

Analysis on Motivation and Risk of E-commerce M&A: Alibaba's Acquisition of Sun Art Retail

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Abstract. With the rapid development of e-commerce in China, the competition among enterprises in the market is becoming increasingly fierce. Many enterprises try to obtain competitive advantages in the market and reduce the risk exposure through mergers and acquisitions. However, corporate mergers and acquisitions is a complex activity and there exists various risks in the process, e.g., financial risk, which directly affects the success of M&A and the development of enterprises after M&A. Based on the case of Alibaba's acquisition of Sun Art Retail, this paper investigates the possible risks of M&A based on motivation analysis and performance analysis. According to the analysis, the acquisition of Sun Art Retail in the short term has brought great growth ability to the profitability of Alibaba, but reduced the debt solvency of Alibaba as well. Given the result of the analysis, this study provides three main measures to manage risks and improve the risk management capability. Overall, these results shed light on guiding further exploration of e-commerce mergers and acquisitions and the new retail model.

Keywords: Company merger and acquisition; risk exposure; e-commerce company.

1. Introduction

E-commerce has brought a huge impact on the traditional retail market, resulting in flat retail channels and higher retail efficiency. However, at the same time, the shortcomings of e-commerce are also obvious, i.e., the lack of offline vivid display opportunities. As a domestic e-commerce giant, Alibaba has long seen the shortcomings of e-commerce and began to pay attention to the offline retail market around 2015 [1]. In recent years, Alibaba has made constant mergers and acquisitions and financing to expand its influence in the offline sector. For example, it has bought shares in express companies such as ZTO and YTO, and built Cainiao Courier Station, which was a transformation of the offline sector, integrating online shopping and offline distribution, and upgrading the original industrial chain. Subsequently, in 2014, Alibaba entered the tourism industry and bought shares in Qiongyou.com and other enterprises, which was the first time for Alibaba to enter non-main business. Afterwards, in 2018, Alibaba acquired Ele.me, breaking through its zero-business volume of take-out. The company is committed to opening the entire supply chain of the offline retail market. After completing the improvement of delivery services, Alibaba believes that it needs to make a new breakthrough in the terminal retail link. After investigation, Alibaba believes that Sun Art Retail's traditional retail channels have penetrated cities at all levels in China, and its subordinate RT-Mart and Auchan are hypermarket models, which can provide sufficient offline display and experience opportunities [2]. Alibaba believes that the acquisition of Sun Art Retail can drive offline drainage, realize the integration of online and offline, and realize O2O three-dimensional marketing. In addition to Sun Art Retail, retail giants such as Metro, Walmart and Watsons have insufficient outlets, which makes it difficult to cover the whole region. These enterprises are usually concentrated in first-tier and second-tier cities, which can effectively connect with the existing offline distribution services. Only Sun Art Retail can give full play to the advantages of offline links and reduce the cost of supply chain management. Alibaba is therefore more inclined to buy Sun Art Retail.

Based on the synergy theory and supply chain management theory, there are still financial risks in Alibaba's acquisition of Sun Art Retail. The research shows that vertical merger and acquisition of non-main business will bring cost changes, and the cultural differences between them will lead to the instability of enterprise operation efficiency. As a domestic e-commerce giant, studying the motivation and risk of Alibaba's merger and acquisition of Sun Art Retail can provide a basis for the merger and acquisition of other e-commerce enterprises. However, as time goes on, COVID-19 has broken this situation. The biggest black swan event since the 21st century has brought a huge impact on the global economic environment, both real economy and virtual economy. The depression of the global consumer market, the bankruptcy and closure of small and medium-sized enterprises, countless people are facing unemployment and employment problems. Sun Art's earnings fell sharply, making it the lowest profit since it was acquired. Such a result and situation are the two companies never expected. It also indirectly leads to the acquisition of failure is inevitable.

2. Descriptions

Alibaba Group was founded in 1999, the company's main business is the Internet business, including Tmall, Taobao, Juhuasuan, 1688, Ant Financial, Cainiao Network and many other brands. In the 2017 fiscal year of merger and acquisition, the overall revenue was CNY 158.273 billion, an increase of 56% compared with that of 2016. The number of active users reached 507 million, and the net profit of the enterprise reached CNY 57.871 billion. The company has started offline layout around 2017, completed the merger and acquisition of the express industry, and then started to investigate the retail industry. The company has bought shares in Intime, hoping to have more shares offline.

