

Research on the Risk Prevention of Overseas M & A of Chinese Enterprises

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ABSTRACT

With the impact of economic globalization and China's going-global strategy, the number and amount of overseas mergers and acquisitions of Chinese enterprises have been increasing. In developing the operating and financial market, capital export has become the focus of a new round of China's foreign cooperation. Although overseas M & A brings many advantages to the development of Chinese enterprises, it also faces a series of risks, such as heavy losses in the process of M & A. How to avoid this problem has become the concern of many scholars and enterprises. In this regard, combined with the knowledge learned, the author makes an in-depth study on the risk prevention of overseas M & A of Chinese enterprises and puts forward countermeasures according to the actual situation.

Keywords: Chinese enterprises, Overseas M & A, Present situation, Risk prevention

1. INTRODUCTION

In 2001, the Silk Road Economic Belt and the 21st-Century Maritime Silk Road were founded by China's entry into WTO, and the international competitiveness of China increased gradually. To better go to the international market, more and more enterprises follow the development trend and embark on the road of overseas M & A. Therefore, with the rapid development of China's Belt and Road Initiative(BRI), and international capacity cooperation, China's foreign direct investment (FDI) has been increasing rapidly, especially in the case of slowing global capital flows. For China with rapid economic development, overseas M & A can help enterprises seek rapid development and occupy a larger market share [1]. However, overseas M & A is a double-edged sword, which can bring perfect combination, but also has many problems.

According to relevant statistics, the overall scale of overseas M & A of Chinese enterprises has experienced a process of continuous decline after growth. From 2012 to 2015, the transaction amount increased slowly. By 2016, the number of M & A projects increased by 186 compared with 2015, with a transaction amount of U.S. \$135.33 billion, an increase of U.S. \$80.89 billion compared with the previous year. However, affected by many factors, overseas M & a continued to decline in 2017, and China's foreign direct investment maintained stable and orderly development in 2019. According to

the data of the Ministry of Commerce, in 2019, China's industry-wide foreign direct investment was USD 117.12 billion, a decrease of 9.8%, and non-financial direct investment was USD 110.6 billion, a year-on-year decrease of 8.2%. The investment structure is more balanced, mainly flowing to leasing and business services, manufacturing, wholesale, and retail.

Overseas mergers and acquisitions of Chinese enterprises tend to developed regions such as Europe and the United States or Peru and Australia with rich mineral resources. After the one belt, one road policy, the Silk Road Economic Belt, and the 21st-Century Maritime Silk Road, many M & A investments increased. However, the investment in Europe and the United States still accounts for a large proportion [2]. Combined with China's policies, to encourage enterprises to "go global," China has formed friendly and cooperative relations with many countries or regions around the world. With the support of China's government policies, the regions of overseas M & A of Chinese enterprises have been well developed [3].

2. CHARACTERISTICS OF OVERSEAS M & A OF CHINESE ENTERPRISES

M & A is a form of merger and acquisition. Whether it is an absorption merger or a new merger, the merged enterprises no longer exist.

2.1. Taking state-owned enterprises as the main body

Due to the particularity of China's economic system and relevant historical factors, state-owned enterprises often start late, have strong strength, and obtain government support. It is worth noting that state-owned enterprises always play the role of the main force of overseas M & A of Chinese enterprises. At the same time, the monopoly advantage and its inherent state-owned economic responsibilities also urge them to win a place for China's economy overseas through scale expansion. From the actual situation of overseas M & A, Chinese enterprises show strong capital bidding strength and sensitive market development ability [4].

When state-owned enterprises dominated the overseas capital market, domestic private enterprises also began to join them and become the new main team of overseas M & A of Chinese enterprises. Combined with the actual development situation, the activity of private enterprises exceeded the development trend of state-owned enterprises for the first time. From Sany Heavy Industry's €324 million acquisition of Germany's Popmaster, the world's cement mixing giant, to Bright Food's £700 million stakes in the U.K.'s largest breakfast cereal brand Vitamix, to Haier Group's announcement that it is the holder of 90% of New Zealand electrical brand Fisher & Paykel, to CNOOC crossing the final hurdle after a seven-month tug-of-war to complete its \$15.1 billion acquisition of Canadian oil and gas company Nexen. The \$15.1 billion acquisition of Canadian oil and gas company Nexen was completed after a seven-month tug-of-war. This speaks volumes about the strong capital competitiveness of Chinese SOEs, showing a flexible ability to capture the market [5].

