes, soft drink manufacturers can better manage these uncertainties, reduce operational costs, and ultimately improve their sales performance. According to Marinelli (2011), vertical integration is one of the strategic methods that companies globally use to create value and boost profitability by improving their control over supply chains and distribution networks.

Moreover, vertical integration allows firms to mitigate risks associated with external market transactions, such as price volatility, inconsistent supply quality, or delays. In a competitive and dynamic market like Nairobi, where consumer preferences and market conditions can shift quickly, having control over various stages of production can give firms an edge over competitors that rely heavily on external suppliers. This is particularly important for soft drink companies, where product availability, freshness, and timely delivery are critical factors in maintaining market share and customer satisfaction. The adoption of vertical integration is further supported by the Transaction Cost Theory (TCT), which asserts that firms engage in vertical integration to minimize the costs of market transactions, such as searching for

suppliers, negotiating contracts, and monitoring the performance of external partners (Coase, 1937; Williamson, 1985). For soft drink manufacturers in Nairobi, integrating vertically into supply and distribution channels can help streamline operations, reduce dependency on third-party suppliers, and improve sales performance through better control over production costs, product quality, and distribution efficiency. Therefore, this study seeks to examine the influence of vertical integration strategy on the sales performance of soft drink manufacturing companies in Nairobi County, Kenya. By analyzing the relationship between vertical integration and sales performance, this research aims to provide insights into how soft drink manufacturers can leverage this strategy to improve their operational effectiveness and competitive positioning in a rapidly changing market environment.

The following hypothesis is formulated for the study:

H_{01}: Vertical integration strategy has on sales performance of soft drink manufacturing companies in Nairobi County, Kenya.

Ha: Vertical integration strategy has significant influence on sales performance of soft drink manufacturing companies in Nairobi County, Kenya.

Statement of the Problem

Review of Related Literature
Theoretical Framework
Theories and models help explain, predict, and understand phenomena, extending existing knowledge within certain limitations (Torraco, 2007). Theories should be chosen based on suitability, ease of application, and explanatory power (Durham and Stokes, 2015; Shapira, 2011). This study reviews the Transaction Cost Theory (TCT),) in the context of vertical integration strategy and sales performance of soft drink manufacturing companies in Nairobi County, Kenya.

Transaction Cost Theory (TCT)
Transaction cost theory (TCT) was developed by Coase (1937). Transaction cost aims at costs reduction by carrying out activities in-house to escape costs of transacting with other firms in the market. Coase (2021) asserts that costs of selling, negotiating, finding, dispute resolving and monitoring should aim at costs reduction or minimisation ways with other firms in open market transactions. Joskow (1988) observed that the main focus of TCT is the coordination of determinants of transactions through hierarchies or markets. Williamson (1994) argues that TCT seeks to address why economic transactions are organized in the way they are in modern society. TCT also aims at governance that minimizes both production costs and transaction. Ghoshal and Moran (1996) noted that opportunism with guile is bad for practise and that TCT is prescriptive or prescriptive and opportunism if taken seriously by managers could result to negative consequences for organisations.

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Jones (1998) who adopted an entrepreneurial or positive view criticises it and argues that the assumptions are not problems but opportunities to be taken advantage of. Henderson (2017) asserts that this theory predicts that the organisation of transactions over the market will outweigh management's internal cost and this led to inter-firm profit claim thus making the firm profitable. This strategic decision is then a transaction-cost minimising response to the limited information and contracting cost. The theory informs the vertical integration strategy. This can be inferred from the following that since the 19th century firms have used vertical integration with the aim of achieving economies of scale and reducing transaction costs. All firms incur costs such as information costs, costs during negotiation and monitoring costs. The theory requires these firms to minimise on the transaction costs involved while at the same time maximise on probable contracts. Madhok (2010) asserts preference for internalizing the transaction results impacts external market thus making the external market an external imperfect market.

Methodology

This study adopted a survey research design, targeting 141 respondents from soft drink manufacturing companies in Nairobi County, Kenya. A census design was used, encompassing strategic managers, operational managers, and sales managers from 46 companies. Primary data was collected using structured questionnaires, which were tested for validity and reliability through a pilot study with 30 participants. Face validity and consultations with experts were employed to ensure the validity of the instrument, while reliability was confirmed using pre-tests. Data was analyzed using SPSS software, with descriptive statistics, Spearman's rank correlation, and multiple linear regression to examine relationships between variables. Ethical considerations, including obtaining permissions and maintaining respondent confidentiality, were strictly adhered to throughout the research process.

Results and Discussions

Correlation between vertical integration strategies on sales performance of soft drink manufacturing companies in Nairobi County, Kenya

The results in Table 4.19 revealed that there was a positive and significant association between vertical integration strategies and sales performance of soft drink manufacturing companies in Nairobi County, Kenya. ($r = 0.704$, $p = 0.000$). This implied that vertical integration strategy have a contribution of 0.704 to the result of sales performance of soft drink manufacturing companies in Nairobi County, Kenya. This correlation coefficient value was between 0.7 and 0.8 indicating a strong positive correlation as a factor of performance. A 2-tailed test at 95% level of confidence had a probability value of less than 0.05 which implied that there was a significant correlation between vertical integration strategy and sales performance of soft drink manufacturing companies in Nairobi County, Kenya. The results were in line with Mutungi, (2018) who noted that vertical integration strategies has been widely used as a tool for budgetary control in sales management by many public entities mainly to achieve their high sales performance and established a strong positive relationship between vertical integration strategy and sales performance of soft drink manufacturing companies in Nairobi County, Kenya.

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Table 1: Correlation test of Vertical Integration Strategy

Variable		Performance	Vertical Integration Strategy
Performance	Pearson Correlation	1	
	Sig. (2-tailed)		
Vertical Integration Strategy	Pearson Correlation	.704**	1
	Sig. (2-tailed)	0.000	

** Correlation is significant at the 0.01 level (2-tailed).
Source: Research Data (2024)

Conclusion and Recommendations

The study concluded that vertical integration positively impacted the overall performance of firms. By adopting this strategy, companies were able to lower transaction costs and enhance market power. Vertical integration also improved technical efficiencies in coordinating, monitoring, and enforcing production processes. Firms that employ variants of vertical integration, such as backward and forward integration, are better positioned to outperform competitors. Additionally, vertical integration allows companies to maintain closer contact with customers, reduce the time needed to source raw materials, and streamline the distribution of finished products.

The study identified a significant positive relationship between vertical integration strategy and the performance of soft drink manufacturing companies. Based on these findings, it is recommended that firms that have not yet adopted vertical integration should establish internal organizational policies and a culture that promotes its implementation. Management should also introduce initiatives to encourage the adoption of vertical integration, incorporating it into performance reviews. Furthermore, the strategy should encompass both backward and forward integration. However, companies should exercise caution when adopting vertical integration to avoid conflicts of interest and rising operational costs, which could result from hiring additional labor to manage the increased activities.

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