Proceedings of the 3rd International Conference on Business and Policy Studies
DOI: 10.54254/2754-1169/71/20241513

Analysis of Hostile Merger: Evidence from Bao-Wan Controversy

Bangjie Li[1,a,*], Feihong Xiang[2,b]
[1]*Department of Finance, University of Western Ontario, London, Canada*
[2]*Suzhou Institute of Technology, Jiangsu University of Science and Technology, Zhengjiang, China*
a. BLI627@uwo.ca, b. 1960589442@qq.com
**corresponding author*

Abstract: As a matter of fact, with the rapid development of enterprises in China, the merger is indispensable during the boosting of the economy, but many of them are not smooth, both sides are not satisfied, and even contradictions. On this basis, through the analysis of the case of Baowan dispute, this study obtains the impact on the acquireee when a hostile takeover occurs. According to the analysis, it is easy to find that hostile takeover will affect the development of the company, but it will show a slight upward trend in the early stage of the takeover. At the same time, the implications as well as suggestions will be proposed based on the evalutions. To sum up, the study can help the company to anticipate the impact of the acquisition and anti-acquisition, so as to facilitate the company to make preparation and prevention in advance. Overall, these results shed light on guiding further exploration of hostile merger analysis.

Keywords: Hostile Merger, M&A, Bao-Wan controversy, Finance analysis

1. Introduction

Corporate mergers and acquisitions have gradually become a common financial investment method in today's capital market and have attracted widespread attention from investors. With the continuous development of the capital market, many cases of hostile mergers and acquisitions have also emerged. The nature of mergers and hostile mergers and acquisitions, as well as the strategies and means used in the process, are very different. Over the past many years, mergers and acquisitions represent complex phenomena that have attracted significant interest across a variety of management disciplines [1]. Analyzing the action strategies adopted by companies in hostile mergers and acquisitions and summarizing the short-term and long-term consequences of hostile mergers and acquisitions are crucial to the continued development of the capital market.

This article takes the "Bao-Wan Controversy" as a case to analyze and summarize the merger and anti-merger strategies adopted in the malicious merger incident between Baoneng Group and Vanke Group, and analyzes the stock price, net profit margin of total assets, return on net assets, investment The models and charts of revenue, total comprehensive income and other related information study the impact of this incident on the subsequent development of Vanke Group, which has certain practical and theoretical significance. Be advised that papers in a technically unsuitable form will be returned for retyping. After returned the manuscript must be appropriately modified.

2. Basic Concepts

Enterprise mergers and acquisitions refer to the merger of two or more independent enterprises to form one enterprise on the basis of equality, voluntariness and equal compensation. Enterprise mergers and acquisitions are an organizational form and an investment method. The purpose is to obtain pricing power in the market economy, minimize risks and obtain the added value of the acquired assets [2]. Financial and operational synergy are approached differently by management during mergers and acquisitions. Long-term synergies can be produced by the acquirer in the form of increased cash flow, increased operations, diversification, cost reduction, etc. [3]. With the continuous development of the financial market, corporate mergers and acquisitions have gradually become a common financial investment behavior in the financial market, and have received extensive discussion among investors in the capital market.

Hostile acquisition refers to the acquisition behavior carried out by the acquiring company without the permission of the target company's board of directors, regardless of whether the other party agrees [4]. When a hostile takeover occurs, the hostile acquirer or activist shareholder will often attempt to take control of the target company by circumventing the target company's management and board of directors and going directly to the shareholders. During the process, hostile acquirers will gradually take control of the target company by purchasing the shares of the target company at high prices, reorganizing the company's top management, and changing corporate policies. One contentious practice in the corporate governance framework is hostile takeover. Supporters of the idea consider it to be the most severe punishment for managerial misconduct or incompetence. Critics contend that it is prone to misuse, imprecise, and the cause of significant system and ad hoc expenses [5].