2.2. It started late and developed rapidly

At the beginning of the 20th century, the M & A activities of global multinational corporations formed a relatively large scale. Chinese enterprises started overseas investment in 1979. At that time, the "Jinghe Co., Ltd." jointly established by Beijing Friendship Business Service Company and Tokyo Marui Commercial Co., Ltd. in Tokyo, Japan, expanded its strength through overseas M & a later, which is not conducive to the development of globalization. However, China has not retreated. It has changed from passive to active in its development, using its advantages to catch up and carry out overseas M & A activities [6]. With the overall development, China's overseas M & a market has achieved blowout growth under the environment of strong economic development and accelerated industrial integration, and the M & A activity and M & A amount have reached a record high [7]. Especially in recent years, the increase of China's

comprehensive strength and the surge of foreign exchange reserves have promoted the continuous appreciation of RMB, and Chinese enterprises have more powerful purchasing power. In particular, the increase in China's comprehensive strength in the past few years and the surge in foreign exchange reserves have contributed to the continuous appreciation of the RMB, and Chinese companies have more powerful purchasing power.

3. RISK ANALYSIS ON OVERSEAS M & A OF CHINESE ENTERPRISES

3.1. Financial risk

The payment forms of overseas M & A are cash, debt financing, and mixed payment. Among them, the risk of cash payment is the greatest. You should know that the transaction amount involved in overseas M & A is very large. The use of cash payment has a higher cash storage capacity for enterprises, which is easy to bring increased pressure on cash reserves to enterprises.

If you choose bank loans, there are problems such as cumbersome procedures, slow arrival of funds, and high-interest rates, which increase the capital risk of enterprise M & A. Mixed payment also has some problems, such as cumbersome approval process, difficult financing[8]. For example, of the US\$380 million capital used for BOE's acquisition of the Korean LCD business in 2003, US\$60 million was purchased with its funds after the foreign exchange, and domestic banks provided another US\$90 million in one-year loans. Huge loans were used for M&A, and BOE's asset structure deteriorated seriously, resulting in a high gearing ratio of 72%, which entered the internationally recognized early warning zone, with rising financial risks, seriously affecting the company's subsequent development.

3.2. Legal risk

Overseas M&A will also encounter many legal risks, and the laws, review systems and regulatory systems for foreign investment vary greatly from country to country, such as safety review risk, antitrust legal risk, labor protection risk, intellectual property risk, and environmental protection legal risk. For example, CIMC's acquisition in the Netherlands was subject to antitrust scrutiny by the European Union. CNOOC, Minmetals, and Huawei's acquisitions in the United States were subject to an antitrust investigation. Companies are subject to strict labor laws in foreign countries in their development and violate the environmental laws of their host countries [9].

3.3. Political risk

The political environment of the host country is easy to have a series of effects on enterprises' overseas M & A. If the political environment of the host country is stable, enterprises will face the common risk of operating and management fees when completing overseas M & A; if politics is unstable, it will increase the risk of personal safety and property loss caused by political changes [10]. For example, in 2005, during CNOOC's bid for Unocal, U.S. government officials and members of the public talked about the "China threat theory" and strongly opposed Chinese companies acquiring U.S. companies. In early 2011, Huawei was forced to abandon its acquisition of 3Leaf after the U.S. Congress blocked it.

