

# ***The Impact of Mergers and Acquisitions on the Long-Term Performance of Securities Firms***

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**Abstract:** In China, the generally small size and weak financing capacity have affected the growth of the securities companies. In recent years, many securities firms have adopted mergers and acquisitions (M&A) to expand the size of their businesses and it is necessary to study the impact of M&A on their long-term performance. This paper selects the acquisition of Guangzhou Securities by CITIC Securities as a case study to examine the impact of M&A on long-term performance. The paper first analyses the motivation for the M&A and describes the background of the two companies. Then it analyses the long-term performance of CITIC Securities before and after the acquisition. As for the financial indicators, the paper compares profitability, solvency, operating efficiency and growth capacity. In terms of non-financial indicators, it focuses on market share and number of business offices. Finally, it makes some suggestions for M&A in the Chinese securities industry. The paper finds that CITIC Securities' profitability, solvency and operating efficiency have all improved after the M&A, and the M&A has brought considerable gains. Its business offices in Guangdong operations have increased, and its market share has further expanded. In the future, CITIC Securities will need further follow-on integration to expand synergies and improve the company's performance.

**Keywords:** CITIC Securities, Guangzhou Securities, M&A, long-term performance

## **1. Introduction**

### **1.1. Background**

At present, Chinese securities companies are generally small in scale and have weak financing capacity, which seriously affects their development. In recent years, many securities companies have adopted the method of mergers and acquisitions to expand the scale of enterprises.

Among the securities companies in China, CITIC Securities has a significant advantage in scale and it is the first security corporate in China whose assets exceed one trillion yuan. The main financial indicators of CITIC have retained the leading position in the industry for more than ten consecutive

years, and the company has maintained a leading market position and accumulated an extensive brand reputation and advantages in the domestic market.

More importantly, the acquisition of Guangdong Securities by CITIC Securities has achieved great success. The scale of the company has further expanded, and the securities underwriting and trading business has grown rapidly. The company's securities subscription scale was in sixth place in 2018, and it increased to third place in 2020. The securities transaction scale was in fourth place in 2018 and increased to the third place in 2020. On the other hand, the economic benefits of the enterprise have also been improved. At the end of June 2021, CITIC Securities' first-half net profit was 10.891 billion yuan, with a 38.13% year-on-year growth, and the company's equity was further improved.

## **1.2. Related Research**

### **1.2.1. Fundamentals of Mergers and Acquisitions**

Calipha et al. addressed three topics. The first is the sequencing of the M&A process, which goes from 2 stages to 7 stages. The second is the motivation for mergers and acquisitions, including the acquisition of new and scarce resources, the realization of synergies, etc. The third relates to M&A success factors, including relative partner size, culture, and organizational structure [1]. Krishnakumar, D. used a study of M&A behavior from the aspect of the ways used to calculate the value of post-acquisition. The conclusions drawn are as follows: studies of international events dominate studies on the performance of acquisitions; Indian acquisition studies are based on accounting returns. Other approaches, including the data envelopment analysis and the balanced scorecard approach, merit further research and in the M&A literature. Furthermore, the conclusions are related to the performance evaluation method [2].

### **1.2.2. Research on Financial Performance and Mergers and Acquisitions**

Chen et al. discovered that mergers and acquisitions can increase value for the acquiring firm and result in higher returns. Specifically, horizontal mergers can accomplish economies of scale or bring more market power and thus achieve more post-merger and acquisition outcomes. In addition, financial synergies can also contribute to better performance after an M&A. Regarding the influence of M&As on cash flow returns, the article states that M&As will bring companies higher operating cash flow returns. Additionally, companies with high cash ratios may perform better [3]. Vinocur et al. explored the relationship between mergers and acquisitions capabilities and long-term firm performance from a strategic management perspective. The results show that by measuring the return on equity and price-to-book ratio, there is a positive relationship between M&A ability and long-term firm performance [4].

