

# Risk Analysis and Preventive Measures of Enterprise Merger and Acquisition

-- A Case Study of Suning Tesco's Merger and Acquisition of Carrefour

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**Abstract:** With the rapid development of the "Internet +" economy, the retail industry began to adjust the traditional business model in line with the development of The Times, and accelerated the deep integration with the Internet through the integration of resources. In this context, the "new retail" era has officially arrived, compared with the traditional retail industry, the new retail model through the combination of online and offline services to achieve intelligence, precision, product quality, and personalized, retail growth has become a breakthrough point, because of this major retail enterprises have in the new retail format of mergers and acquisitions. Based on this background, this paper takes Suning Tesco's cross-border merger and acquisition of Carrefour as an example, and combines the historical background of new retail to study its merger motivation, merger risk and put forward relevant suggestions. By summarizing the problems existing in the process of enterprise merger and acquisition and merger experience, the study has certain objective and realistic significance.

**Keywords:** Merger and acquisition, M & a motivation, M & a risk, New retail.

## 1. Introduction

With the rapid development of the Internet, the development of domestic e-commerce industry has been particularly obvious in recent years. However, behind the rapid growth of the e-commerce industry, new opportunities for offline retail are beginning to emerge. As the profit margin of e-commerce is getting smaller and smaller, on the other hand, the traditional offline physical retail business is in difficulties (Zhang Xiaoqing, 2018)[1], thus the concept of "new retail" came into being. In addition, Fang Jing (2018) also said that the diversification of consumer demand and the development of information technology are also important reasons for the formation of new retail[2]. With the proposal of new retail, online and offline are no longer two parallel lines. Zhao Shumei (2017) believes that "new retail" is a comprehensive reform of traditional retail management mode by modern enterprises through the application of emerging information technology[3]. Wang Baoyi (2017) believes that "new retail" is essentially a comprehensive retail industry that can better meet people's multiple needs such as shopping, leisure and social interaction in a multi-channel way[4]. Based on such a business background, major giants have begun to layout the offline market through mergers and acquisitions, but there are not a few failed cases in mergers and acquisitions. Therefore, this paper provides experience and reference suggestions for other new retail mergers and acquisitions by analyzing the merger risks in the case of Suning Tesco's merger and acquisition of Carrefour.

## 2. Relevant Overview

### 2.1. Research on the motivation of merger and acquisition

Wang Ruiyu (2018) studied the evolution process of the home appliance industry and concluded that when the

industry forms scale, the motivation for mergers and acquisitions will shift to improving its core competitiveness and expanding the market scale[5]. Mitchell and Mulherin (1996) believed that mergers and acquisitions were caused by some external factors, such as technological innovation, the development of economic globalization, and the tightening of conquest supervision policies [6]. Liu Yunguo. (2018) made an in-depth analysis of the reasons for overseas mergers and acquisitions in the hotel industry by using event research method, financial analysis and other methods, and believed that the main reason for mergers and acquisitions was to meet the strategic needs of the global development of the industry, cross-business, focus on the long-term, obtain synergies in mergers and acquisitions, and increase market share[7].

### 2.2. Risk types and causes of merger and acquisition

As for the types of M&A risks, scholars at home and abroad have conducted in-depth studies. The M&A risks of enterprises run through the whole M&A process, and scholars generally believe that common M&A risks mainly include investment decision risk, valuation risk, financing risk, payment risk and integration risk. Zhang Chenyan (2019) believes that the main risks faced by enterprises in M&A are the selection of target enterprises before M&A and the excessive premium paid in the valuation, the financing and payment risks in the M&A process, and the integration risks after M&A [8]. Zhu Siqi (2021) identified and analyzed financial risks, which mainly included political risk, valuation risk, financing and payment risk and integration risk, and integration risk was reflected in human and cultural integration risk[9].