Sun Art Retail was established in 2000. The company is mainly engaged in retail business, with hypermarkets as its main business type. The main brands of the company in mainland China are Auchan and Da Runda. Sun Art went public in 2011. The company's high point came in 2011, when revenue and net profit jumped 55.2 percent. After 2014, with the impact of new retail and e-commerce, the enterprise suffered from an operating crisis. Sun Art Retail encountered operational obstacles around 2017. Cost growth and the disorderly expansion of e-commerce led to great fluctuations in the revenue of the enterprise. According to the annual report of Sun Art Retail in 2016, the net profit of the enterprise was CNY 2.571 billion, with an increase of only 5.24%, while in 2015, the net profit of the enterprise even showed a situation of -15.99%. Considering profit fluctuation and market competition pressure, Alibaba's merger is the best choice for enterprises.

Alibaba bought Sun Art Retail in 2017. On November 20 of the same year, Alibaba issued the purchase offer and officially announced that the amount of capital invested reached CNY 22.4 billion y. In this way, Alibaba directly held 36% of the shares of Sun Art Retail and became the second largest shareholder [3]. In 2020, Taobao China, a subsidy of Alibaba, invested another US \$3.6 billion (HK \$28 billion) to acquire a stake from other controlling parties, ultimately bringing Alibaba's economic interest in Sun Art to 72%.

Sun Art started laying out offline stores as early as 1998 and launched its own e-commerce platform, Feiniu, in 2014. By the end of 2017, Sun Art Retail had more than 400 retail stores nationwide, covering more than 200 cities. Sun Art has numerous offline stores and delivery platforms, which Alibaba values most [4]. Alibaba has always hoped to achieve the integration of offline and online, and Sun Art Retail is the most ideal target across the retail market of China. At the same time, Sun Art Retail is also weak in the traditional retail market. After its listing in 2011, Sun Art suffered from the impact of e-commerce and its revenue went from bad to worse. Therefore, the merger and acquisition can achieve deep integration and achieve a win-win result.

3. Merger Motivation Analysis

3.1 External Causation

With the continuous improvement of residents disposable income, consumers focus on products has gradually changed from price to consumption experience. The huge market potential brought by China 's huge population base and the demand of Chinese consumers to improve the quality of life have brought great opportunities and challenges to the transformation and development of the retail industry [5]. At the 2016 Yunqi Conference, Jack Ma, the founder of Alibaba Group, first proposed the concept of "new retail" pointing out that in the next ten years or even twenty years, the retail industry will enter the new retail era from the traditional pure e-commerce era to the combination of online and offline and logistics [6]. Under the background of new retail, many traditional supermarkets have carried out cerebation and exploration on transformation, building and improving the new retail ecosystem.

As more and more e-commerce enterprises enter the market, the market share of individual e-commerce enterprises is constantly squeezed. Nowadays, the profit of online sales alone is not enough to maintain the healthy development of e-commerce enterprises. In addition, the marketing of e-commerce companies can now be carried out through live broadcasts, Weibo, WeChat public accounts, etc., and the increase in traffic costs also forces companies to find competitive advantages in other areas. Mining offline entities can make consumers' consumption scope more diversified, and create a new business model of online service and offline experience, which can bring and fix customer groups for enterprises. Therefore, the retail model of online and offline integration has become a new field of innovation in the e-commerce industry [7].

In 2016, General Office of the State Council of China issued the "Opinions on Promoting the Innovation and Transformation of Physical Retail" and gave the overall development direction plan of new retail. In terms of guiding ideology, the government encourages e-commerce enterprises to change from decentralized and independent competitors to integrated and coordinated new ecology, thus reducing circulation costs and improving circulation efficiency [8]. Under the guidance of the government, the merger and acquisition of retail enterprises and the integration of resource advantages can expand the operation scale of enterprises, help to promote the upgrading of the overall economic structure of the retail industry, improve economic efficiency and efficiency, and realize the strategic layout of enterprises.

3.2 Internal Motivation

Alibaba has long cultivated the online market with sufficient cash flow and information technology advantages, but lacks physical retail experience. Under the new retail model, its idea of re-opening the offline retail market not only requires a lot of capital investment, but also faces many barriers. As a large commercial super leading enterprise, Sun Art Retail has been trying to expand its online retail business. However, at present, the monopoly situation of China 's e-commerce market has been formed. It is extremely difficult for Gaoxin to successfully build a new e-commerce platform alone, and cooperation with existing e-commerce platforms has become a better choice.

Therefore, this merger and acquisition hopes to achieve synergy between Alibaba, which has capital and technical advantages, and Sun Art Retail, which has a broad offline retail market. After the merger and acquisition of the two sides, Alibaba was able to successfully open up the offline retail market at a lower cost, and Sun Art Retail also opened up online business. At the same time, the two sides can achieve supply chain sharing, greatly saving the cost of building a new supply chain. Therefore, mergers and acquisitions by both parties can improve operating efficiency and achieve synergies [9].

