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Implementation Effect of the Company's Equity Incentive Plan: Evidence from Youyou Food

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Abstract: As a matter of fact, regarding as an effective way to attract and retain talents, equity incentives were first implemented by high-tech enterprises in the United States. The purpose of this study is to deeply explore the implementation effect of the company's equity incentive plan. With this in mind, this paper takes Youyou Food Company as a case for analysis. By comparing the situation before and after the implementation of the equity incentive plan of Youyou Food Company, the effect of its equity incentive in three aspects (i.e., profitability, development ability and debt repayment ability) was analyzed. According to the analysis, the effect of Youyou Food's implementation of equity incentives did not reach the expected rate of return, which may be due to the economic downturn in the general environment eating up the benefits of equity incentives. At the same time, the problems as well as suggestions are proposed based on the analysis.

Keywords: Equity incentives, Youyou Food, financial indicators.

1. Introduction

As an effective way to attract and retain talents, equity incentives were first implemented by high-tech enterprises in the United States. Youyou Food Co., Ltd. implements the equity incentive system, which can bind the interests of the management with the interests of shareholders, and promote the management to consider the long-term development of the company from the standpoint of maximizing the company's rights and interests. Fig. 1 can be clearly concluded that the growth rate of the market will continue to decline, especially in 2023, there will be negative growth. In addition, Youyou Food has implemented equity incentives in response to the reform situation, and the analysis of the effect of Youyou Food's incentives is mainly analyzed from the aspect of financial indicators. Profitability, growth ability, and solvency are three aspects to determine whether to achieve the improvement of enterprise value. Therefore, this paper first sorts out the equity incentives implemented by Youyou Food, and then selects the financial data from 2019 to 2022 for specific analysis, and judges the impact of equity incentives on the financial performance of enterprises in two time periods before and after the implementation.

Jensen and Murphy believe that enterprises can encourage managers to bind corporate value with their own interests, so that managers can pursue their own personal interests with the goal of maximizing corporate value, avoid short-sighted profit-seeking behaviors, reduce the possibility of managers making decisions that are harmful to the long-term stable development of enterprises in order to obtain short-term performance improvements, and reduce principal-agent costs [1]. Berle

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and Means pointed out that modern enterprises have the characteristics of separation of powers, and proposed the optimal contract theory, in which owners take their own interests as the starting point to establish the optimal remuneration contract, and hope to reduce agency costs, alleviate conflicts with managers, and maximize shareholder value [2]. According to Tzioumis' research, the main reason why companies implement equity incentives is to attract and retain good employees [3]. Spalt points out that such incentives can also help maintain employee loyalty, which in turn reduces employee turnover [4].

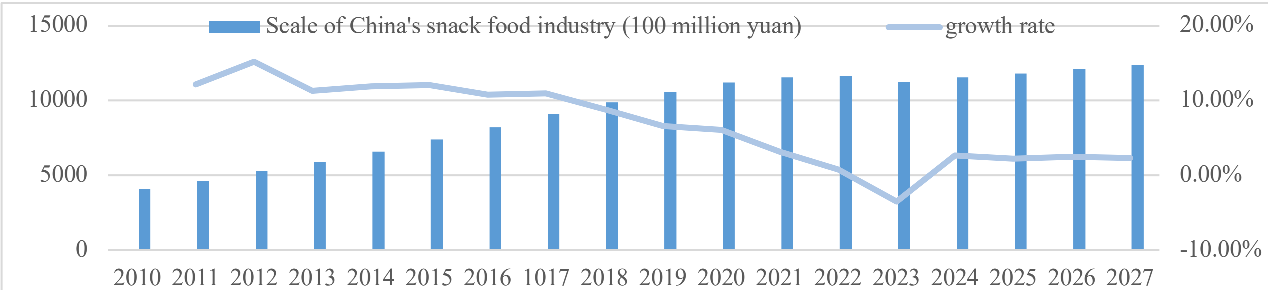

Figure 1: Scale and forecast of China's leisure and snack industry from 2010 to 2027.

