

## Case study of Midea Group's merger with Little Swan

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### Abstract

**Faced with fierce market competition and changing markets, many companies choose mergers and acquisitions to expand business scale or achieve new business directions, expand into new areas, achieve business diversification, improve competitiveness, and maintain original business conditions and field. In recent years, other companies that need to merge can refer to the analysis results and make correct merger and acquisition decisions by analyzing the performance of the merged company. This article introduces the merger and acquisition of Swan on the American Stock Exchange, and uses financial performance analysis and case analysis techniques to analyze the financial performance of the Midea Group's merger and acquisition. It is hoped that the analysis results will have certain reference value and relevance to the merged company.**

### Keywords

**Share swap merger; financial performance; Midea Group.**

### 1. Case introduction

Midea Group was founded in 1968 and is headquartered in Foshan City, Guangdong Province. It is a technology group integrating consumer electronics, heating and air conditioning, robotics and automation systems, smart supply chain, chip industry and elevator industry. It has approximately 200 subsidiaries around the world, over 60 overseas subsidiaries, and 10 strategic business units. In the 1980s, Mei officially entered the home appliance industry and registered its own brand in 1981. In 2014, Mei Group recruited a total of 130,000 employees and owns more than ten brands including Meizu, Little Swan, Weiling, Huawei, Ande, and Meizu. Wuxi Little Swan Co., Ltd. mainly produces and operates household and commercial appliances such as washing machines, air conditioners, refrigerators, and dishwashers. In 1978, China's first fully automatic washing machine was born. In 2010, his brand reached US\$15.016 billion. China has become the world's third largest washing machine manufacturer, capable of simultaneously producing a full range of automatic axial-flow washing machines, front-loading washing machines and hybrid washing machines.

### 2. M&A process

On January 14, 2008, Little Swan announced that the company's controlling shareholder Wuxi Guolian Group planned to transfer its 24.01% stake in the company through a public solicitation of interested transferees. Due to conditions, only Midea and Changhong are most likely to acquire Little Swan. Sichuan Changhong proposed mutual shareholding, or partial cash and partial shareholding plans, but they were all rejected by Little Swan. Midea Electric submitted a transfer offer letter to Guolian Group on February 15, 2008, and signed a "Share Transfer Agreement" on February 26, 2008. According to the agreement, Midea Electric intends to transfer 87,673,341 shares of Little Swan held by Wuxi Guolian. The share transfer fee is RMB 1.68 billion. The transferred shares will reach 24.01% of Little Swan's total shares. From then

on, Midea's interest in Little Swan The company carried out mergers and acquisitions for the first time and became the controlling shareholder.

From 2008 to 2013, Midea Group continued to increase its holdings in Little Swan Company. When Midea Group was listed, in 2013, Midea Group already held more than 50% of the shares. When the shareholding ratio reached 52.67%, Midea Group maintained its share of Little Swan shares for several years. It was not until 2018 that this status was broken. Midea Group launched a second merger and acquisition of Little Swan Company.

In this second merger, first of all, on September 9, 2018, both parties to the merger and acquisition suspended trading and issued announcements to publicly announce the merger and acquisition. In this second merger between Midea Group and Little Swan Company, Midea Group's merger plan is to adopt the method of share exchange and absorption. Midea's plan is aimed at Little Swan shareholders who agree to the merger. Midea will acquire its shares in Little Swan through the issuance of new shares. Regarding the issuance of new shares, Midea chose to circulate on the main board of the Shenzhen Stock Exchange. After the merger is completed, Midea plans to cancel all Little Swan-related stocks. After the completion of this merger, all resources under the name of Little Swan Enterprise will belong to Midea.

Midea's plan for this merger is to issue new shares in exchange for the shares held by Little Swan shareholders. Since the actual controllers of Midea Group and TITONI are the same, and both hold shares of Little Swan, during the entire process of share exchange, Midea only needs to purchase the shares held by other shareholders. The share exchange price in Midea's merger plan is based on the average market price of the 20 trading days before the announcement date. However, since both parties have distributed the company's profits to shareholders from the announcement date to the completion of the merger, the stock value estimates of both parties to the merger and acquisition have also been adjusted accordingly. In short, the specific plan for this merger is that Midea will issue 323,657,476 new shares at 40.74 yuan/share to replace the 202,503,775 A shares at 46.91 yuan/share and the 96 A shares at 38.07 yuan/share. 830,930 B shares were purchased, thus privatizing Little Swan and becoming a subsidiary of Midea.