4. ANALYSIS ON RISK PREVENTION COUNTERMEASURES OF OVERSEAS M & A OF CHINESE ENTERPRISES

4.1. No blind M&A

In the early stage of M & A, we should do a good job in investigating and formulating appropriate M & A and post-M & A integration strategies. In the process of investigation, we pay attention to the macro aspects involving different political, economic, cultural, legal, religious, and other information of the two countries, and the micro aspects involving the enterprise's background and history, the enterprise's industry, the enterprise's manufacturing mode, marketing mode, financial data and financial system, research and development plan and other related issues. Do a good job in the investigation of the company, grasp the enterprise market objectives in combination with the actual situation of the company, and lay the foundation for the follow-up development of M & A.

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The reason why Shuanghui was willing to spend \$7.1 billion to buy Smithfield was that the acquisition would reduce its dependence on the Chinese pork

farming market, introduce SFD's mature management experience and methods, and directly own an international operating team as a way to increase its international position and voice. Shuanghui International has prepared two sets of programs in the process of the acquisition. That is, one set of options is just a full-scale tender offer for a listed company with a relatively high leverage ratio of acquisition capital, and the other set of options is a full-scale tender offer for a listed company with a leveraged buyout as the main method, and it is the SFD debt restructuring situation that determines how Shuanghui International takes. This is enough to see that before the merger, Shuanghui did a lot of preparatory work.

4.2. Improving the ability to assess risk

Before the process of corporate M&A, Chinese companies should carefully study the evaluation issues before M&A and actively use the help of international intermediaries to study carefully to avoid losses caused by blind investments. It is important to collect as much information as possible and to review and evaluate the collected information and make full use of the information disclosed in the financial reports. It is worth noting that the sufficient information is gathered during the information collection process, the more the risk of information asymmetry can be reduced, and the probability of successful M&A can be promoted. Companies hire authoritative and professional appraisal organizations to collect, review and evaluate information and reasonably judge the true value of the company [12]. In addition, companies also need to hire professional intermediary structures, such as accounting firms, to review and confirm the authenticity of the information collected, and to reduce overall losses by determining the liability between the two parties through not long agreements.

4.3. Policy support for M&A

Numerous examples prove that policy and institutional support from home countries play an important role in the success of overseas M&A. The government can provide some macro-level guidance on overseas M&A activities based on the current status of M&A in the home country during the development process. For example, China can set up unified management and consulting service for overseas M&A, collect political, cultural, economic, and social knowledge of each country, and let enterprises consult when they need it, help them to formulate their policies and rules for overseas M&A, and help them to go abroad from the national level so that Chinese enterprises' overseas M&A can be smoother. We have issued various regulatory documents on foreign exchange, taxation and state-owned assets management system and financial regulation, accounting standards

harmonization, domestic and foreign capital market convergence.[13]. It is committed to standardizing and coordinating rule of law management, market mechanisms, and information services, and actively promoting Chinese enterprises to explore cross-border M&A models and paths that effectively utilize domestic and international securities markets, conform to domestic and international legal systems, and follow international market practices. The relevant information of a wide range of external personnel will be registered, the filing database will be established, and the monitoring work will be done well [14]. At the same time, pay attention to the regional security situation, issue an early warning and timely remind evacuation to ensure the overall development trend.

5. CONCLUSION

The scale and growth rate of overseas M & A of Chinese enterprises are normal and reasonable, which plays an important role in improving the status of Chinese enterprises in the global value chain, serving the transformation and upgrading of the domestic economy, and deepening the mutual benefit, win-win and common development between China and other countries in the world. In addition, with the continuous increase of China's economic strength, its position on the international stage is becoming more and more important. Under such a development background, the pace of internationalization of Chinese enterprises will be firmer. Combined with China's development trend, the full vitality and vitality of Chinese enterprises on the world stage inject new vitality into the overall development. With the changes of the times, the world pattern is also changing, the characteristics of overseas M & A are not changing, and M & A has to bear more and more risks. Therefore, enterprises need to constantly adjust their strategic behavior in combination with the actual situation of overseas M & A. It is worth noting that overseas M & A is a long road, which needs continuous exploration and summary in the actual development, to explore an overseas M & A road with Chinese characteristics in combination with the actual situation.

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