Through empirical research, Shen and Wang found that with the increase of agent equity, the agent's status as a shareholder makes its goals tend to be consistent with the goals of the owner of the enterprise, so it can alleviate the principal-agent contradiction and reduce the agency cost [5]. Du and Xu believe that by giving the agent part of the ownership of the enterprise through equity incentives, which is similar to the concept of the enterprise owner, and thus can alleviate the contradiction between the principal and the agent [6]. Lu and Li proposed that the motivation of enterprises to implement equity incentives for employees is to alleviate the contradictions and conflicts between enterprise owners and employees through the fair distribution of resources [7]. According to Fama and Jensen's research, when a company's management owns a large number of shares, they may abuse their power and cause immeasurable losses to the company [8]. Oyera and Schaefer's investigation, when given equity to rank-and-file employees, may lead to higher agency costs [9]. According to the findings of Benson and Davidson, it can be seen that there is an inverted U-shaped relationship between firms' TobinQ and firms' performance [10]. Investigations by Zhu, Ding et al. also show that the equity of senior managers may bring adverse consequences to enterprises. According to Huang and Zhang's research, when the top management of a state-owned enterprise owns a large number of shares, it may lead to a decline in its operating performance [11]. However, Pan's investigation shows that there is no clear link between the grant of equity or options and the company's operating performance [12]. According to the research results of Li et al., the effect of equity incentives in China is not obvious at present, mainly due to the low level of stock incentives (only 13.1% on average), which cannot effectively stimulate the enthusiasm and enthusiasm of executives [13].

In general, equity incentive plans are a complex topic, and their implementation and effectiveness are affected by a variety of factors. Researchers need to consider the company's specific context and goals, as well as the market environment, to gain a more complete understanding of the impact of these programs on the company's performance. In addition, the implementation and effectiveness of equity incentive plans may change over time, so continuous monitoring and evaluation are required.

2. Case Selection and Background Overview

2.1. Company Overview

Youyou Food Co., Ltd. is an enterprise specializing in the research and development, production and sales of marinated flavor snack food. Since establishment in 1997, it has always adhered to the enterprise spirit of "integrity and pragmatism, persistent innovation", and has contributed delicious and high-quality, safe and healthy leisure food to the society. At present, the company has two production bases in Chongqing and Sichuan, including Sichuan Youyou Food Development Co., Ltd., Chongqing Youyou Food Sales Co., Ltd., Chongqing Youyou Import and Export Co., Ltd. and Youyou Food Chongqing Manufacturing Co., Ltd., and the company has been awarded the honorary titles of "Top 50 Private Enterprises in Chongqing" and "Excellent Private Enterprises in Chongqing" by Chongqing Municipal People's Government. It bravely assumes social responsibility, standardizes operation, and boosts local economic development. Through a variety of ways and carriers such as employment, donating to education, disaster relief, and helping the elderly, one strives to share the worries and worries of the government, let the society share the development results and love of the enterprise, and contribute to the construction of a harmonious society.

Table 1: List of first-time incentive recipients.

Serial Number	Name	Office	Number of Restricted Shares Granted (10,000 shares)	Proportion of The Total Number of Restricted Shares Granted Under This Incentive Plan	The Proportion of The Total Share Capital of The Company on The Date of The Announcement of This Incentive Plan
1	Li Xuehui	Director and Deputy General Manager	12	2.55%	0.04%
2	Choi Haibin	Director, Chief Financial Officer	12	2.55%	0.04%
Middle Management and Core Backbone(234)			352.3	74.96%	1.16%
Total			470	100.00%	1.54%

2.2. Case Study

On March 15, 2021, according to the authorization of the company's first extraordinary general meeting of shareholders in 2021, it was determined to grant 3.58 million restricted shares to 207 eligible incentive recipients. On March 24, 2021, the Company completed the registration of the first grant of rights and interests under the 2021 restricted stock incentive plan (seen detailin Table 1 and Table 2). October 27, 2021 is the reserved grant date, and 937,000 restricted shares will be granted to 50 incentive recipients who meet the grant conditions, and the grant price is 8.32 yuan per share. Part of the reserved stock source is the company's private placement of A-share ordinary shares. The corresponding assessment years for the release of restricted shares reserved for grant under this incentive plan are three fiscal years from 2021 to 2023, and each fiscal year will be assessed once, based on the operating income in 2020, and the performance assessment targets for each year are shown in the Table 3.

