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THE SURGES AND TRENDS OF THE MERGER AND PURCHASE BETWEEN CHINESE ENTERPRISES

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For the whole 30 years from the 50s to the 70s, China has been practising a planned economy model of high concentration, and carrying out the system of the enterprises' being exclusively owned by the state and managed by the government. Enterprises, which were like chessmen on the chessboard, had to be subjected to the control of the officials and organize all of their activities according to the government's decrees, from the production and sales of product to the merger, adjustment, and recombination. Because enterprises at that time were not really granted the status of legal bodies and their property was owned by the state exclusively, such problems as of merger and purchase between enterprises and assets recombination that we discuss nowadays under present condition of market economy did not exist.

In the 80s Deng Xiaoping started the reformation movement of economic setup and adopted an open policy, which freed China's economy from the yokes of traditional planned system and caused its rapid transition to a market one. As a result, the old economy of the state's exclusive ownership was substituted by a new one of diversifying ownership, and the compound and private economy developed. There on the vast land of China came the great surge of the merger and purchase between enterprises and that of assets recombination.

The following part of this article basically analyses the current situation, characteristics, and trend of the merger and purchase between China's enterprises.

The Rise of the Enterprises' Merging and Purchasing Surge

In 1984, Baoding Boiler Factory merged Baoding Blower Factory and setup the first case of the merger and purchase between enterprises in China. In May 1998 Wuhan took the lead and established China's first enterprise property transaction market, which was followed by the establishment of the markets in Baoding, Zhengzhou, Luoyang, and Taiyuan, one after another. In 1989 the Chinese government laid down the "Temporary Provisions about the Merger and Purchase between Enterprises" which prologued the surges and sped up China's enterprises' merging and purchasing process. During the whole decade of the 80s, 6966 enterprises were merged in China. This is the first surge.

The second surge began with China's official proclamation in 1992 of setting up market

economy system, after which enterprise merger and purchase became active again. A survey covering only 6 cities showed that in 1993 more than 2,900 enterprises were merged, with \$800,000,000 of stock assets transfer, among which what is notable is the case of Shenzhen Bao'an Corporation's merging Shanghai Yangzhong Stock Corporation through buying its stocks in Shanghai. In Oct. 1993, Bao'an Corporation purchased 16.8% of Yangzhong's listed circulating stocks and became its biggest stockholder. Later Bao'an's representative took the position of Yangzhong's president in Apr. 1994. This is the first case of merger and purchase between corporations in China's stock market.

In 1997 the policy of "encouraging enterprise merger" put forward during the 15th Conference of Chinese Communist Party further stimulated the enterprises' merger and purchase. Up to now, there are more than 200 property transaction institutions in China, and tens of thousands of enterprises have been merged while tens of billions of dollars of assets have been recombined.

Through the merger and purchase between enterprises, a large quantity of stock assets have been activated and in turn have appreciated, which sped up the gathering of scattered capital, resulting in the rapid expansion of many corporations' assets and an evident increase of their operating profit. Among the successful cases were those of Qingdao Hai'er Group and that of Changchun Motor Group.

Case 1: Hai'er Group was only a small collectively-owned enterprise with assets no more than 2 million dollars ten years ago before merging 14 other household electric appliance enterprises in succession, which added to its assets to 500 million dollars odd. Making an annual net profit of more than 100 million dollars, it is now No.1 among all China's household electric appliance enterprises. With an output of more than 1 million sets and a sales volume of more than 200 million dollars annually, 6 years after its being merged by Hai'er Group, Tsingtao Air-conditioner Factory was brought back to life from the serious problems of over stock and large deficit.

Case 2: Relying on its advantages in technology and management, Changchun Mobile Group, through merging, holding stocks, has in the 90s developed from a unitary factory into a big enterprise group owning 37 specialized factories, 12 full-asset sub-companies, 11 holding companies, 3 listed companies, 18 joint ventures, and 250-odd participating and relevant enterprises, with the whole operating assets of 5 billion dollars and an annual sales volume of more than 4 billion dollars, while its technological level, economic effects, and ability to develop new products have obviously improved.

But the market of enterprise merger and purchase is not always so promising. There are successors and losers as well.

Case three---Kang'enbei Pharmaceutical Corporation's merging and purchasing Phoenix Daily Chemical Articles Corporation: Anxious to find a suit to get listed in the market, Kang'enbei Corporation blindly bought state-owned 50.01% of the closing-down Phoenix Corporation's stocks in June, 1994. Up to now, Kang'enbei has during the latest 3 years put large amounts of manpower and financial resources into Phoenix, but because of its under-estimation of the market risk brought by conglomerate operation, the deterioration of Phoenix's staples' market situation and of its assets structure, Phoenix's still increasing overall deficit and failures of its policy of listed corporations' stock allocation from no control to rigid control, Kang'enbei failed to make Phoenix finance itself directly in spite of the sacrifice of some of its own interests.