At the stage of M&A preparation, Xie WW (2020) et al believe that the more opaque corporate information is, the more likely managers are to manipulate goodwill to achieve their interests. At the same time, the less negative corporate

news, the less media supervision, and the higher the degree of information asymmetry between enterprises and investors, which will lead to mergers and acquisitions with high goodwill[10]. During the implementation stage of M&A, Zhang Jingbei (2021) analyzed the financial risks caused by unreasonable financing methods. If the scale of M&A requires more funds, there will be many limitations in internal financing. However, external financing is very complicated and takes a long time, so the use of this financing method may miss the opportunity of M&A[11]. Han Zhiqing (2021) believes that financing risks mainly come from wrong selection of financing methods, such as too fast or too slow financing time in the financing plan, unreasonable financing ratio, and too single financing channels, which will increase financing risks[12]. In the stage of merger and integration, Hu Guifen (2020) subdivided merger and integration risks, including integration risks caused by the inconsistency of strategic objectives between the merger and acquisition parties, integration risks caused by cultural differences between the merger and acquisition parties, and human resources and organizational structure risks caused by salary and performance system adjustment and personnel post transfer[13]. Li Mengqi (2021) The different corporate culture and business philosophy between the two sides of the merger and acquisition may hinder the integration of enterprises and bring risks[14].

### **3. Case Introduction**

#### **3.1. M&a Company profile**

##### **3.1.1. Acquirer profile**

Suning was established in Nanjing in 1990. After more than two decades of continuous growth, Suning has expanded its business scope from air conditioning distributor to telecommunications and digital products. The development process of Suning Shopping can be roughly divided into three stages: traditional sales stage, O2O stage and smart retail stage. The new retail management concept pushes smart retail further and pushes Suning Tesco to a new stage of development. At present, Suning Tesco focuses on the multi-format smart retail model, and strives to create a full-scene retail model with online and offline multi-channel and multi-format integration.

##### **3.1.2. Profile of the acquiree**

Founded in 1959, Carrefour is a pioneer in the supermarket industry and is not only the largest retailer in Europe, but also the second largest international retail group in the world. Carrefour adopts the international advanced supermarket management model, which is deeply loved by the majority of consumers. Carrefour is one of the first foreign retailers to cooperate with China and officially enter the mainland market and set up business in China in 1995. Since its expansion into China, Carrefour China has benefited from the mature operation mode established by many years of deep overseas cultivation by constantly adding new stores, vigorously expanding the Chinese market and rapidly expanding its business.

#### **3.2. Merger and acquisition process**

Suning Tesco announced on June 24, 2019 that its subsidiary would acquire 80% of Carrefour China. The process of the transaction was rapid, taking only three months from the first disclosure to the completion of the transaction. On June 24, 2019, Suning Tesco disclosed the acquisition for

the first time, planning to acquire 80% of Carrefour China's shares with 4.8 billion yuan in cash. On August 27 of the same year, Suning Tesco announced the acquisition progress announcement, indicating that the merger and acquisition activity has passed the relevant anti-monopoly review. On September 27, Suning announced the completion of the acquisition, Suning paid the full price of the acquisition, and acquired 80% of the shares of Carrefour China.

### **4. M&a Motivation**

#### **4.1. Adapt to the development of The Times and improve the strategic pattern**

With the development of the Internet, the competition of e-commerce has become more and more fierce, and the online retail market has basically formed a pattern dominated by Jingdong and Taobao, and there are few markets left to explore. In the face of this market pattern, especially after the normalized management of the epidemic, the state has many supportive policies for the entity industry, in this context, the e-commerce industry has gradually shifted its attention to the offline industry, forming a "new retail" model development wave of online and offline integration.

Faced with this market pattern, Suning must seize the opportunity of this strategic transformation and expand its scope of influence to gain market share through mergers and acquisitions. The "smart retail" proposed by Suning in 2017 is in line with the development background of today's retail industry. By using technologies such as the Internet, the Internet of Things and big data, "smart retail" takes consumers as the core to predict group consumption trends according to their consumption habits, and deeply integrates online shopping services with offline shopping experience and logistics distribution. To provide them with diversified, specialized and personalized products or services. As a well-known supermarket chain in China, Carrefour has been suffering from the double impact of the epidemic and e-commerce, and its turnover has been in a state of loss. Therefore, for Suning, the acquisition of Carrefour can not only cause losses, but also is the best choice for its layout of "smart retail" strategy.

