

Discussing the Importance of Capital Operation to the Development of Enterprises with Practical Cases

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Abstract

Since the 1990s, due to the continuous improvement of China's capital market and the characteristics of capital operation to maintain and increase the value of enterprises, capital operation in China has been gradually developed, and many enterprises have achieved value enhancement through the means of capital operation. With the establishment and improvement of the market economic system, the significance of capital operation for promoting the development of enterprises has become increasingly prominent. Combining with specific cases, this paper further analyzes the importance of capital operation for enterprise development, and provides reference for enterprise strategy formulation.

Keywords

capital operation, enterprise development, great significance.

1. Introduction

With the rise of the wave of globalization, the scale of capital operation in the world is expanding day by day, at the same time the methods are also abundant. In the process of China's economic system reform, capital operation has also received great attention from domestic enterprises. At present, the reform of the economic system needs to be deepened, enterprises pay less attention to capital operation, and relevant domestic theories need to be perfected. In the face of these problems, this paper focuses on analysing the significance of capital operation, aiming at providing reference for the strategic decision-making of enterprises and promoting the development of the domestic capital market.

Wang Shuli (2000) made a preliminary exploration on the significance of capital operation of state-owned enterprises, and proposed that capital operation has certain significance for the maintenance and appreciation of state-owned capital and the reform of enterprise financing system. Zhu Junyi (2015) explored the theories and methods of enterprise capital operation and proposed relevant suggestions and measures. Combining the current sharing economy background, Zhou Honggen (2017) constructed the path of technological innovation and capital operation under the sharing economy from the perspective of technology capital generation and operation, laying a foundation for the further development of capital operation in the new era. So far domestic researches mainly aim at the state-owned enterprises and the method innovation of capital operation, lacking the inquiry of the significance for capital operation. Combining with the specific cases, this paper analyses the importance of capital operation to enterprises, market and government, which provides reference significance to promote enterprise capital operation process and the market system reform.

2. Capital Operation and its Methods Introduction

2.1. The Meaning of Capital Operation

In a broad sense, capital operation refers to achieving the strategic goal of capital appreciation and profit maximization through the organization, management, operation, planning and optimal allocation of available resources and production factors.

In the narrow sense, capital operation refers to a series of capital operation activities such as merger, acquisition, reorganization and appreciation of enterprises and external capital to achieve the goal of profit maximization.

Whether in a broad sense or a narrow sense, capital operation covers the whole process of production and circulation of an enterprise from a vertical perspective, while from a horizontal perspective, it is to optimize the allocation of all resources owned by an enterprise, including financial capital operation and equity capital operation. Starting with the narrow sense of capital operation, this paper studies the significance of the narrow sense of capital operation for the development of enterprises.

2.2. Capital Operation Modes

Traditionally, capital operations are divided into expansion and contraction.

Expanding capital operation includes horizontal capital expansion, vertical capital expansion and mixed capital expansion. Horizontal capital expansion means that under the premise of the same type or field, enterprises of both sides conduct transactions to achieve scale effect, optimize industrial structure and enhance market competitiveness of enterprises. Vertical capital expansion refers to the trade between different enterprises in the upstream and downstream of the industry based on the industrial chain. Through vertical expansion to achieve the improvement of bargaining power and strengthen the control of the industrial chain. Hybrid capital expansion refers to the integration of resources through cross-border transactions between unrelated enterprises in different industries. On the one hand, enterprises can enhance their anti-risk ability and market competitiveness through hybrid capital expansion. On the other hand, it helps enterprises to adapt to the diversified trend of market competition and enhance market competitiveness.

Contractionary capital operation includes divestiture, company division, share repurchase, spin-off and listing.

Common capital operation methods: company listing, merger and acquisition and asset reorganization, as shown in table 1.

Table 1: Common capital operation modes

Company listing	Direct listing Indirect listing (shell buying, backdoor, shell making)
Mergers and acquisitions	Enterprise merger Asset purchase Equity acquisition
Assets reorganization	Asset reorganization (divestiture, replacement, sale and transfer of assets) Debt restructuring Management restructuring, etc

3. The Significance of Capital Operation

Capital operation is the product after the practice of western capital market. It activates the assets by redistributing the tangible or intangible assets of enterprises and achieves the purpose of maintaining and increasing the value of enterprises. In the face of the current Chinese capital market, although it is gradually improving, the development of enterprises is still limited. However the introduction of capital operation will enable enterprises to make better use of existing assets and achieve long-term development. Therefore, no matter from the perspective of enterprises or the market, capital operation is the only way for enterprises to develop, and it is also an important way to promote enterprises to achieve a leap forward. This paper expounds the significance of capital operation from three aspects: enterprise, market and government.