Table 2: Reserve part of the list of incentive recipients and their award

Serial Number	Name	Office	Number of Restricted Shares Granted (10,000 shares)	Percentage of The Total Number of Restricted Shares Reserved for Grant	Proportion of The Company's Current Total Share Capital
1	Lu You	Deputy General Manager	15	16.0085%	0.0487%
2	Liu Yucan	Secretary of the Board of Directors	6	6.4034%	0.0195%
3	Choi Haibin	Director, Chief Financial Officer	2	2.1345%	0.0065%
Middle Management and Core Backbone (47)			70.7	75.4536%	0.2295%
Total (50)			93.7	100.0000%	0.3041%

Table 3: Annual performance appraisal targets

Assessment year	2021	2022	2023
Target value for the growth rate of operating income	15%	33%	55%
The actual growth rate of operating income achieved as a percentage of the actual achievement of the target value set for the year(A)			
In 2021-2023, the proportion of sales restrictions that can be lifted at the corresponding company level(M)			
When A < 70%.		M=0	
When 70% < = A<100%.		M=A	
When A>=100%		M=100%	

Table 4: Individual-level assessments

At the individual level, the results of the previous year's assessment	At the individual level, the restricted sales ratio can be lifted(N)
outstanding	100%
good	80%
passing	60%
Unqualified	0%

The individual-level assessment of the incentive recipients shall be implemented in accordance with the relevant provisions of the company's current remuneration and assessment (given in Table 4). If the company-level performance appraisal of each year meets the standard, the actual amount of sales restriction lifted by the individual target in the current year = the individual plan to release the sales restriction quota in the current year× the proportion of sales restriction that can be lifted at the company level (M) × the proportion that can be lifted at the individual level (N). The restricted shares that cannot be lifted in the year of assessment of the incentive object shall be repurchased and cancelled by the company.

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3. Analysis of the implementation effect of the equity incentive plan

3.1. Operational Performance

There are three main purposes of equity incentives: first, to attract the core personnel of the enterprise and build a stable management team, second, to improve the performance of the enterprise and maximize the value of the enterprise, and third, to solve the problem of principal-agent. Therefore, the analysis of the effect of Youyou Food incentive is mainly analyzed from the aspect of financial indicators. For example, profitability, growth ability, solvency, operating effect and agency cost are judged whether to achieve the improvement of enterprise value (seen from Table 5).

Table 5: Business performance evaluation indicators:

Classification of indicators	The name of the metric
Profitability	Return on equity
	Return on total assets
	Net profit margin on sales
Develop competencies	Net asset growth rate
	Growth rate of operating income
	Net profit growth rate
Solvency	Debt-to-asset ratio
	liquidity ratio
Operational capacity	Total Asset Turnover
	Accounts receivable turnover ratio
	Current asset turnover ratio