### **1.2.3. Impacts of Internal and External Factors on the Medium and Long-term Performance of Mergers and Acquisitions**

Weber et al. examined the joint effects of company culture, national culture and synergy potential on different integration methods and their impact on performance mergers and acquisitions. The article presents a theoretical framework that explains how the specific national and corporate cultural characteristics of the acquirer should be associated with the choice of the integration method. It also highlights the role of cultural differences in the choice of integration method and provides a solution to the conflicting empirical results regarding the impact of cultural conflicts and integration methods on mergers and acquisitions performance [5]. According to the diversity of M&A motives, Zhang et al. explored the synergistic effects of post-merger technological progress and capacity utilization on the behavior of merged firms in all sectors of activity. The article presents a methodology based on

the analysis of panel data and the Pearson correlation in order to test the performance of M&A and the specific factors contributing to their success [6].

#### **1.2.4. Mergers and Acquisitions in the Banking Sector**

Zhu et al. discovered a data-driven approach to finding the best partners for M&As in banking. They developed a novel DEA framework approach and then proposed 0-1 integer programming to construct the optimal mate selection model. When resources are aligned, the new integration firm can use the best production techniques from both partners to align the new production [7]. Abdulwahab and Ganguli assessed the influence of four mergers and acquisitions on Bahrain's financial performance during 2004-2015. The study applied CAMEL rating methodology and Excel financial modeling to examine the changes in the bank's financial performance before the merger and three years after the merger. The results show that there is no noticeable difference between the two periods of time [8].

#### **1.2.5. Cross-border and General Mergers and Acquisitions**

Reddy et al. explored the process of internationalization of Indian multinational corporations (MNCs) through international mergers and acquisitions (M&A). The study reveals that the number of outgoing transactions exceeded incoming transactions between 1991 and 2002, but incoming and outgoing transactions evolved together from 2002 to 2006. From 2007 to 2010, the number of purchases exceeded that of sales. The authors attributed this to economic, financial and banking reforms [9]. Zhu and Zhu provided a report and comparison of M&A research in leading journals, focusing on studies conducted before and after 2009. The paper stresses the need for researchers to conduct studies in the context of China or other emerging economies before generalizing findings to developed countries. The authors also suggested future research opportunities related to Chinese mergers and acquisitions and call for differentiated theorizing for Chinese M&As, given the increasing use of M&As by Chinese companies to compete in local and global markets [10].

### **1.3. Objective**

The research aims to analyze how the mergers and acquisitions of Guangzhou Securities by CITIC Securities impact the medium-term and long-term performance of CITIC Securities. The analysis of short-term M&A activity can not only show the direct impact of M&A activity on securities firms but also help investors and analysts assess the value of the company better. Mid-term performance research can show the long-term development of securities companies and help investors and analysts better assess the company's prospects.

## **2. Current Status of Corporate Mergers and Acquisitions**

### **2.1. Principles and Motivations of Mergers and Acquisitions**

Corporate mergers and acquisitions refer to strategic actions taken by a company to expand its size, increase market share, or gain resources through the purchase, merger, or acquisition of other companies. The principles and motivations behind these actions involve various factors, including market growth, resource integration, risk diversification, and market competition.

Firstly, market growth is a significant motivation for corporate mergers and acquisitions. In highly competitive market environments, mergers and acquisitions allow companies to rapidly expand their scale, enter new market domains, and achieve higher revenue growth. Through mergers and acquisitions, companies can leverage existing market channels and customer bases, reducing the time and cost of market development.

Secondly, resource integration is a key principle in mergers and acquisitions. Companies can acquire assets, technologies, brands, talent, and other resources from the target company, optimizing resource allocation and achieving synergistic effects. By integrating resources, companies can improve production efficiency, reduce costs, and enhance competitiveness.

Mergers and acquisitions can also help companies achieve risk diversification. By expanding their business scope through mergers and acquisitions, companies can reduce reliance on a single market or industry, thereby lowering market and operational risks. Additionally, acquiring complementary businesses allows for risk diversification across multiple market domains, enhancing the company's resilience.

Lastly, market competition is another significant driving force for mergers and acquisitions. In increasingly intense market competition, mergers and acquisitions can enhance competitive advantages. By acquiring competitors or companies with similar businesses, companies can reduce the number of competitors, increase market share, and improve bargaining power.