3.1. Enterprise

(1) It helps enterprises to expand financing channels. At present, most Chinese enterprises use loans and loans for financing, and the issuance of bonds has certain requirements for the size of the net assets of enterprises. Therefore, the single financing method and high financing cost have become a bottleneck for the development of Chinese enterprises. Capital operation can effectively solve the problem of insufficient funds of enterprises, such as raising idle funds from the capital market through listing and operating with the funds of the merging party through enterprise merger. These means can enable enterprises to obtain development funds and achieve further development.

(2) It can effectively expand the scale of enterprises and improve market share. In the horizontal expansion mode, enterprises can promote the integration of technology level and other aspects by merging with the same type of enterprises, so as to realize the integration of the market, thus forming the scale effect and improving the profit level with the decrease of costs. Under the vertical expansion mode, enterprises could strengthen the control of the industrial chain, increase product varieties, realize the integration of upstream and downstream, and enhance the market competitiveness of their products or services.

(3) It can maintain and increase the value of enterprise assets and promote the optimal allocation of resources. The goal of capital operation itself is to organize, manage, plan, and optimize the allocation of available resources and production factors, so as to maximize the benefit of resources. For example, enterprise acquisition is an efficient allocation of the acquired party, and business restructuring is also a redistribution of sluggish business. These operation modes can reconfigure idle or unreasonable resources to optimize resources.

(4) It is conducive to maximizing the operating profit of the enterprise. Idle resources held by enterprises will also be expended at a cost, such as depreciation of idle fixed assets. The unreasonable use of resources will also lead to the increase of costs and the emergence of sunk costs. Capital operation is targeted at the resources of the enterprise, through an effective way to not only control costs, reduce unnecessary sunk costs, but also improve the strength of the enterprise to increase profits.

(5) It can effectively reduce business risks. Through capital operation, managers can get to know the real value of enterprise assets and turn passive management into active management, so as to effectively avoid the risks brought by wrong operation methods. In addition, methods such as mergers can enhance the ability of a single firm to cope with risks, while also providing more resources to cope with risks.

(6) It can encourage enterprises to establish effective constraints and incentive mechanisms. Capital management requires the enterprise to operate independently and be responsible for its own profits and losses. Due to the pursuit of profits, enterprise will establish an effective mechanism to effectively control the whole process before, during and after operation.

(7) It help to establish brand image and enhance corporate cohesion. In today's information technology era, enterprises' capital operation activities will achieve effective publicity through various media, thus highlighting the brand effect. At the same time, it is also an incentive for employees. The expanded capital operation marks the enhancement of the enterprise's ability, while it is also a positive guidance for employees which can enhance their enthusiasm and work motivation, cultivate their loyalty to the enterprise brand, and achieve the purpose of cohesion.

3.2. Market

(1) It is conducive to establishing a modern enterprise system and improving the market mechanism. Capital operation is the most reasonable and efficient allocation of resources which follows the law of market development,. The strengthening of capital operation of enterprises is conducive to the formation of effective capital combination, competition and value-added mechanism, so that the capital market plays a decisive role in the allocation of resources. It is consistent with the requirement of our country's economic development coincide in recent years.

(2) It helps enterprises follow the trend of globalization and better realize "Going Global".

With the development of information technology, globalization is unstoppable. Effective overseas mergers and acquisitions can enable Chinese enterprises to "Go Global" and make better use of foreign capital and advanced technology to achieve the long-term development of enterprises. At the same time, it also meets the requirements of the country to promote enterprises to the world, which is conducive to improving China's financial market.

(3) To a certain extent, it contributes to guide investors to avoid investment risks. Whether the expansion or contraction of capital operations, they are a hint for investors that the current operating and financial conditions of the enterprise. Investors can track the changes of enterprises before and after capital operation to effectively evaluate whether other enterprises are worthy of investment, which is an effective way for investors to avoid investment risks.

3.3. Government

It is helpful for the government to simplify the examination and approval procedure, change "manager" into "supervisor" and strengthen the supervision function. To actively promote the capital operation of enterprises means that the government should reform the existing approval and supervision system, and explore the mechanism of "leniency and strict management" which will promote the standardization and transparency of government regulation, so as to better realize the construction of service-oriented government.

4. Specific Case Analysis

4.1. Qihoo 360 Backdoor SJEC Corporation Successfully Listed

Qihoo 360 technology co., LTD., founded in 2005, withdrew from the US stock market after its privatization in 2016. The transaction plan includes two parts: one is based on the value of SJEC Corporation's all assets at RMB 1.872 billion, in which SJEC Corporation exchanged assets worth RMB 182 million with the equal value of Qihoo 360, and sold the remaining assets worth RMB 1.69 billion to the original actual controller of Qihoo 360. In addition, SJEC Corporation issued 6.367 billion shares to Qihoo 360 at 7.89 yuan per share, and Qihoo 360 subscribed for 50.235 billion yuan of assets. After the transaction is completed, all assets of Qihoo 360 are injected into SJEC Corporation and Qihoo 360 become the actual controller of SJEC Corporation.