#### **4.2. Avoid barriers to entry**

Although Suning Tesco and Carrefour are both in the retail industry, one is the e-commerce and the other is the traditional retail industry, and their audience groups are very different. In this case, Suning is faced with many industry barriers to enter such a new field, and mergers and acquisitions are the usual means to break the barriers. On the one hand, Carrefour has unique views on offline retail operations, and has perfect supply chain and management experience. It can directly acquire its offline management experience through mergers and acquisitions to break technical barriers. On the other hand, Carrefour directly obtains the customer group. As a well-known old supermarket chain, Carrefour's reputation is deeply rooted in the hearts of the people. Customers are the guarantee of sales, and sales are the measure of survival of the retail industry. So far, the number of Carrefour members in China has reached 30 million, and Suning can gain direct access to a large number of consumers through the acquisition of Carrefour, thus overcoming the problem of entry barriers.

#### **4.3. Gain synergy**

The synergy effect of merger and acquisition is one of the

most important reasons for enterprises to carry out merger and acquisition. The success of merger and acquisition can integrate the human, material and financial resources of two enterprises, so as to achieve the effect of one plus one greater than two. Suning's acquisition of Carrefour is intended to have this effect. It is specifically reflected in the following three aspects: In terms of operation coordination, mature supply chain is the top priority for the retail industry. Through the integration of Suning and Carrefour offline stores, Carrefour China's eight central warehouses cover dozens of cities across the country, improving the construction of the national supply chain warehousing and distribution network, and giving full play to the advantages of supply chain; In terms of business cooperation, Suning is an online e-commerce enterprise, while Carrefour, as an established offline supermarket chain, has sufficient management experience in the real economy. In addition, as a foreign enterprise, Suning can learn from the western business philosophy and lay the groundwork for opening foreign markets. In terms of financial coordination, Carrefour has suffered losses for years, and the continuing operation situation is not optimistic. In this situation, Suning's acquisition of Carrefour has certain bargaining power, and it can use its losses to carry out reasonable tax avoidance, in addition, it can expand its business scope to increase sales revenue.

## 5. Merger and Acquisition Risk Analysis

### 5.1. M&a preparation stage - Valuation risk

Generally, before the merger and acquisition, the enterprise will pay the consideration according to the financial statements, operating conditions and cash flow of the target enterprise. Effective evaluation can enable enterprises to achieve M&A activities at less cost, on the contrary, excessive valuation, that is, paying a higher premium, will aggravate the liabilities of enterprises and thus increase financial risks, affecting the normal operation of enterprises.

On the one hand, according to the theory of information asymmetry, Suning Tesco inevitably has misunderstandings about Carrefour's information. Since Carrefour China is not listed, Suning has limited access to the financial and operating conditions of the acquired party, and can only judge it through the financial reports and historical announcements disclosed by Carrefour China. In addition, Carrefour, as a French enterprise, adopts international accounting standards for its financial statements, while Suning is prepared by accounting standards issued by the Ministry of Finance of China. Although the difference between Chinese accounting

standards and international accounting standards has been gradually reduced in recent years, there is still a gap and the degree of impact cannot be assessed.

On the other hand, different valuation methods calculate different enterprise values, and the most common evaluation methods are income method, cost method and market method. Suning Tesco used the price-to-sales ratio valuation method to evaluate the enterprise value of Carrefour, and valued the 100% equity of Carrefour China at 6 billion yuan. This is also a commonly used method in the industry, with reference to the market to sales ratio of listed companies in the industry in 2018, as shown in the table below. The average market sales ratio of listed companies in the same industry is 0.88, and the median is 0.7, while Carrefour China is only 0.2, far lower than the industry average, so Suning Tesco believes that the valuation of this transaction is more reasonable. However, Carrefour China has been in a state of long-term loss, and Suning Tesco uses Yonghui Supermarket, Jiayiyue, Zhongbai Group and other profitable supermarkets as the comparable objects of Carrefour, which lacks certain rationality and may lead to valuation risks.