## **2.2. Impact of Mergers and Acquisitions on Financial Performance (Key Analytical and Measurement Indicators)**

The impact of mergers and acquisitions on financial performance is a crucial indicator to assess their success. Here are several key analysis and measurement indicators:

Firstly, post-acquisition financial indicators serve as important benchmarks to evaluate the success of mergers and acquisitions. These indicators include post-acquisition sales growth rate, net profit margin, and earnings per share, among others. If the financial indicators show significant improvement after the acquisition, such as increased sales and improved profit margins, it indicates a positive impact on financial performance. Secondly, mergers and acquisitions can affect a company's market position and competitiveness. By increasing market share, expanding brand influence, and gaining more market opportunities, companies can strengthen their market position. Indicators to measure market position and competitiveness may include market share, brand recognition, and product innovation capabilities. Additionally, the impact of mergers and acquisitions on cost efficiency is another important measurement indicator. The ability to control costs effectively and achieve efficiency gains post-acquisition is a critical factor in evaluating the effectiveness of mergers and acquisitions. Relevant indicators include cost reduction magnitude, production efficiency improvement, and optimized resource allocation. Lastly, for the long-term impact of mergers and acquisitions, the growth of company value needs to be considered. The increase in market value and enhancement of shareholder equity after the merger and acquisition process are essential indicators for evaluating long-term effects.

Therefore, corporate mergers and acquisitions play a significant role in expanding scale, optimizing resource allocation, diversifying risks, and enhancing competitiveness. Evaluating the post-acquisition financial performance and changes in market position can provide better insights into the success of mergers and acquisitions and serve as a reference for strategic decision-making in companies.

## **3. Case Study of CITIC Securities' M&A of Guangzhou Securities**

### **3.1. Overall China Securities M&A**

Since the establishment of the first domestic securities company in 1987 and the establishment of the Shanghai Stock Exchange in 1990, China's securities industry has gone through several phases of cleaning, restructuring, and reform.

With the gradual improvement of regulation, the securities industry entered a new era of vigorous development after 2005. The number of securities companies and the total assets of the industry have

been continuously increasing. However, compared to developed countries with mature capital markets, China's securities industry still faces a significant gap in terms of scale and depth of development.

Therefore, large securities firms acquiring small and medium-sized ones to achieve scale expansion, fill gaps, and further consolidate market positions is expected to be a trend in the securities industry's future development. The China Securities Regulatory Commission (CSRC) has expressed its encouragement for market-driven mergers and reorganizations to build large-scale leading securities firms with enriched service functions. Enhancing the core competitiveness of securities companies and promoting the industry's growth and high-quality development is crucial for the current economic development.

Thus, efforts must be made to facilitate industry consolidation, optimize the market structure of the securities industry, and focus on creating a few leading securities firms that can compete with foreign investment banks while strengthening the professional capabilities and service characteristics of Chinese securities firms. Corporate mergers and acquisitions are important means to enhance asset size, improve industry concentration, and achieve economies of scale, providing an effective pathway for companies to rapidly absorb resources and address shortcomings.

Mergers and acquisitions (M&A) have become a prominent feature of the industry's development. The motivations behind these M&A activities include expanding market share, enhancing comprehensive strength, improving operational capabilities, diversifying business scope, and consolidating resources. By pursuing mergers and acquisitions, securities firms aim to increase their scale, broaden their range of services, and ultimately strengthen their competitiveness and profitability.

The targets of these M&A activities can include other securities firms, brokerage divisions, and asset management companies, among others. The selection of M&A targets is often based on strategic planning, complementarity of business operations, market positions, and potential growth prospects.

### **3.2. CITIC Securities' Process of M&A of Guangzhou Securities**

In order to further expand its business in stock custody, futures brokerage, and investment banking, CITIC Securities plans to acquire Guangzhou Securities through a merger and acquisition (M&A) strategy. Simultaneously, the objective is to increase the market share of the company in the securities market of Guangdong Province.

CITIC Securities had been considering the acquisition of Guangzhou Securities as early as 2016. However, due to the substantial amount of preparatory work and considerations regarding the direction and cultural differences of the target company, no further action was taken at that time. It was not until early 2017 that the two companies initiated preliminary negotiations. After exploring the market position, financial conditions, and management structure of both parties, they drafted a memorandum of understanding and established a cooperative direction.