The backdoor listing has great significance, the market price of Qihoo 360 has increased nearly 6 times, and many consortia involved in Qihoo 360's merger, such as CITIC Securities, China Renaissance, Sequoia Capital, all have obtained rich investment returns. This transaction achieved a multi-win situation. At the same time, for Qihoo 360 itself, firstly, it successfully raised a large amount of funds from the A-share market, laying A foundation for its development in scientific research and other aspects. Secondly, relying on the domestic capital market, it adjusted the distribution of industries and services and improved the core competitiveness of enterprises; At last, it has greatly improved its brand influence and become a famous Internet enterprise in China.

4.2. China Merchants Bank Successfully Acquired Hong Kong Wing Lung Bank

China Merchants Bank (CMB) was founded in Shenzhen in 1987 and listed on the Shanghai Stock Exchange and the Hong Kong Stock Exchange in 2002 and 2006 respectively. From the perspective of capital acquisition, CMB chose to issue subordinated debt for financing and paid in full cash. The transaction was divided into two stages: in the first stage, CMB paid 134.43 yuan per share, totaling 16.1 billion yuan in cash, to acquire 123 million shares of Wing Lung, accounting for 53.22% of the shares. In the second stage, CMB began to launch a general offer for the remaining 46.88% of the shares to all shareholders at 130.43 yuan per share, receiving 230 million shares. At this time the purchased part accounted for 97.82% of the total shares. According to the related rules, the ratio is more than 90 percent, so CMB has the right to the remaining 2.18 percent of the shares for mandatory acquisition. The acquisition cost a total of 303 billion yuan.

For Wing Lung, the acquisition has transformed and improved its brand image, number of customers, operation level, management ability, asset scale and profitability. For CMB, the transaction helped perfect the international sales network and cross-border services platform and integrate the resources, achieving customer sharing, improving financial efficiency and increasing their income. The most important thing is that the two sides complement each other's strengths, seek common ground while reserving differences, and make steady progress.

4.3. Geely Successfully Acquired Volvo

Geely was founded in 1986 and listed on the Hong Kong Stock Exchange in 2005. In 2010, Geely acquired 100% of Volvo cars' equity and related assets for \$1.8 billion, as well as the ownership of the brand. The deal was leveraged to raise nearly \$1.78 billion from banks, investors and Goldman sach. Equity of Geely itself only accounted for only 1.6 per cent of total funds.

Firstly, this cross-border merger and acquisition can help Chinese self-owned automobile enterprises enter the international market as soon as possible, accelerate the internationalization process of Geely, improve its domestic and foreign popularity, and promote its brand building. Secondly, Geely acquired high-end research and development technology through merger and acquisition, making it get rid of low-end image, broaden its consumer group range and expand market share. Finally, the two sides can effectively realize the combination of strong and strong, and develop and grow together.

5. Conclusions and Recommendations

The case analysis reflected capital operation for the further development of the enterprise is very important. Companies with a long-term perspective tend to include capital operation in the strategic plan. It is important to note that there are many capital operation modes, the enterprises need to adjust measures according to local conditions and choose suitable ways for their own development, so as to play a positive role of capital operation.

Based on the above analysis, the following suggestions are proposed:

- (1) The enterprises should have a long-term strategic vision and list the capital operation into development plan. At the same time, managers should be rational and not be blind expansion.
- (2) Enterprises should choose the appropriate mode of capital operation according to the type of idle resources and their own ability. Only the suitable mode can promote the long-term development of enterprises.
- (3) The risks in the process of capital operation should be paid attention to. Due to different ways of capital raising and changes in external conditions, enterprises will face greater financial and operational risks in the process of capital operation. Therefore, enterprises should establish an effective risk response mechanism in the whole process of capital operation.
- (4) Enterprises should improve the internal control and supervision mechanism of capital operation. Internal control is extremely important for the development of enterprises, and it can timely find out the problems existing in the development process of enterprises. In the process of capital operation, internal control and supervision mechanism are also needed to conduct supervision, so as to timely find out and solve problems when engaging in capital operation and reduce the probability of risks.
- (5) The capital operation should combine with Internet, so as to realize efficient capital operation. Under the background of the rapid development of Internet, the effective combination of electronic information technology and capital operation is worth exploring and practicing. From the perspective of fund raising, P2P loans, crowdfunding and Yu 'e Bao loans can be selected to conduct and manage the whole process of capital operation through the Internet. However, managers should pay attention to the control of risks and enterprises need a complete risk monitoring mechanism.

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