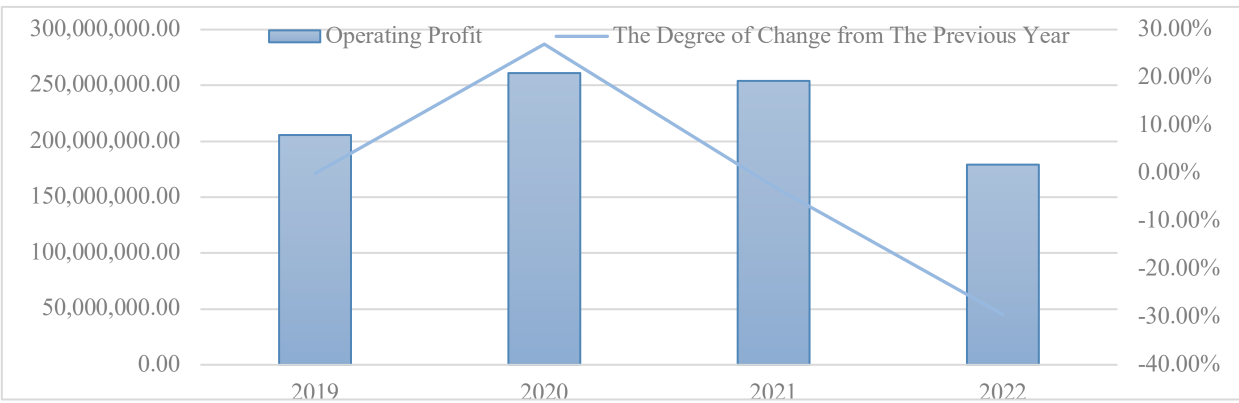


Figure 2: 2019-2022 Youyou Food operating profit

According to the data disclosed in Youyou Food's annual report, its performance evaluation indicators from 2019 to 2022 are summarized. Therefore, the financial data from 2019 to 2022 are selected for specific analysis, and the financial data before and after the implementation of equity incentives are compared to judge the impact on the financial performance of enterprises. In terms of profitability, the longitudinal comparison of operating profit and return on equity from 2019 to 2022 is mainly conducted (seen from Fig. 2). After the implementation of the restricted stock incentive plan, the company's profitability decreased significantly from 2021 to 2022. The operating profit in 2021 was 179,140,189.54, and the operating profit in 2022 was 254,084,615.35 yuan, a year-on-year decrease of 29.50% (seen from Fig. 3).

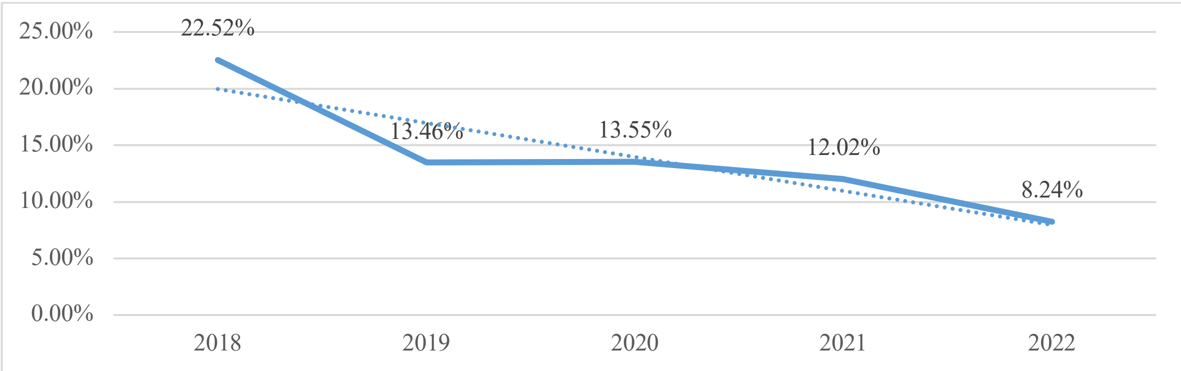
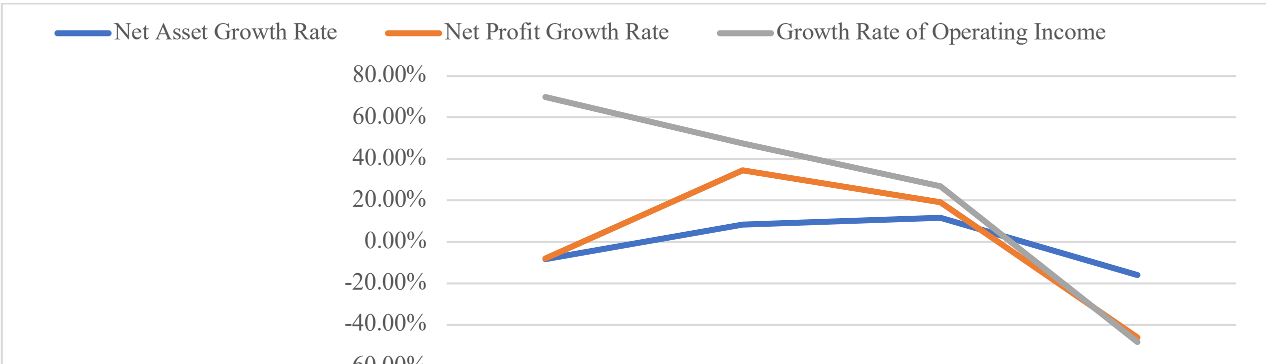