From the cases mentioned above, successful or unsuccessful, we can draw the conclusion that what determines most the results of enterprise merger and purchase are the operator's decisions. While making decisions, the operator should see that they themselves know not only themselves

but also their enemies, not only their bosses but also their men. Detailed investigations should be made on the assets' composition, liability situation, product market, and operating situation of the enterprise that is to be merged or purchased and also on the government's policies, the business' characteristics and the enterprise's circumstance before the final decision of merging or purchasing is made.

The merger and Purchase by Overseas Capital

The great economic effects of enterprise merger and purchase under present condition of China's immature market economy have been urging shrewd overseas entrepreneurs to take drastic actions of merging and purchasing in Mainland China. Some corporations from foreign countries and Hong Kong, Taiwan and Macau have found their share of China's market through buying part or all of the stocks of enterprises.

The following presents the most typical case. Since 1992 Hong Kong Zhongce cooperation has got the controlling interest of 180 state-owned enterprises in Mainland China and has established 35 joint-venture corporations. It holds more than 51% of the stocks of each of these corporations. After it had got the control of so many enterprises in Mainland China, Zhongce Corporation registered two of them in America as one corporation---China Tire Corporation, which was listed in New York market and got 94 million dollars. Zhongce has the ownership of China Tire Corporation's full assets, of course. There are many more cases like this one.

To the end of 1996, in China foreign firms had in their hand the controlling interest of 12 of the 13 largest enterprises in the medicine line and 10 of the 59 state-fixed enterprises in the rubber line; while in the beer line, all of those enterprises whose annual output was more than 100,000 tons were joint ventures except 2, while among those that had an annual output of between 50,000 tons and 100,000 tons 7% were joint ventures. It was also the same in other lines.

Foreign capital's monopolizing China's trade markets, especially in those lines that have a high profit margin, through purchasing and holding the stocks of state-owned enterprises in a planned way purposefully, has drawn the attention of the government and all circles of the society.

The Inevitability of the Enterprise Merger and Purchases Surge

It is not by chance that the surges of merger and purchase between enterprises rose, one higher after another. The basic reason lies in the development of market economy and the diversifying ownership of enterprises.

The stiff planned economy system caused the terrible waste of resource and capital allocation and in turn bad economic results, while the flexible market economy system spurs enterprises to merge and purchase each other in the pursuit of possibly highest profits and as a result resource allocation is rationalized and capital joins in an optimized way.

The emerge of compound economy, private economy, and foreign capital has stimulated the establishment of diversifying ownership and the development of stock and bond market system and enterprise property exchange. The promulgation of Company Law by Chinese government in 1994 marked the substitution of the old enterprise property system by a new one and at the same time laid down the lawful foundation for the new system and the operation of enterprise merger

and purchase.

The establishment of Shanghai stock exchange and Shenzhen stock exchange in 1990 and the launch of the nation-wide stock exchange electronic system provided for the merger and purchase between enterprises in market indispensable conditions.

Characteristics of the Merger and Purchase between Enterprises

Because the merger and purchase between enterprises in China are conducted under the circumstance of an imperfect market economy and a not-so-standardized stock system, some defects and immaturity to certain extent should be within expectation. In present situation, enterprise merger and purchase in China have four forms and characteristics as listed below:

1. Listed corporations merged or controlled unlisted corporations by holding their stocks.

Listed corporations used the large amount of capital drawn from issuing stocks to merge and purchase unlisted corporations. For example, Jiabao Group holds the controlling interest of Shanghai Dongjing Instrument Company; Dongbei Hualian has merged or purchased 3 directional collected companies; Tsingtao Beer Group has purchased Yangzhou Beer Factory; Wanke Corporation owns stocks of scores of other enterprises, among which New Energy Source, Meidi, and Changyin have been listed on market. Listed corporations' active participation in stock equity investment embodies the characteristic that with purchasing and participating stocks as guidance, China's big corporations expanded not only their industrial capital but also their financial capital, mixed into each other, and developed toward big corporation groups.

2. Unlisted corporations purchased listed corporations' stock equity.

Because it was very difficult to get the government's approval to be listed on market, many unlisted corporations turned to the approach of purchasing the listed corporations' stock equity as "a suit" to get partly listed, and there was the fierce competition between purchasing and anti-purchasing, merging and anti-merging in the security market. Changchun Motor Group spent mimes amount of capital purchasing Shenyang Gold Cup Motor Joint Stock Company. After taking in hand part of Dongbhei Hualian's state-owned stocks and corporation-owned stocks transferred to its ownership through various ways and at various prices, Hai'nan Wantong Corporation bought 2% more of stocks in secondary market and owned the total of 16.4% which made it the biggest stock holder of Hualian.