In friendly mergers, the acquirer and target may often engage in discussions and negotiations for weeks or months before announcing a deal. The target may agree to share certain information with bidders to better inform a possible transaction. Once a deal is struck, the two companies announce the acquisition together and frequently hold calls with shareholders and analysts to tout the benefits of the proposed deal. In contrast, hostile mergers typically occur after target company management refuses to engage with potential acquirers. The acquirer appeals directly to the target's shareholders, often offering a premium for the stock and developing plans to enhance the company's future prospects. Management may try to discredit the acquirer or paint a group of investors as corporate raiders in an attempt to get shareholders to reject any offer. Hostile takeovers may also cause the target company's primary attention to be diverted and may even lead them to engage in value-destroying actions to prevent a takeover. In a hostile takeover, bidding firms receive greater value; but, they also pay acquisition costs, which could lead to a preemption equilibrium if the costs rise [6].

Generally speaking, friendly mergers cost less and take less time to complete than hostile mergers. Furthermore, friendly takeovers tend to produce better results than hostile takeovers. If this transaction cannot be completed, these shares can only be purchased on the secondary market and added to the board of directors. The commercial laws and securities legislation of various countries cover the procedures for real acquisitions, reflecting the government's support for real acquisitions. Therefore, the laws and regulations of many countries (including corporate and securities laws) pay close attention to hostile mergers and mitigate the risks they bring [7].

3. Case Descriptions

In June 2015, A-shares are only within 14 trading days, the Shanghai Composite Index plummeted from 5,166 to 3,686,the scene of thousands of shares falling to the limit has been staged many times, the central bank and the China Insurance Regulatory Commission and other institutions have vigorously supported, among them, the China Insurance Regulatory Commission has relaxed the upper limit on the proportion of insurance funds invested in blue chip stocks and equity assets. So far,

DOI: 10.54254/2754-1169/71/20241513

insurance funds have entered the market in a big way, more than 10 insurance companies such as Baoneng and Anbang have raised a total of 35 listed companies. At that time, Vanke's total assets were 500 billion, the total profit is 25 billion, the monetary funds on the account are as high as 62.7 billion, with such excellent financial data, the stock price has only hovered between $4 and $4 in '08-14,and the shareholding is extremely diversified, as shown in Table. 1, Vanke's largest shareholder is China Resources Group, but he is not the actual manager of Vanke. Therefore, the Baoneng Department wants to seize this once-in-a-lifetime opportunity to swallow the elephant [8].

Table 1: Top 10 Shareholding Ratios of Vanke in 2014.

Name	Nature of shareholders	Shareholding ratio
China Resources Co., Ltd	State-owned legal persons	14.91
HK SCC NOMINEES LIMITED	Foreign shareholders	11.91
Guosen Securities	Other	3.30
Anbang Life Insurance Company Limited	Other	2.13
GIC PRIVATE LIMITED	Other	1.32
Liu Yuansheng	Other	1.21
UBS AG	Other	1.08
National Social Security Fund	Other	0.72
China Construction Bank	Other	0.65
CSOP Asset Management Limited	Other	0.65

On July 11, 2015, Qianhai Life Insurance, an insurance company under Baoneng, purchased 552 million shares of Vanke from the secondary market, for the first time, it won 5% of Vanke's total share capital. This kicked off the prelude to the "Baowan Dispute". Subsequently, Baoneng's subsidiary, Jushenghua, raised Vanke for the second time,won 5% of Vanke's equity again. Jushenghua and Qianhai Life Insurance have 67.4% and 51% of Baoneng Investment Group's shares, respectively, which also makes Baoneng's total shareholding in Vanke reach 10%. In just half a month, two cards were raised in succession, this also made Wang Shi, the sensible of Vanke, realize that this is obviously not a simple financial investment.

The two had their first conversation, in the end, it ended in failure. As the actual manager of Vanke, since he doesn't want Baoneng to become the largest shareholder, the simplest and most straightforward way is to ask China Resources, the largest shareholder, to increase its shareholding ratio to retain its position as the largest shareholder, however, after several conversations, the response received was also that China Resources refused to increase its shareholding. After asking China Resources to increase its holdings to no avail, and the plan was rejected one after another, there was a contradiction between Vanke and China Resources for the first time. Noticed that China Resources had no intention of saving Vanke, Baoneng raised its cards for the third time a month later and raised its shareholding to 15.04%, surpassing China Resources to become Vanke's largest shareholder [9]. Seeing that his position as the largest shareholder was not guaranteed, and Wang Shi publicly praised China Resources' contribution to Vanke, China Resources increased its stake by 0.4% in the secondary market in the following days, and its shareholding ratio rose to 15.29%, returning to the position of the largest shareholder. On December 4, Baoneng raised Vanke again, and its shareholding ratio rose sharply to 20.008%. At this time, Anbang suddenly came to an end, this comedic scene made the battle situation confusing, and on December 7, Anbang Insurance strongly raised Vanke's stake to 5% [9]. According to Vanke's articles of association, if the shareholding ratio reaches 30%, it will become the actual controller of Vanke, and it has the right to reorganize the board of directors. At this time, Anbang's participation made him one of the important factors affecting the trend of the