Figure 3: 2018-2022 Youyou Food's return on net assets



	2019	2020	2021	2022
Growth Rate of Operating Income	77.85%	12.87%	7.59%	-2.19%
Net Profit Growth Rate	0.48%	26.12%	7.59%	-30.13%
Net Asset Growth Rate	-8.44%	8.40%	11.62%	-16.01%

Figure 4: Youyou Food's growth ability

As can be seen from the above Fig. 3, the return on equity is decreasing year by year, which is 22.53%, 13.46%, 13.55%, 12.02% and 8.24% respectively. The dotted line in the chart above represents the trend of ROE from 2018 to 2022. In terms of development capacity, the effect of equity incentive is mainly analyzed from three aspects: net asset growth rate, operating income growth rate and net profit growth rate. From 2019 to 2021 the growth rate of net assets, operating income and net profit were all positive, indicating that shareholders' equity and operating income had increased before the implementation of the stock incentive plan, but the growth rate showed a decreasing trend, indicating that the growth value of net assets and operating income was shrinking year by year. After the implementation of the stock incentive plan, the growth rate of net assets and operating income in 2021-2022 are negative, which means that shareholders' equity and operating income have decreased. Especially from the perspective of net profit growth rate, it will be -30.13% from 2021 to 2022, mainly due to the fierce competition in the industry market in recent years, the price of raw materials, and the malicious sales of products at low prices by some competitors. Coupled with the impact of external objective factors such as the Russia-Ukraine war, economic downturn, weak consumer demand, high temperature and power rationing (seen from Fig. 4).

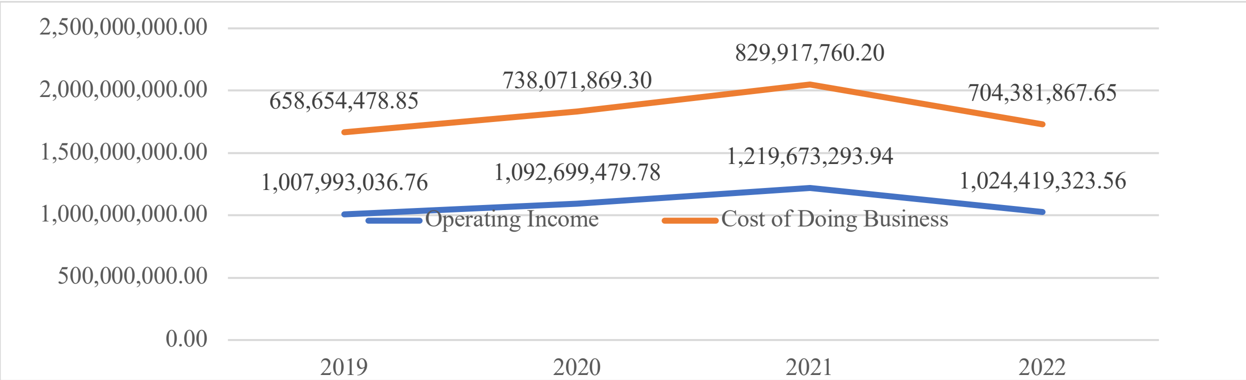


Figure 5: 2019-2022 Youyou Food's operating income and operating costs

Fig. 5 shows that the company's operating income increased much more than operating costs in the current year, but between 2021 and 2022, operating income decreased more than operating costs. It can be seen that the cost control is not ideal. Therefore, it shows that the effect of the implementation of the equity incentive plan on the growth rate of net assets, the growth rate of operating income and the growth rate of net profit has not increased, but has declined. Solvency mainly refers to short-term solvency, and this paper selects the asset-liability ratio and current ratio as the indicators. Fig.6 shows the current ratio increased from 9.51 in 2019 to 15.56 in 2020 before the implementation of the restricted stock incentive plan. After the implementation of the restricted stock incentive plan, the current ratio showed a decreasing trend, from 12.29 in 2021 to 9.5 in 2022. This indicates that the ability of the enterprise to realize its assets is weakened. The short-term solvency of enterprises is still weakening.