On December 24, 2018, CITIC Securities announced its intention to acquire 100% equity of Guangzhou Securities through share issuance, and subsequently reorganize it as a wholly-owned subsidiary. According to the transaction plan, CITIC Securities planned to purchase 100% equity of Guangzhou Securities, which includes a 99.03% stake in Guangzhou Futures and a 24.01% stake in Golden Eagle Fund, from Yuexiu Financial Holdings and its wholly-owned subsidiary. In addition, CITIC Securities designated its wholly-owned subsidiary, CITIC Securities Investment, to hold a 0.10% equity stake in the target company. Specifically, CITIC Securities planned to issue shares to acquire a 32.765% equity stake held by Yuexiu Financial Holdings and a 67.235% equity stake held by Jinkong Limited. The valuation of the target assets in this transaction was based on the evaluation value of 100% equity of Guangzhou Securities, excluding the 99.03% stake in Guangzhou Futures

and the 24.01% stake in Golden Eagle Fund. The total number of shares issued by CITIC Securities was approximately 810 million shares, with an issuance price of RMB 16.62 per share, resulting in a total transaction price of RMB 13.46 billion.

### **3.3. Motivation for CITIC Securities to M&A Guangzhou Securities**

#### **3.3.1. Strengthening Regional Presence and Market Share**

In 2018, CITIC Securities had a total of RMB 28.801 billion in main business revenue and its business revenue in Guangdong Province was only RMB 243 million, which is only 0.84% of the total business revenue of the enterprise in Guangdong Province. Compared with CITIC Securities' main business revenue in Zhejiang and Beijing, there is great room for development in South China and Guangdong Province.

On the other hand, Guangzhou Securities has strong business revenue in South China, with significantly higher securities revenue than CITIC Securities. In addition, Guangzhou Securities has significantly more relevant indicators than CITIC Securities in both South China and Guangzhou. In summary, CITIC Securities' acquisition of Guangzhou Securities is intended to leverage Guangzhou Securities' strong performance and market position to increase CITIC Securities' business and market share in South China (especially in Guangdong Province) to further develop its momentum.

#### **3.3.2. Strategic Deployment and Synergy**

The synergistic effects of CITIC Securities' M&A include operational synergies, management synergies, and financial synergies.

Operational synergy refers to the increase of the company's share in the industry and anti-risk ability after the M&A, as well as the effective optimization of resource allocation. CITIC Securities has a low market share in South China; Guangzhou Securities has a high market share and good performance in South China, so the acquisition of Guangzhou Securities by CITIC Securities has a positive impact on its operating synergies.

In addition, management synergies not only improve operational performance but also enhance the ability to adapt and respond to market uncertainties and changes. Financial synergies allow for a more rational allocation of time, expansion of operations, diversification of sources of capital, enhancement of the company's capital, improvement of the company's ability to obtain external borrowings and repay debt, expansion of business operations, and diversification of the investment portfolio. According to the 2020 CITIC Securities annual financial report, the net cash flow from operations of CITIC Securities as of the end of 2020 was RMB 101.825 billion, compared to RMB 57.654 billion as of the end of 2018; the net cash flow from the financing of CITIC Securities as of the end of 2020 was RMB 11.998 billion, compared to RMB 21.751 billion as of the end of 2018, thus, the cash flow from the merger of CITIC Securities has been significantly improved.

#### **3.3.3. Business Expansion and Efficiency**

After the completion of the M&A restructuring, the Company can further expand its business scope and business scale, which will facilitate it to improve its competitive advantage in the market, harvest more abundant potential customers and promote the continuous development of new business. Such diversification can reduce the impact of underperforming business units, thus allowing for more robust business development. By expanding the scale of its business, it can enhance the competitive advantage of the merged company, reduce operational risks, and achieve more stable business development.

#### 4. Long-term Performance Comparison Before and after the M&A

This paper uses financial and non-financial indicators to analyze the long-term performance of CITIC Securities' acquisition of Guangzhou Securities.

##### 4.1. Analysis of Financial Indicators

###### 4.1.1. Profitability

Profitability measures the level of profitability of a company. In this paper, the operating revenue, total profit, net profit, and net profit attributable to shareholders of the parent company of CITIC Securities and Guangzhou Securities from 2019 to 2020 are selected as the variables for analysis, as well as data on the main business of Guangdong Province, to conduct a comparative analysis of their profitability, as shown in Table 1 and Table 2.

Table 1: Profitability of two companies for 2019-2020 (billion RMB).