DOI: 10.54254/2754-1169/71/20241513

Baowan dispute. Baoneng increased its stake in Vanke to 22.45%, becoming Vanke's largest shareholder [10].

On December 17, Anbang followed up to 7% of its shares. Subsequently, Baoneng continued to buy Vanke shares in the secondary market on December 18, and even after the opening of Vanke shares, the direct limit of Vanke shares, according to this posture, even without Anbang, Baoneng itself can hold 30% of the shares, for which Vanke management was forced to announce the suspension of stock trading [8]. For Baoneng, the suspension of stock trading undoubtedly increased its burden, because Baoneng's financing leverage was as high as 20 times, the entire capital chain collapsed very tightly, and during the suspension period, Baoneng still had to pay financing interest. As far as Vanke is concerned, if it can be confirmed that Baoneng's funding organization is problematic, and thus cut off its funding source, it can turn the tide against the wind. However, under the investigation of the professional institutions dispatched by the Shenzhen Stock Exchange, Baoneng barely passed. At this time, the supervision bureau in South China required the joint-stock branches and city commercial bank branches to give feedback to the second share of Baoneng's credit and credit in the bank, and the China Banking Regulatory Commission and the Insurance Regulatory Commission did not have a substantive effect on the use of Baoneng's funds, but it also showed something, and at the same time Wang Shi also won the support of Anbang.

Later, under the negotiation between Wang Shi and China Resources, China Resources said that Vanke could introduce other state-owned assets to ensure its status as the largest shareholder of state-owned assets. With Wang Shi's efforts for a month, Shenzhen Metro Group issued a public statement of intention to reach an asset restructuring plan with Vanke, after Wang Shi and China Resources repeatedly communicated without a response, Vanke Board of Directors took it upon itself to unilaterally sign a memorandum of cooperation with Shenzhen Railway Group, Vanke will issue new shares in exchange for two pieces of land held by Shenzhen Railway Group, if the transaction is successful, Shenzhen Railway Group will surpass Baoneng to become the largest shareholder in one fell swoop, Vanke management is full of confidence. However, at this time, China Resources suddenly changed its mind and sent a letter to the regulatory authorities accusing Vanke of having problems in the disclosure of information on the restructuring proposal, and publicly expressed the hope that Vanke would not disrespect China Resources' opinions again, otherwise it would lose the trust of China Resources. China Resources does not want to give up Vanke, and the rejection of Vanke's restructuring proposal also shows that China Resources does not want to give up control of Vanke to Shenzhen Railway Group. However, an accident at the final board meeting changed the pattern at that time, and due to coincidence, the reorganization proposal of Vanke's management team was also passed. Nevertheless, at the subsequent shareholders' meeting, Baoneng and China Resources Group, the two largest shareholders before the reorganization, raised objections to the board of directors of Vanke at the same time, simply put, they opposed the reorganization proposal, and at the same time proposed to convene the second extraordinary general meeting of shareholders, and proposed to remove all the directors of Vanke, including Wang Shi and Yu Liang. On June 27, 2016, Vanke held the 2015 annual general meeting of shareholders at its headquarters in Shenzhen, and after the shareholders' meeting did not end smoothly, Vanke launched a counterattack. As more and more inside stories were exposed, the major interests of China Resources and Baoneng attracted the attention of the regulatory authorities, and the Shenzhen Stock Exchange issued a letter of inquiry to China Resources and Baoneng, requiring both parties to explain whether there were concerted actors. So far, both parties have expressed their support for Vanke's board of directors, and China Resources has directly rejected Baoneng's decision to convene an extraordinary general meeting of shareholders to remove a number of board members. So far, the board of directors and Vanke's management have won two consecutive games. There has been a fundamental reversal of the situation in the Baowan controversy. Due to the intervention of the State-owned Assets Supervision and

DOI: 10.54254/2754-1169/71/20241513

Administration Commission, China Resources had to gradually fade out of the Vanke equity dispute. After two days of huge holdings on July 5 and July 6, Baoneng's shareholding ratio finally came to 25%, triggering the fifth move [9].