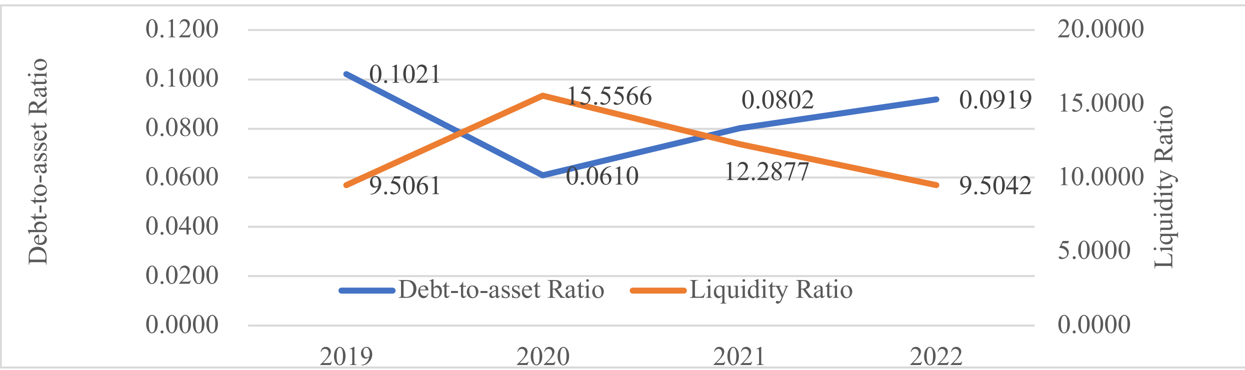


Figure 6: 2019-2022 Youyou Food's solvency

3.2. Cause Analysis

In 2019, in the face of many unfavorable factors such as the overall decline in the macroeconomic environment, the escalating Sino-US trade war, and the increasingly fierce market competition, the company's board of directors led the management team and all management cadres to achieve a slight year-on-year increase in profit level in a more difficult objective environment by strengthening internal management, expanding the market externally, strengthening product quality, and innovating and changing. The main reasons are as follows. Due to the sharp rise in raw material prices, the company raised the price of pickled pepper phoenix claws series products of different categories and specifications in September 2018, and the terminal market needed a certain amount of time to digest the impact of price increases, resulting in a year-on-year decrease of 5.86% in sales revenue of pickled pepper phoenix claws in 2019. In addition, the raw materials of the company's turkey wings come from the American market, and due to the impact of the Sino-US trade war, the market supply of turkey wings has decreased sharply and is extremely unstable, affecting sales by about 40 million yuan year-on-year. In the case of a year-on-year decline in operating income, due to the increase in gross profit margin, reasonable control of expenses during the period and increase in financial income, the company achieved a net profit of 179,051,977.81 yuan during the reporting period, a slight increase year-on-year, and the profitability was enhanced.

In 2020, the haze of the new crown epidemic shrouded the world, bringing a huge impact and test to economic development, the total amount of social zero fell by 3.9% for the whole year, although the growth rate rebounded quarter by quarter, and the consumption vitality gradually recovered, but the market environment still has great uncertainty, which brings certain challenges to business operations. In the face of the complex and changeable external environment, while doing a good job in epidemic prevention and control, the company made every effort to organize the resumption of work and production, overcome difficulties, strengthen internal control management, and achieved double growth in operating income and net profit.