### **3. Changes in governance forms before and after mergers and acquisitions**

#### **3.1. Reform the business department system and establish and improve the decentralization system**

The company has been implementing product-based ownership reforms for U.S. businesses since 1997. Five major business departments have been established, including air conditioners, household appliances, compressors, engines and kitchenware. Systematically introduce outstanding professional management talents. The group headquarters only manages finance, budgeting, investments and the appointment and staffing of professional managers. The businesses listed below have a high degree of autonomy and can independently manage all aspects of the entire value chain, including R&D, manufacturing, sales, and even service industries. At the same time, each business segment has human resources expertise, allowing business unit CEOs to organize their own management teams and have the authority to approve tens of millions of dollars. The logic of the American reform is that since \$3 billion is the upper limit for management, the company is divided into smaller individuals. .

#### **3.2. Establish a relatively complete organizational system**

There are four main aspects: audit constraints, disciplinary constraints and legal constraints. Midea Group has established a relatively comprehensive disciplinary supervision organization system, audit organization system and financial budget organization system. This mechanism

not only ensures the appropriate distribution of power and encourages professional managers, but also prevents the abuse of power. Establishing a sound and clear organizational structure is an important guarantee for the decentralization of power by major shareholders. He Xiangjian delegated responsibilities to the business departments responsible for production, production and sales, and guide the company toward a business model in which shareholders, the board of directors, and the management team “share power.” .

### **3.3. Reuse professional managers and gradually withdraw from family management**

He Xiangjian took this opportunity to persuade some American entrepreneurs to exit through restructuring and business unit diversification. Particular emphasis is placed on establishing incentives, decentralization and accountability mechanisms. In the 2000s, the United States continued to comprehensively promote the management of secondary subsidiaries under the management of enterprises and business units, and began to implement MBO. In 2001, the management buyout (MBO) was completed and transformed into a private company, which partially solved the group's institutional problems in the United States, led the group to embark on the path of managing professional managers in the United States, and further promoted the group's professional management in the United States. Under the guidance of professional managers, the beauty team has developed rapidly. In 2004, the joint venture company successively acquired Hefei Rongxida and Guangzhou Valin, further expanding and consolidating the home appliance industry. In 2008, the acquisition of Swan further enhanced the competitiveness of the ice washing plant.

### **3.4. Introducing strategic investors and diversifying the equity structure**

In 2009, He Hengjian resigned as a director of the electrical company and continued to maintain absolute control of American Electric, accounting for more than 40%. However, since 2009, the He family's control has begun to decline. The decrease in 2009 was mainly due to the listing of 189,106,922 shares, resulting in a relative decrease in total capital. Rongrui Investment holds 12.18% of the shares of the controlling shareholder Mei Investment Holdings Co., Ltd., and CDH Investment holds 3.12% of the shares. As the He family's share in Midea Group decreased, their indirect participation in American Electric decreased. According to people familiar with the matter, this move will not only help improve the U.S. governance mechanism, but also speed up the group's strategic integration and overall listing. According to He Xiangjian, this also clears the way for a common roster for future teams.

### **3.5. Changes in strategic development planning**

In 2005, the U.S. government took over Jiangsu Chunhua and formulated the "Eleventh Five-Year Plan" for Midea Group, which comprehensively outlined a grand blueprint for the future development of the United States. In 2006, the United States carried out equity reforms, introduced strategic investors, and introduced option incentives. Midea's development has gone through three stages: the first stage - 80 years since its establishment. This leadership development focusing on fan product operations has laid the foundation for the subsequent development of the beauty brand. The second phase was an attempt at diversification in the 1990s. In the mid-1990s and late 1990s, Midea began to actively participate in efforts to diversify consumer devices on a solid business basis. The third stage is the rapid expansion stage that started in 2000. At this time, the United States has entered a stage of rapid business expansion and has gradually become China's richest production line and the most powerful overall force. From that moment on, as it continued to grow and develop, it gradually transformed from a single US\$120 billion international consumer electronics manufacturing group.

## 4. Operation status of the merger and acquisition so far

After the merger, Midea Group has integrated Little Swan's brand, human resources and culture.

### 4.1. Brand integration

Brands can correspond to different customer groups, so that companies can better expand their market share and gain a firm foothold in market competition. In this acquisition, Midea integrated Little Swan, which just met Midea's demand for washing machine brand positioning. Little Swan's washing machine brand can help it open up the washing machine market.