One of the motivations for Alibaba 's acquisition of Sun Art Retail is diversification, which not only expands the scope of business, but also integrates more diversified formats. The combination of Alibaba and Sun Art Retail is an attempt to integrate the Internet industry with the traditional retail industry, and it is also a mutual empowerment and upgrading of the business [2]. Online, Sun Art

Retail's Darunfa stores began to access Taobao APP and share user data with Alibaba, objectively increasing the user base of RT-MART.Offline,RT-MART began to put on the shelves of Alibaba 's Hema Fresh 's own brand goods, and screened out the explosive products according to Alibaba 's big data analysis ability, presented them on the shelf,and increased sales and sales profits.Consumers can not only enjoy a high-quality consumption experience in offline stores, but also buy goods from RT-MART stores online without leaving home [6].

4. Performances Analysis

Based on the financial data of Alibaba before and after the acquisition from September 30,2020 to December 31,2020, the financial analysis is carried out from the aspects of debt repayment, profit, operation and growth ability. As shown in Fig. 1, Alibaba 's operating income, gross profit and return net profit after the acquisition were significantly higher than those before the acquisition, and the return net profit was twice as high as that before the acquisition, indicating that the acquisition of Sun Art Retail in the short term has brought great growth ability. After the acquisition, its profitability indicators have increased, indicating that the profitability has not been significantly affected by the acquisition of Sun Art Retail, but may have enhanced profitability to a certain extent (seen from Fig. 2).

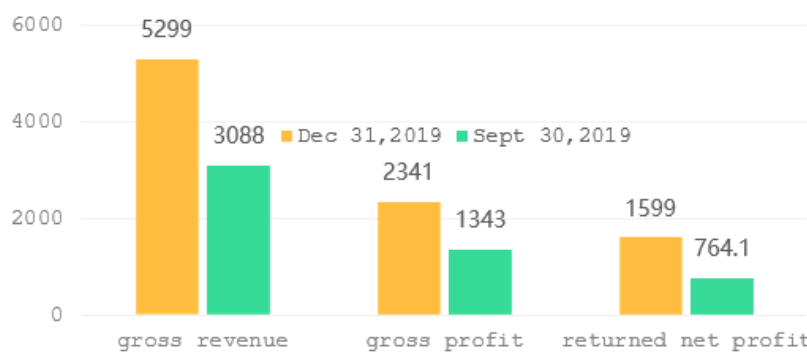


Fig 1. Alibaba growth capacity data before and after the acquisition(Unit:100 million yuan).

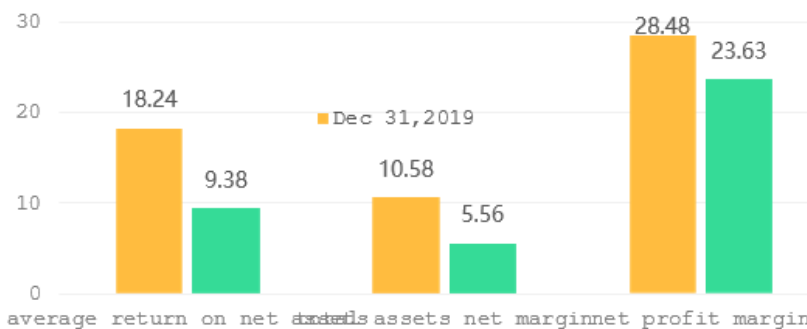


Fig 2. Alibaba profitability data before and after the acquisition(Unit:%).

After the completion of the acquisition, the tax rate of Alibaba 's income tax was lower than that before the acquisition (as depicted in Fig. 3), while the ratio of operating cash flow to operating income was higher than that before the acquisition, indicating that the acquisition played a role in tax reduction and cash flow increase, and improved its profit quality. Moreover, the current ratio of Alibaba before the acquisition was about 2, and decreased to 1.67 after the acquisition (as illustrated in Fig. 4), indicating that the acquisition reduced the short-term solvency of Alibaba. The asset-liability ratio and current debt ratio have increased slightly, indicating that the long-term debt capacity has declined, and the financial leverage has not been used well, weakening the solvency of enterprises.