According to the provisions of the Securities Law, after the shareholding reaches the red line of 25%, the shares of the listed company will not be allowed to be bought and sold again in the next two days. At this time, Evergrande bought a large number of Vanke shares, which made Vanke's shares skyrocket. Subsequently, Evergrande continued to invest in shares, but at this time, Baoneng did not choose to continue to increase its holdings after getting out of the liquidation alarm. Subsequently, the China Securities Regulatory Commission and the China Insurance Regulatory Commission formally intervened in the dispute with Baowan, and China Resources also received strict supervision from the State-owned Assets Supervision and Administration Commission [9]. Immediately afterwards, the China Insurance Regulatory Commission issued a regulatory letter to Yao Zhenhua's Qianhai Life Insurance, and simultaneously suspended the Internet insurance business of six insurance companies, including Qianhai Life Insurance and Evergrande Life, thus cutting off the most important source of funds for Baoneng Group. Subsequently, China Resources, Baoneng, and Evergrande successively transferred their shares to Shenzhen Railway Group, and the dispute between Baowan and Baowan came to a complete end.

4. Case Analysis

Seen from Table 2, as of the end of December 2014, Vanke's entire net asset income is gradually declining, it can be found that before the Baowan dispute, Vanke's entire development was affected by the stock market crash, resulting in the overall rate of return is not ideal, and the overall income has become a downward trend, so after the insurance funds entered the market in a big way, Baoneng will only have the idea of annexing Vanke after seeing the situation of Vanke.

Table 2: Vanke's net profit margin on total assets and return on net assets from 2012 to 2014.

Report date	Return on assets (ROA) A (%)	Return on Equity (ROE) A (%)
December 31, 2012	4.1348	19.0686
December 31, 2013	3.8183	17.3536
December 31, 2014	3.7937	16.6424

In the first large-scale acquisition of Vanke by Baoneng, Vanke first asked the company's largest shareholder, China Resources, for help, hoping that China Resources could increase its shareholding ratio to ease the pressure on Vanke, but due to China Resources' refusal, the plan ended in failure. Vanke's executives actively communicated with Anbang and introduced Anbang as their "white knight" to unite all forces against the invasion of Baoneng [11]. Later, when Baoneng re-invested, Vanke closed the stock market, and found another "white knight" Shenzhen Metro during this period, with the shareholding of Shenzhen Metro, the situation reversed, and after the implementation of the restructuring plan with Shenzhen Metro, it became the largest shareholder of Vanke in one fell swoop.

When Vanke was first acquired by Baoneng, because Baoneng's shareholding gave the shareholders hope, it was estimated that it would also rise temporarily, and after Baoneng held more than 25% of the shares, it was decided to lay off all Vanke's original board of directors, which made Vanke's original management team completely reshuffle, which also led to chaos within the entire shareholders' meeting. Due to the business war between Vanke and Baoneng, the stock price fell sharply, and it was at this time that Evergrande Group's purchase pulled the stock price back to save Baoneng from the risk of liquidation. During this period, Vanke's stock price fluctuated severely, and the company's development almost came to a standstill, which had a negative impact on the company.

DOI: 10.54254/2754-1169/71/20241513

As shown in Table 3, Vanke's overall investment income declined in the early stage of the Baowan dispute, and then slowly increased, while the total comprehensive income increased slowly in the three years of the Baowan dispute, that is, from 2015 to 2017, and the total comprehensive income of Vanke increased after the restructuring with Shenzhen Metro in 2017.