In 2021, the domestic and foreign environment is complex and changeable, the new crown pneumonia epidemic situation is complex, the price of bulk raw materials continues to rise, the consumption structure is differentiated, and the industry competition is becoming more and more fierce. In the face of the new situation and new changes, the company has always maintained strategic concentration, focused on the established development strategy and annual work objectives, adhered to the work tone of "seeking progress while maintaining stability", kept an eye on the task, reduced costs and increased efficiency internally, intensively cultivated the market externally, and maintained a stable growth in production and sales scale in an unfavorable environment.

2022 is an extraordinary and challenging year in the company's development history, affected by the high price of raw materials, superimposed by external objective factors such as the Russia-Ukraine war, economic downturn, weak consumer demand, high temperature and power rationing, the company's business environment is complex and severe, and the company is facing unprecedented pressure. In the face of the new situation and new changes, the company has always maintained strategic focus, focused on the established development strategy and work objectives, adhered to the work tone of "seeking progress while maintaining stability", kept an eye on the task, reduced costs and increased efficiency internally, intensively cultivated the market externally. In 2022, the company will concentrate on overcoming difficulties and make every effort to promote the following four aspects: lean management to improve efficiency, systematic planning to ensure profits; intensively cultivate the channel and seek layout, and improve the quality of the operation and build the brand; there is a breakthrough in product research and development, and the market development has increased momentum; actively return investors and achieve common development.

4. Problems in Equity Incentives and Suggestions for Improvement

Through the above overview of Youyou Food's equity incentive plan and analysis of its implementation effect, it shows that the company's equity incentive plan has not been successful. It can be seen that there are some unreasonable aspects in the company's equity incentive plan. This section is expected to summarize the existing problems of equity incentives and give suggestions for improvement. The company should set more reasonable constraints, and the dimensions of the assessment indicators can be more diversified, such as profitability, growth ability and solvency, etc. In terms of pricing, it is necessary to weigh the benefits that employees can obtain and the value of human capital, and too high pricing may harm the interests of the company and shareholders, and too low pricing will not have a higher incentive effect.

In the choice of equity incentive model, you can choose a variety of ways to combine equity incentives. Because different equity incentive models have their own advantages and disadvantages, the use of different combinations can play a complementary role and diversify risks on the basis of giving full play to their respective strengths.

For the food industry, the industry has the characteristics of a large number of customers in the downstream of the industrial chain, frequent sales transactions, diverse sales channels, and fast product upgrading, which requires sales personnel to respond quickly to customer orders. Due to the low degree of innovation in the snack food industry, the problem of product homogenization has always existed, and innovative products have a greater role in brand influence and brand value, so it is necessary for enterprises to continue to invest in research and development, enrich the product matrix, and improve the company's core competitiveness. Therefore, when setting up the equity incentive plan, sales management personnel can be considered as incentive objects, and R&D-related indicators can be taken into account as performance conditions.

5. Conclusions

In the case analysis, this study will start with the market reaction before and after the announcement of the draft equity incentive of Youyou Food, and analyze the effect of the equity incentive from three aspects: profitability, development ability and debt repayment ability. The effect of Youyou Food's implementation of equity incentives did not reach the expected rate of return, which may be due to the economic downturn in the general environment eating up the benefits of equity incentives. The value and business performance of an enterprise include many aspects, and this paper does not analyze more aspects in the analysis of these aspects, nor does it consider the longitudinal comparative analysis. At present, more and more listed companies have begun to realize the importance of market value management to their own development, and the means used are becoming more and more scientific. Advanced, one of the most popular is the equity incentive means, this management method can positively affect the market value management of enterprises, but whether any enterprise can achieve the purpose of market value management through equity incentives after listing, what requirements should be met by the equity incentive plan implemented by listed companies in order to consolidate their market position, which is a new direction for the industry to study the relationship between equity incentive and market value management. These results put forward suggestions for improving equity incentives based on the above analysis. The company should set more reasonable constraints, the dimensions of the assessment indicators can be more diversified, in the selection of equity incentive models, can choose a variety of equity incentives combined, for the food industry, in the setting of equity incentive plan can take into account sales management personnel as incentive objects, with R&D-related indicators as performance conditions.

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