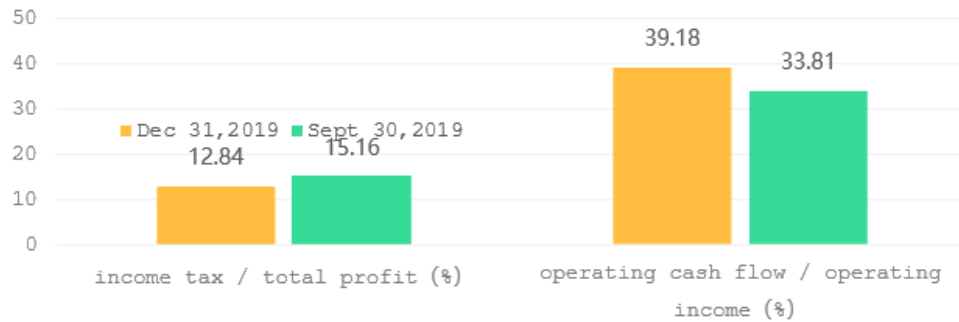


Fig 3. Alibaba earnings quality data before and after the acquisition (Unit:%).

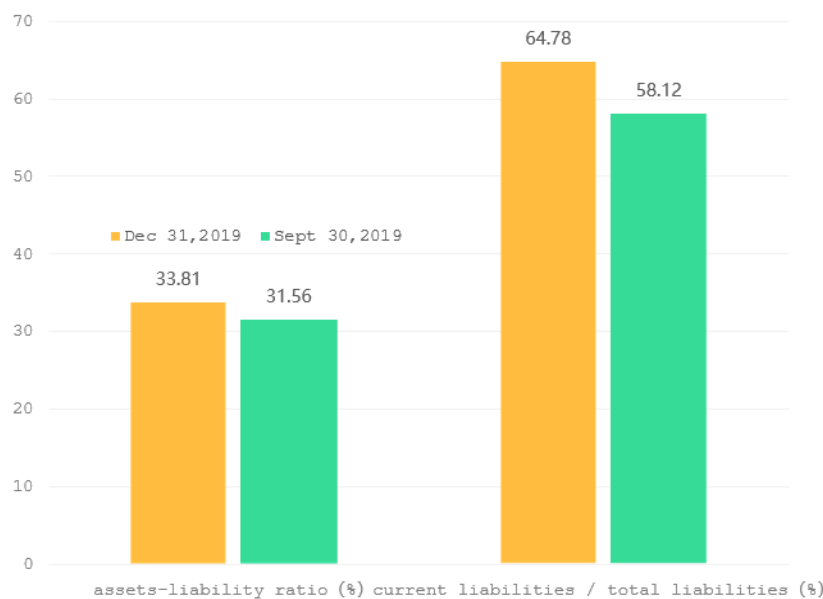


Fig 4. Alibaba earnings quality data before and after the acquisition (Unit:%).

5. Suggestions & Implications

First, one needs to accelerate the business integration and corporate culture fusion of Alibaba and Sun Art Retail. After the mergers and acquisitions, Alibaba and Sun Art Retail should complement each other's strengths and find commonalities, integrate each other's business in various aspects such as resources, technology and products, and share each other's platforms to find new growth points for their business, thus bringing into play synergy and scale effects and putting the two companies on the right track as soon as possible [10]. Its acquisition of Sun Art Retail is a typical case of integration of Internet e-commerce and retail industry. Based on the differences in business scale and internal business strategies, both companies should adjust the relevant systems and policies as soon as possible and train their docking staff. Meanwhile, both enterprises should strengthen communication and exchange, understand and pay attention to the opinions of management and employees, and make readjustment to the diversified business operation.

Second, it is necessary to establish a sensitive risk control system to prevent M&A risks. Inside the enterprise, financial management and audit should be strengthened to fully understand the financial information and operation of the enterprise before and after the M&A; outside the enterprise, the current market risks should be fully understood, and the risk control department should make early warnings for each risk in time and prepare response plans in advance.

Moreover, one needs to set clear corporate development goals and directions. Internet e-commerce and retail industry integration to clarify the future development of enterprise planning, do a good job of internal policy adjustment. Whether it is the integration of online and offline or digital upgrade to launch a new retail model, enterprises should be based on the development goals and market orientation to develop a reasonable development strategy.

6. Conclusion

In summary, Alibaba's acquisition of Sun Art Retail is a typical case of the integration of Internet e-commerce and retail industry. Whether it is the combination of online and offline operation mode or the digitalization to accelerate the realization of the "new retail" concept, it reflects the broad prospect of this merger and acquisition, but the risks of the merger and acquisition should not be ignored. However, the risks of M&A should not be ignored. After M&A, enterprises should strengthen their financial management and risk monitoring, understand the market trends, clarify their development goals, and designate reasonable development strategies to lay a solid foundation for future integration and development. Nevertheless, this study has some shortcoming, e.g., the analysis of the financial reports of Alibaba and Sun Art Retail is insufficient. For further study, a thorough research of the influence of this M&A will be done and the observation time will be longer. Overall, these results offer a guideline for the merger and acquisition of e-commerce enterprises and the development of online and offline combination retail.

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