Table 3: 2014-2018 Vanke's total investment income and comprehensive income

Year	Investment income (RMB)	Total Comprehensive Income (RMB)
2014	4,159,261,964	19,352,124,836
2015	3,561,908,084	25,844,716,277
2016	5,013,835,862	28,311,311,326
2017	6,244,561,688	37,007,858,045
2018	6,787,934,513	46,279,008,441

As depicted in Table. 4, in the early stage of the development of the Baowan dispute, because of the addition of the Baoneng Department during the stock market crash, the shareholders, the board of directors of Vanke and the society gave hope to the shareholders, the board of directors of Vanke and the society, resulting in the rapid growth of Vanke's fixed assets at this time, but later due to the progress of the Baowan dispute, the company's overall fixed asset income seriously slowed down, and finally after the end of the Baowan dispute (after 2018), Vanke's development returned to the right track, and the income led to a rebound in the growth rate of fixed assets. During this period, due to the sudden acquisition of Baoneng and Evergrande in 2015, the stock price rose, which promoted the rise of Vanke's estimates, but in addition to the stock market crash, the stock price has been in a downward trend during the rest of the period, which shows that although during the hostile merger period, the investment of large enterprises will still have a positive impact on the stock price.

Table 4: Vanke's fixed asset growth rate and basic earnings per share growth rate.

Year	Growth rate of fixed assets (%)	Basic earnings per share growth rate
2014	8.3851	4.6
2015	113.0299	4.666667
2016	38.5017	3.259259
2017	4.2288	3.449275
2018	62.4751	3.102975

After the "Baowan dispute" was resolved, Vanke's share price quickly returned to normal, after a sharp rise due to large-scale acquisitions by Evergrande, Baofeng and other groups. The influence of the "Baowan dispute" has gradually dissipated, and the overall movement is basically in line with the trend of the real estate index. After a period of turmoil, Vanke's share price continued to fall as the real estate industry gradually entered a downturn. This represents the end of the equity competition between all parties in the "Baowan Dispute", and allows Vanke's stock price to end its long-term fluctuation and continue to develop in a stable manner.

5. Enlightenment and Reference

Hostile mergers and acquisitions will affect the operating conditions and development prospects of both companies, and the company's stock price and various related indexes will fluctuate significantly. Markets and governments in many countries are paying close attention to hostile mergers and acquisitions. The behaviors and strategies of malicious mergers and acquisitions participants will

DOI: 10.54254/2754-1169/71/20241513

inevitably be subject to supervision by multiple parties. In the process, the reputations of both companies will also be damaged, causing confusion to shareholders and investors. and worries. From a macroeconomic perspective, the stock market is contagious, and fluctuations in corporate stocks may have a certain impact on the entire market and even the national economy [12].

In the face of hostile mergers and acquisitions, target companies can also adopt many countermeasures and means. One of the most important elements in the successful execution of a merger or acquisition is the presence of a communication plan. The likelihood of a successful post-M&A integration can be greatly increased by using an effective communication approach. The formalization of the decision-making process, the outcomes of the M&A, and the external business environment are further drivers [13]. When a target company faces the threat of acquisition, it can seek help from friendly companies to find a more receptive buyer. Friendly companies often promise not to dissolve the company or dismiss management and other employees, and the target company will provide the friendly company with a more favorable stock price [14]. The target company may also choose to transfer a significant portion of its equity to a friendly company. Sometimes preferred stock, sometimes common stock, is offered to favorable companies. If it is the former, the friendly company has no voting rights; if it is the latter, the friendly company must guarantee that it will not sell these shares to the hostile acquirer. In addition, the target company can also adopt strategies such as adjusting the company's capital structure to improve its ability to resist mergers and acquisitions, and even reverse acquisitions of hostile acquirers to counter hostile mergers and acquisitions. The government also needs to introduce more relevant policies to limit the occurrence and subsequent adverse effects of malicious mergers and acquisitions in more in-depth detail.

6. Conclusion

Corporate mergers and acquisitions have become a frequent financial investment behavior in the financial market. At the same time, because they have had many serious impacts on target companies and even the entire market, malicious mergers and acquisitions have gradually been taken seriously by investors and managers. The boundaries between friendly mergers and hostile mergers are becoming increasingly clear. Once a friendly merger is struck, the acquirer and target company announce the deal together and often hold calls with shareholders and analysts to tout the benefits of the proposed deal. In contrast, hostile mergers and acquisitions often bring many undesirable consequences. When facing a hostile merger, the first thing that bears the brunt is the stock price of the target company. During the "Bao-Wan Controversy", Vanke Group's stock price fluctuated significantly, showing a completely different trend from the real estate index. Due to the fluctuations in stock prices, Vanke's development almost stagnated. This long-term counter-trend shock will definitely cause worries to shareholders and related investors, reduce their investment confidence in the company, and adversely affect the future development of the company.