**Table 1.** Market share ratio of listed companies in the industry in 2018 1

Comparable listed company	Market-to-sales ratio
Yonghui supermarket	1.37
Jiayiyue	1.02
Higher step by step	0.38
Sanjiang Shopping	1.87
Zhongbai Group	0.32
Renrenle	0.29
Carrefour China	0.2

### 5.2. M&a implementation stage -- payment risk

Payment risk refers to the unreasonable payment method chosen by the enterprise when paying the consideration of merger and acquisition, which has a negative impact on the normal capital operation of the enterprise. In this case, Suning bought Carrefour shares in cash. This payment method reflects the strong cash capacity of Suning Tesco, but at the same time increases the cash burden of Suning Tesco. A large amount of cash outflow brings a certain degree of risk to the operation of the company, may also compress the investment proportion of other funds, bring a little burden to the internal operation of the company, and increase the financing cost. The following figure shows some key data in the cash flow statement of Suning Tesco in the year of the merger. It can be seen that its cash and cash equivalents are abundant, and there is enough cash flow to support its completion of the merger.

**Table 2.** Cash flow Statement of Suning Tesco in the fourth quarter of 2019 (thousands of yuan)

project	2019Q1	2019Q2	2019Q3	2019Q4
Net cash flow from operating activities	-5,817,083	10,267,957	-19,963,541	17,864,555
Net cash flow from investing activities	-5,672,911	8,203,147	-22,498,856	20,871,110
Net cash flow from financing activities	7,514,043	13,949,650	26,891,316	26,201,239
Net increase in cash and cash equivalents	-4,477,558	4,593,986	-15,231,332	12,300,943
Opening cash and cash equivalents balances	30,220,850	30,220,850	30,220,850	30,220,850
The effect of exchange rate changes on cash and cash equivalents	-501,607	72,532	339,749	233,483
Closing cash and cash equivalents balances	25,743,292	25,626,864	14,989,518	17,919,907

Although Suning can pay the consideration at present, Suning Tesco needs to consider whether the remaining funds can maintain the current daily operations after such a large amount of expenditure, which is a huge challenge that

enterprises must consider after M&A activities. General current ratio and quick ratio can very well reflect the realization ability of an enterprise. According to the analysis of the status of current ratio before and after the merger, it

shows a downward trend after the merger. After the completion of the merger, the realization ability of Suning

Tesco becomes weak, resulting in increased financial risk.

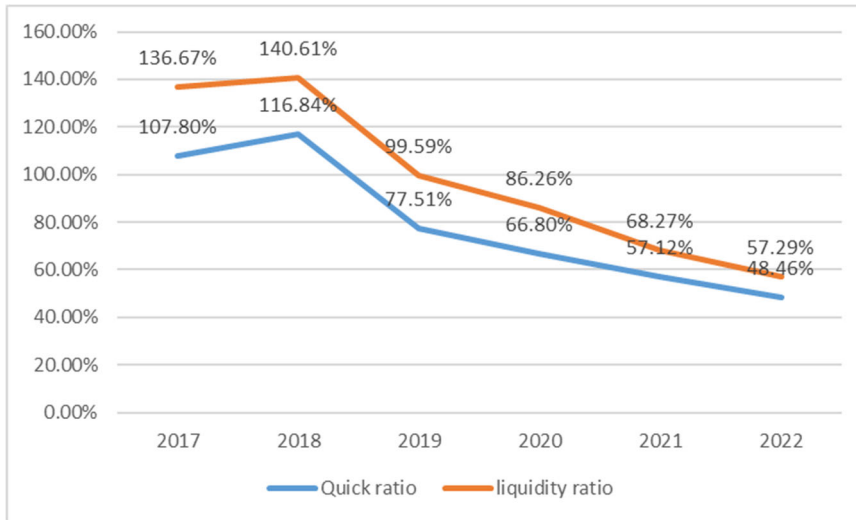


Figure 2. Changing trend of current ratio and quick ratio of Suning Tesco from 2017 to 2022