Year	2019			2020		
Company	CITIC Securities	Guangzhou Securities	Proportion	CITIC Securities	Guangzhou Securities	Proportion
Operating income	431.40	40.67	9.43%	543.83	12.53	2.30%
Total profit	169.95	-6.12	-3.60%	204.70	-1.43	-0.70%
Net profit	126.48	-4.32	-3.42%	155.17	-1.14	-0.73%

Table 2: CITIC Securities' revenue in Guangdong Province.

Year	2019	2020
Operating income (billion RMB)	2.82	7.52
Gross margin (%)	2.37	34.75

Data source: CITIC Securities, CITIC Securities South China Annual Report.

In 2019, CITIC Securities has operating revenue of RMB43.140 billion and Guangzhou Securities had an operating revenue of RMB4.067 billion, accounting for 9.43% of CITIC Securities. After the merger and acquisition, CITIC Securities' operating revenue in 2020 was RMB54.383 billion, an increase of 26.06% year-on-year. Guangzhou Securities' revenue was RMB1.253 billion, showing negative growth and accounting for only 2.30% of CITIC Securities' revenue. However, Guangzhou Securities' total profit, net profit and net profit attributable to shareholders of the parent company all achieved positive growth.

Before the merger and acquisition, CITIC Securities' operating revenue in Guangdong in 2019 was only RMB282 million. After the merger, it gained a significant boost in operating revenue in Guangdong province. 2020 CITIC Securities' operating revenue in Guangdong was RMB752 million, representing a year-on-year increase of 166.67% from 2019. In terms of operating revenue share, Guangdong Province contributed 1.38% to CITIC Securities' operating revenue in 2020, well above 0.65% for the same period in 2019. Its gross margin also increased by 1,366.24%. It can therefore be seen that CITIC Securities has improved its profitability in Guangdong Province by covering the business of Guangzhou Securities.

#### 4.1.2. Debt Servicing Capacity

Solvency measures a company's ability to pay off its liabilities as they come due promptly. In this paper, CITIC Securities and Guangzhou Securities' total assets, total liabilities, gearing ratio and equity ratio from 2019 to 2020 are selected as variables for analysis to compare their solvency, as shown in Table 3.

Table 3: Solvency of two companies for 2019-2020 (billion RMB).

Year	2019			2020		
Company	CITIC Securities	Guangzhou Securities	Proportion	CITIC Securities	Guangzhou Securities	Proportion
Total assets	7917.22	299.82	3.79%	10529.62	238.99	2.27%
Total liabilities	6262.73	197.03	3.15%	8670.80	124.87	1.44%
Gearing ratio (%)	79.10	65.71	-	82.35	52.25	-
Equity ratio (%)	3.87	1.92	-	4.77	0.91	-

Data source: Flush official website, CITIC Securities annual report, CITIC Securities South China annual report.

Guangzhou Securities was in a loss-making position before the merger. As can be seen from Table 3, CITIC Securities' gearing and leverage ratios both increased after the merger, indicating that CITIC Securities assumed the number of losses of Guangzhou Securities after the merger and its solvency declined.

#### 4.1.3. Operating Efficiency

Operating efficiency measures a firm's ability to control its capital operations and turnover. In this paper, CITIC Securities' total asset turnover and return on assets from 2019 to 2020 are selected as variables for analysis to compare its operating efficiency.

As can be seen from Table 4, the changes in CITIC Securities' total asset turnover ratio and return on assets after the M&A are relatively small, indicating that the M&A has had a limited impact on CITIC Securities' operating capabilities.

Table 4: CITIC Securities' operating efficiency for 2019-2020.

	2019	2020
Total asset turnover (%)	0.033	0.034
Return on assets (%)	1.8	1.7

Data source: CITIC Securities Annual Report

#### 4.1.4. Growth Capacity

Growth capacity is a measure of a company's potential for future growth. In this paper, CITIC Securities' total assets, net profit, operating income, earnings per share, return on net assets and growth rate from 2018 to 2020 are selected as variables for analysis to compare its growth capability, as shown in Table 5.



Table 5: CITIC Securities' Growth Capacity 2018-2020.