In the process of hostile mergers and acquisitions, acquirers, also known as activist shareholders, often try to bypass the board of directors and management and conduct hostile mergers directly with shareholders to seize control of the target company. Throughout the merger and acquisition process, the hostile acquirer will gradually seize control of the target company by paying high prices to purchase the target company's shares, rearranging the senior management team, changing corporate principles, etc. There will always be changes in the target company's board of directors, and the management team will begin to shuffle, leading to internal chaos in the shareholders' meeting and seriously affecting the target company's operations and future development prospects. Hostile mergers may also divert the target's attention from its current operations and potential growth directions. They may even take actions that devalue the company to block a takeover bid. The target company's total asset net profit margin, return on net assets, investment income and other indicators will fluctuate significantly, which will have a serious adverse impact on the company's operating

DOI: 10.54254/2754-1169/71/20241513

income, industry credit rating, future development potential, etc. This article only studies the impact of failed hostile merger cases on the relevant companies within the case. There is no research on whether successful M&A cases will bring different consequences, which has certain limitations. This article analyzes the action strategies adopted by companies in hostile mergers and acquisitions and summarizes the short-term and long-term consequences that malicious mergers and acquisitions will bring to relevant companies, which has certain practical and theoretical significance. In the future, we can refer to other cases of hostile mergers and acquisitions under different circumstances to more comprehensively analyze and summarize the consequences of malicious mergers and acquisitions.

Author Contribution

All the authors contributed equally and their names were listed in alphabetical order.

References

[1] *Cartwright, S., and Schoenberg, R. (2006). Thirty years of mergers and acquisitions research: Recent advances and future opportunities. British journal of management, 17(S1), S1-S5.*

[2] *Chengtian Finance. (2023). The concept of corporate mergers and acquisitions. Retrieved from: https://www.citygassafe.com/article/17178.html*

[3] *Kumar, S., and Bansal, L.K. (2008). The impact of mergers and acquisitions on corporate performance in India. Management Decision, 46(10), 1531-1543.*

[4] *Oriental Fortune. (2012). Hostile takeover, 2012,01,31. Retrieved from: https://baike.eastmoney.com/item/%E6%81%B6%E6%84%8F%E6%94%B6%E8%B4% AD*

[5] *Conyon, M.J., Girma, S., Thompson, S., and Wright, P.W. (2001). Do hostile mergers destroy jobs?. Journal of Economic Behavior and Organization, 45(4), 427-440.*

[6] *Ebina, T., Kumakura, Y., and Nishide, K. (2022). Hostile takeovers or friendly mergers? Real options analysis. Journal of Corporate Finance, 77, 102292.*

[7] *Admin. (2013). How to distinguish between hostile acquisitions and friendly acquisitions. Retrieved from: http://www.0755lvshi.cn/binggoulvshi/20130916671.html*

[8] *Jiang, Z. (2023). Analysis of the motivations, paths and economic consequences of stakeholder participation in control struggle.Yunnan University of Finance and Economics.*

[9] *Qi, Y. (2021). How to prevent the risk of takeover and anti-takeover by the original shareholders of listed companies: A case study of "Baowan dispute"[J].Guangxi Quality Supervision Herald, 6, 96-101.*

[10] *Wu, Y. (2023). Research on anti-takeover strategy of listed companies in China[D].Central University of Finance and Economics.*

[11] *Zhu, Y. (2020). Research on anti-hostile takeover strategy of listed companies. Nanjing Agricultural University.*

[12] *Xu, G. (2015) How big is the macro impact of stock market shocks.Retrieved from: https://finance.sina.cn/china/cjpl/2015-07-08/zl-ifxesftm9849667.d.html?from =wap*

[13] *Papadakis, V.M. (2005). The role of broader context and the communication program in merger and acquisition implementation success. Management Decision, 43(2), 236-255.*

[14] *China Capital Alliance. (2021). Interpretation: Confrontation Strategies of Hostile Takeovers and Anti-takeovers. Retrieved from: https://www.sohu.com/a/465613080_270543*