### 5.3. Post-merger stage - integration risk

For enterprises, M&A is a double-edged sword, if it is not well integrated after M&A, it may lead to the eventual failure of M&A. Therefore, the integration work after the merger is a crucial task. First of all, in terms of corporate culture, both companies are well-known in their respective fields. As mature companies, both sides have already formed their own corporate cultures. Due to the different management systems adopted by both sides and the fact that this merger is a transnational merger, the integration risks of culture and human resources are increased. Secondly, in terms of business integration, Carrefour's main business serves large chain supermarkets and adopts the form of hypermarket sales, which is large, complex, rich and comprehensive, while Suning classifies its business in detail, which leads to

conflicts between the two business models, thus increasing the risk of business integration. If the business is not well integrated, it will affect the layout of smart retail, which will also affect the subsequent development of Suning, bringing certain risks. Here, this paper mainly analyzes the business integration of Suning Tesco from the perspective of development ability. As can be seen from the figure below, both the growth rate of net profit and operating income of Suning Tesco were positive before the merger, indicating that the enterprise had a good development prospect. After the merger, Suning Tesco turned to a negative growth state. It has a certain impact on Suning's liabilities and profits. According to the existing data, this merger has not brought the growth of the company's development ability to Suning, and has affected the development ability of Suning to a certain extent.

Table 3. Indicators of Suning Tesco's development capability from 2017 to 2022

fiscal year	2017	2018	2019	2020	2021	2022
Net profit growth rate	721.02	212.2	-26.28	-157.49	7.25	-0.62
Growth rate of operating	26.48	30.35	9.91	-6.29	-0.45	-1.00

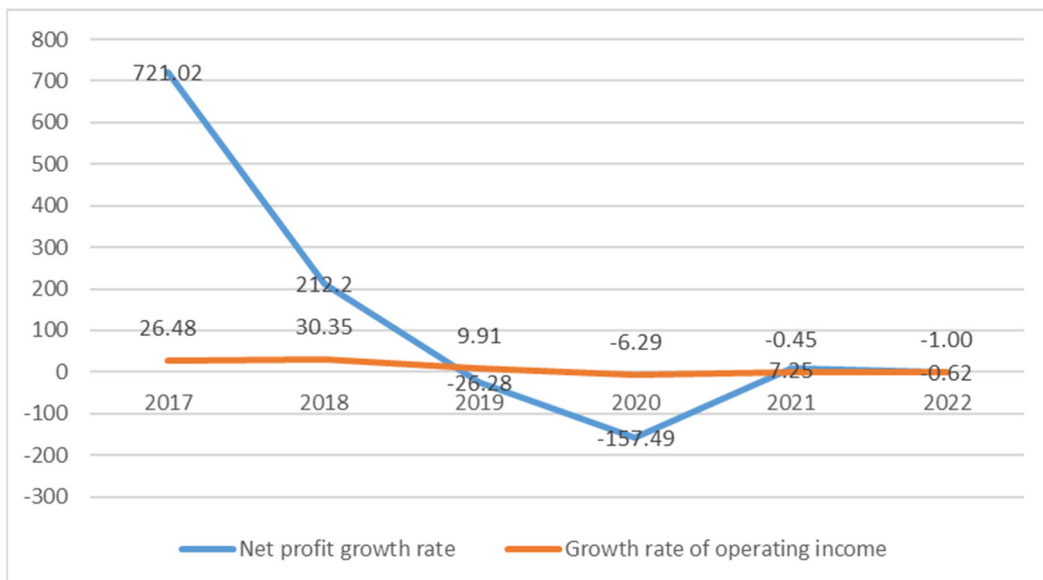


Figure 3. Change trend of Suning Tesco's development capability index from 2017 to 2022