### 4.2. Human resources integration

For enterprises, human resource management is the most critical part. In order to ensure the overall efficient operation of its internal operations, it is Midea's consistent style to manage the company while respecting the operations and regional characteristics of the acquired company. Midea's human resource integration for Little Swan management can not only maintain the effective operation of the original Little Swan, but also promote the overall control of Midea Group. After the management integration is completed, there is also the integration of the employees of the original Little Swan Company. Without so many skilled workers, Little Swan would not be as big as it is today. It is the unremitting efforts of many R&D personnel and technical workers that make Little Swan possible. Only Swan will always be able to stand firm in the field of washing machines. After Midea acquired Little Swan, these R&D personnel and technical workers were retained by Midea and continued to work for Midea, helping Midea control costs and develop new technologies.

## 5. Financing of mergers and acquisitions

Midea's acquisition of Little Swan did not involve financing. Judging from whether this transaction of Midea Electric Appliances has a financing function, it is an acquisition without a financing function. Its acquisition funds all come from its own funds and do not come directly or indirectly from Little Swan and Little Swan. Its related parties have not conducted asset swaps or other transactions with Little Swan to obtain funds. Paying the acquisition price of 1.68 billion yuan in a short period of time will undoubtedly be stressful for Midea Electric.

It can be seen from the liabilities of Midea Electric Appliances and Little Swan that Midea Electric Appliances' asset-liability ratio is 67.3%, which means that it uses 33.7% of its funds to control 100% of its assets. After acquiring Little Swan, assuming that Little Swan also reaches Midea Electric's negative ratio of 67.3%, that is to say, Little Swan can also use 33.7% of the funds to control 100% of the assets, then Midea Electric can use 114% ( $33.7\% \times 33.7\%$ )'s funds control 100% of the assets. When a holding subsidiary also owns a holding subsidiary, the leverage will be further expanded. In fact, Little Swan owns a large number of holding subsidiaries, so for Midea, its financial leverage is further amplified.

## 6. Summary

Based on the above analysis, this article draws the following revelations from the overall incident of Midea Group's share exchange, absorption and merger with Little Swan.

### 6.1. Design an appropriate merger plan based on your own situation

In the case of Midea Group's merger with Little Swan again, Midea Enterprise chose to exchange shares for merger and acquisition. For Midea Group, using shares for mergers and acquisitions can ensure sufficient capital flow for integration after the merger. When conducting the transaction, Midea Group largely passed on the issues of transaction costs and tax changes to B shareholder holders. In terms of corporate taxation, the use of stock payments defers tax

liability compared to cash payments. Compared with using cash as a payment method, Midea Group chose to adopt a stock exchange merger when acquiring Wuxi Little Swan's B shares, which can effectively avoid foreign exchange risks and minimize the foreign exchange risks arising from the merger.

To sum up, Midea Group has chosen a merger and acquisition method that is more suitable for the development of its company based on its own specific situation, the characteristics of the acquired Little Swan and the strategic direction of Midea Group. Overall, it is a development strategy that is beneficial to the company. realized.

Our country has clearly put forward requirements for listed companies in terms of mergers and acquisitions. In this environment, before listed companies achieve the goal of becoming bigger and stronger, companies should make mergers and acquisitions with different payment methods based on their own operating conditions, financial status, equity Choose the payment method for the merger and acquisition from various aspects such as structure and characteristics of the acquired company, and formulate a more targeted merger and acquisition plan to make it operable, consistent with usual operations, and able to solve the problems existing between the two parties. utility.

## **6.2. Do a good job in the follow-up integration of the merged enterprise**

The success of an enterprise's integration does not only depend on whether the merger and acquisition plan is successfully implemented. After the completion of the stock exchange and absorption merger, how well the integration of various resources of the enterprise proceeds is also one of the factors that determines the success of the merger and acquisition. If the company misses the step of integration, it will only be a formal expansion for the company. The development of the surviving company will not benefit from the merger and acquisition. What is worse is that such a merger may have a negative impact on the surviving company after the merger. produce adverse effects. Therefore, companies must do follow-up integration work in a timely manner after completing mergers and acquisitions.

The use of stock exchange by enterprises to achieve mergers and acquisitions can reduce the demand for the cash flow of the acquiring company as much as possible, which provides a sufficient guarantee of funds for subsequent integration work and can improve the competitiveness of the enterprise from all aspects. At the same time, since the need for corporate cash flow is avoided, the debt demand of the merged company will not increase significantly due to the merger, which provides a better environment for the company to better integrate after the merger.

All corporate strategic plans are not for the short-term results of the company, but for the longer-term development of the company. Regarding the various risks that may arise during the merger process and the operational risks that may arise after the merger mentioned above, Midea Group Good integration within the enterprise is needed to ensure the long-term performance of the enterprise and achieve the strategic goals of the enterprise.

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