Year	2018	2019	2020
Total assets (billion RMB)	6531.33	7917.22	10529.62
Year-on-year growth rate of total assets (%)	4.41	21.22	33.00
Operating income (billion RMB)	372.21	431.40	543.83
year-on-year revenue growth (%)	-14.02	15.90	26.06
Net profit attributable to shareholders of the parent company (billion RMB)	93.90	122.29	149.02
Year-on-year net profit growth (%)	-17.87	30.23	21.86
Basic earnings per share (RMB/share)	0.77	1.01	1.16
Basic earnings per share year-on-year growth rate (%)	-18.09	31.17	14.85
Return on net assets (%)	6.20	7.76	8.43
Return on net assets growth rate (%)	-20.72	25.16	8.63%

Data source: CITIC Securities annual report, Flush official website

The data shows that CITIC Securities' total assets, net profit, revenue, earnings per share and return on net assets as a whole showed a more significant upward trend after the M&A, with total assets increasing by 33% in 2020. At the same time, the year-on-year revenue growth rate, earnings per share growth rate and return on net assets growth rate all turned negative to positive after the M&A. In summary, the M&A has had a very significant positive effect on CITIC Securities' ability to grow.

#### 4.2. Analysis of Non-financial Indicators

In this paper, market share and number of business units are selected as measures. Equity business underwriting is one of CITIC Securities' main businesses. Table 6 shows data relating to the size and market share of the domestic equity business underwriting business in investment banking.

Table 6: Size and market share of selected main businesses of CITIC Securities, 2018-2020.

Year	2018	2019	2020
Underwriting size of domestic equity business (billion RMB)	1,783	2,798	3,136
Market share of underwriting for domestic equity business (%)	14.75	18.16	18.94

Analysis shows that CITIC Securities has attracted more clients and capital inflows following the M&A, which has increased transaction volumes. At the same time, as can be seen from Table 7, there was a slight reduction in the number of Guangzhou Securities' business offices after the M&A as a result of consolidation. However, the total number of CITIC Securities' business offices in Guangdong increased significantly by 107.7% as the M&A met the objectives and needs of CITIC

Securities' business expansion in southern China. This indicates that CITIC Securities' market share in Guangzhou was expanded after the M&A.

Table 7: Number of CITIC Securities' business offices in Guangdong Province, 2018-2020.

Year	2018		2019		2020	
Company	CITIC Securities	Guangzhou Securities	CITIC Securities	Guangzhou Securities	CITIC Securities	Guangzhou Securities
Number of sales offices in Guangdong Province	26	32	26	31	54	27
Year-on-year growth rate (%)	0	0	0	-3.13	107.7	-12.90

Data source: CITIC Securities Annual Report, CITIC Securities South China Annual Report.

### 4.3. Summary of This Chapter

Overall, in terms of financial indicators, CITIC Securities has improved in all areas after the M&A, except for its debt servicing capacity, so the M&A has brought considerable benefits. In terms of non-financial indicators, the number of business offices of CITIC Securities in its Guangdong operations increased after the M&A, and its market share expanded further. In summary, the impact of the M&A of Guangzhou Securities on the long-term development of CITIC Securities is positive in the long run and will help to improve the Company's performance.

## 5. Conclusion

This paper presents a case study of the impact of mergers and acquisitions on the long-term performance of securities firms. The case examines the motivation behind the M&A and the acquisition process. Then, the long-term performance of CITIC Securities after the acquisition is analyzed in terms of both financial and non-financial indicators.

The case study finds that the profitability, solvency, and operational efficiency of CITIC Securities have improved after the acquisition. Secondly, the number of CITIC Securities' Guangdong business offices increased and its market presence further expanded. Third, CITIC Securities' market share expanded as a result of the acquisition. These findings suggest that CITIC Securities' acquisition of Guangzhou Securities has yielded positive results in terms of its financial performance, business expansion, and market share growth.

This case study provides the following suggestions for future mergers and acquisitions. Firstly, the analysis of financial and non-financial performance shows that, although CITIC Securities' merger was successful, it will require good follow-up integration to continue to expand synergies and improve the company's performance in the future. Secondly, this case study shows the importance of market presence and expansion in the securities industry. Thirdly, Companies should focus on financial indicators such as profitability, solvency, and operational efficiency when evaluating potential M&A targets. Fourthly, financial institutions can explore similar regional expansion and growth opportunities, taking into account local market dynamics and potential synergies.

## Authors Contribution

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

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