## 6. M&A Risk Prevention Measures

### 6.1. Risk prevention in the preparation stage of M&A

On the one hand, when an enterprise has merger and acquisition activities, the first thing is to choose the target enterprise. The choice of target enterprises is not blind expansion, and whether it is in line with the company's development strategy, strategic mergers and acquisitions can give full play to the synergies. In this case, in order to build "smart retail", Suning Tesco began to layout through mergers and acquisitions, which is worthy of learning from other enterprises. On the other hand, after determining the needs of the target enterprise, it is necessary to conduct a scientific and reasonable evaluation of the M&A enterprise to avoid excessive M&A premium affecting capital operation. Especially in such cross-border M&A activities, incomplete market information disclosure will inevitably lead to information asymmetry, which will have an inestimable impact on the evaluation of the enterprise. In addition, after understanding the basic information of the target enterprise, a scientific evaluation system should be established for its value, which can be carried out from the perspectives of finance, industry and operating status. A rigorous evaluation system can predict the future development and profitability of the target enterprise, which is of great help to the merger and integration. At the same time, a reasonable evaluation system can effectively reduce pricing risks and prevent excessive premium from being paid for the real value evaluation of the target enterprises.

### 6.2. Risk prevention in M&A implementation stage

In this paper, Suning chooses to pay the acquisition consideration in cash, which will undoubtedly cause a sharp drop in short-term cash flow. Therefore, before choosing to pay in cash, it should fully measure whether the operating turnover of other businesses can be satisfied after the payment of its own funds, or whether other strategic opportunities lost during the period of shortage of funds can be made up through this acquisition. In other words, when choosing cash payment, enterprises should prevent the increase of opportunity cost caused by high cash reserves, prevent the payment risk caused by insufficient funds, and strengthen the fund budget management to avoid capital loss. In addition, when the enterprise chooses the means of payment, the diversified means of payment can reduce the unilateral merger risk of the merger and acquisition enterprise. Therefore, in the payment stage, this paper believes that enterprises should consider adopting a mixed payment method of multiple payment means to avoid the sudden decline of capital flow in the short term and maintain stable cash flow for themselves. In addition, on the basis of reasonable planning of payment structure, appropriate allocation of the use ratio of various payment means can also help enterprises reduce payment costs and ensure normal operation of enterprises.

### 6.3. Risk prevention after the completion of the merger

In terms of finance, it is required that after the completion of the merger and acquisition, the enterprises of both sides should reorganize the financial information and other aspects,

form a consistent, standardized and unified financial system, and reach an agreed financial goal. In terms of culture, different enterprises have different business concepts and managers' risk preferences, which are bound to form a variety of corporate cultures. Therefore, after the completion of enterprise mergers and acquisitions, it is necessary to have a full grasp of the cultural concepts of the acquired enterprises and give correct and patient guidance. In terms of business, before the merger, both companies have their own growth and development of business fields, but also have their own relatively stable customer base, each has its own advantages, and after the merger is a partnership, the advantages of both sides should be complementary. Therefore, the two sides should coordinate development, optimize the allocation of resources on both sides, and actively promote the development of related businesses on the basis of maintaining their own characteristics.

## 7. Closing Remarks

This paper takes the merger and acquisition of Carrefour by Suning Tesco as an example, first analyzes the motivation of the merger, and then analyzes the possible risks hidden in the whole process of the merger and acquisition, and based on this, provides reference suggestions for preventing risks in the same industry. However, there are many differences between each company. Therefore, in the preparation stage of M&A, enterprises should select the appropriate target enterprises according to their strategic layout and financial status, and carry out necessary scientific evaluation; In the M&A stage, we should choose flexible payment methods, strengthen fund budget management, and avoid capital loss caused by too high or too low funds. After the completion of the merger, in the subsequent stage, a scientific and reasonable integration plan should be formulated to optimize the resource allocation of both parties, and the possible financial risks in the merger should be controlled in all aspects including the whole stage.

## Acknowledgment

Fund Project supported by Talent Introduction Project of Sichuan Light Chemical University (2017RCSK22).

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