3. Enterprise merger and purchase was conducted with speculation.

The mergers or purchasers bought their target corporations' circulating stocks directly from the circulation market. Because Chinese government decreed that state-owned stocks and corporation-owned stocks not be listed on market, only public-owned stocks were listed and some "merger and purchase concept stocks" have come into being. In many cases the purchasing was not a strategic investment at all, but only a kind of speculation in the stock market.

4. Corporation-owned stocks were alienated according to negotiations by foreign capitals.

At present, China's state-owned stocks are to be listed on market for exchange, so they can only be alienated by negotiations, and it makes no difference whether it is foreign capitulator not. In 1995 through negotiated alienation Japanese Wushiling Motor Corporation and Yingtengzhong Business Corporation together held 25% of Beijing Tour Vehicle Joint Stock Company's corporation-owned stocks, Jiangling Motor Corporation has transferred 20% of its newly issued B stocks to Ford Motor Company. These two cases were followed by the "merger and purchase negotiations" of many other enterprises like Guangzhou Electronic, Guanhua, and Shenzhen Estate. The way of alienating corporation-owned stocks through negotiations helps a lot to attract foreign capital, obtain operating and managing skills, and widen business channels.

The Trends of Merger and Purchase between Enterprises

The process of China's enterprise merger and purchase will in the future mainly go in three directions.

1. Capital will tend to gather in big enterprises.

All that have been listed on market are big enterprises. They will constantly merge and purchase other enterprises according to the need of their producing and operating activities as well as the capital they get from the stock market, Through merging and purchasing, at a low cost, resource combination and capital combination will be optimized; the enterprise's ability to compete with others will be improved; industrial capital will be gathered together. At last there will appear many new big corporations with solid synthetic strength.

2. Products will tend to that of famous brands.

Those enterprises with famous brands will merge and purchase those have no famous brands. Through these merging and purchasing, the production scale of products of famous brands will be enlarged; production cost will be reduced; social assets will be saved; the economic effects and chances to win international competitions of famous brands will be improved. All of the above will amounts to the final assimilation of kindred products in the line to famous brands.

3. State-owned property tends to go into market.

The state-owned and corporation-owned stocks of listed enterprise will gradually became mobile and exchangeable in the stock exchange market. At present, because state-owned and corporation-owned stocks can't circulate in market, violations are very common while merging and purchasing. Even though state-owned stocks, corporation-owned stocks, foreign-owned stocks, and public-owned stocks may exchange with each other through alienating, too striking is the difference between prices. The freeze of state-owned and corporation-owned stocks not only caused the big

lose in the activation and appreciation of state-owned and corporation-owned assets, but also hindered fair exchange between property of various kinds of owner ship. This irrational phenomenon will sure be broken by the market principle of fair trade, and state-owned and corporation-owned property will sure go into market, changing from solid to liquid. 4. Property merger and purchase will tend to expand overseas.

Along with the trends of capital's concentrating on big corporation groups and of products' concentrating on famous brands that appear in the process of China's economic development, China will see the rise of many powerful big transnational enterprise groups which are capable of investing and conducting merger and purchase overseas. The trend of trasnational merger will go further.

Difficulties Remaining to Be Solved

Now China is undergoing the transition from the old planned economy to a new market one. So it is quite natural that there remain some difficulties in enterprise merger and purchase.

1. Property relationship should be further clarified

Private enterprises see their property basically clear, while the property relationship of township enterprises, collective enterprises, and state-run enterprises is so complicated that there seems somebody responsible though actually there is nobody. Merger and purchase between enterprises has run into a lot of concrete problems that are waiting to be solved.

2. Hedges should be further broken through

Property exchange market should be an unified market, or it is inefficient, but China's present divided and separated administration system makes the merger and purchase between regions or lines much harder than within the same region or the same line. This should change.

3. The government's supervising should be further standardized

The subject of enterprise merger and purchase is the enterprise itself, and the enterprise should behave according to the laws of market economy. It is quite necessary that government bring to play their functions in policy, law, supervision, and so on, for the government's performance will affect the result of merger and purchase between enterprises. In the past, for the integration of administration and enterprise, during the process of merging and purchase the blind interference by the government through administrative measures always caused negative effects. From now on, while dealing with problems concerning merger and purchase the government should concentrate its efforts on policy, law, and supervision to ensure that the merger or purchase goes on a normal and proper way.