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Original Paper

Analysing the Financial Synergy Effect of Corporate Mergers and Acquisitions

—Yili's Acquisition of Ausnutria

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Abstracts

With the development of the economy, enterprises advance with the times, and mergers and acquisitions (M&A) is undoubtedly one of the important means for enterprises to integrate their own resources and explore new markets. The creation of synergies after M&A is usually the key to determine the success of M&A, and the creation of synergies can not only reduce the cost of capital of enterprises, but also improve the asset structure of enterprises. The paper analyses the case of Yili's acquisition of Ausnutria to determine whether it generates better financial synergies and draws corresponding insights.

Keyword

M&A, Yili, Ausnutria, financial synergies

1. Introduction

Nowadays, our population is becoming more aware of the institutional strengthening aspect and the health benefits of dairy products are receiving attention. The new crown epidemic has also boosted people's demand for immune boosting through dairy protein supplementation. The popularity of China's mid-to-high-end dairy products in the market has also been further strengthened.

China's dairy industry can be said to be composed of two giants, Yili and Mengniu, with some regional brands competing with each other. Yili has taken corporate globalisation and product health diversification as its strategic goal. The most crucial part of its business map is undoubtedly to become "top three in the global dairy industry by 2025" and "No. 1 in the global dairy industry by 2030", but Yili's share of foreign markets is not large, and the level of internationalisation needs to be improved. After the Sanlu milk powder incident, market has been hit hard, Ausnutria mainly focuses on high-quality products, it has high-end nutritional products and herbal formulas, and its goat milk powder also belongs to the status of the industry leader, and has the rare "blue hat" qualification in the health care products, has 9 factories in the overseas market and mature industrial chain ,supply chain layout. Yili acquires it will can help strengthen brand reputation, seize market share and expand scale of the overseas market, enable Ausnutria's advantages to be transformed into its own advantages more quickly and realise its strategic goals.

M&A can gain synergies. Both of them enjoy relatively high visibility in the dairy industry and have their own competitive qualities. Through M&A, the leading position of Yili can be solidified, and the shortcomings of Ausnutria such as under-utilisation of local resources can be solved, so that the complementary and synergistic effects of M&A can be achieved from all dimensions.

2. Method

2.1 Theoretical Analysis

2.1.1 Theories of M&A

M&A theory suggests that this is one of the most important tools for sustainable development of enterprises in contemporary economic life, which not only enables enterprises to make a rational allocation of resources, but also expands the scope of production and reduces the cost of capital, thus increasing the value of the enterprise. The global merger and acquisition wave of the nineties, before that, there have been four large-scale global merger and acquisition wave and produced relative merger and acquisition theory. With the development of M&A behaviour, M&A theory has been further improved.

2.1.2 Theory of Financial Synergies

Financial synergies, which refer to the direct benefits of a merged enterprise's improved financial position as a result of synergies. This is expressed in terms of improved financial capabilities, including higher internal cash flows, investment of internal funds in more productive investment opportunities, lower cost of capital, and improved profitability and solvency. The enterprise will receive a higher return on its investment after the completion of the M&A.

2.2 Analysis of the M&A Parties and the M&A Process

2.2.1 Company Profile

Yili, founded in June 1993, is one of the top five groups in the global dairy industry, and has been ranked No. 1 in the Asian dairy industry for nine consecutive years. Yili is also the largest and most complete range of products in China's dairy industry, and has long been in the leading position in China's dairy industry. The enterprise has a wide range of main businesses, including dairy products for infants and young children, products for the middle-aged and elderly, liquid milk, yoghurt and raw milk. It has made steady progress even though the industry is in a tough situation.

Ausnutria, established in September 2003, has nine factories around the world and currently ranks among the top five infant formulae in China. Its main business involves infant formula, children's and adult milk powder, nutraceuticals, probiotics and other nutritional foods for the whole life cycle. Over the past decade, Ausnutria has been continuously laying out new industrial chains globally and devoting itself to the development of high-end nutritional food, laying the foundation for its products to achieve quality, differentiation and high-end.

2.2.2 M&A Process

On 27 October 2021, Yili announced the acquisition of shares of Ausnutria Dairy by the Group's subsidiary, Goldenport Trading Holdings Limited of the Hong Kong Special Administrative Region, by way of a wholly-owned subscription of new shares and an agreed transfer. As of 3 March 2022, Yili held a total of 953,163,623 shares in Ausnutria Dairy, representing approximately 52.70% of its total shares. On 17 March of that year, Golden Harbour Holdings became the largest shareholder of Ausnutria Dairy, holding a total of 1,070,113,149 million shares of Ausnutria Dairy, accounting for approximately 59.17 per cent of the total shares of the enterprise, and completing the general tender offer for Ausnutria.

2.3 Financial Synergy Analysis

2.3.1 Analysis of Operating Capacity

Table 1 Indicators of Yili's corporate operating capacity

Unit: times

	Time							
norm	2021.6	2021.9	2021.12	2022.3	2022.6	2022.9	2022.12	2023.3
Inventory turnover	2.65	3.17	2.50	2.00	1.91	1.81	1.51	1.47
Accounts receivable turnover ratio	55.56	50.20	49.46	50.26	44.68	42.10	39.42	44.95
Total asset turnover	0.34	0.33	0.28	0.28	0.27	0.25	0.23	0.24

Operational capacity reflects the speed at which assets flow from inputs to outputs during the period of the enterprise's operations.

Inventory turnover ratio responds to the time it takes to sell and realise a firm's inventory. From Table 1, there is a significant drop after Yili's merger with Ausnutria. 2022 in the first half of the year, looking at Ausnutria's inventory turnover days alone was as high as 211 days, while Yili's was 44 days, and the merger of Ausnutria has made in the statement of Yili suffered a certain impact. Affected by the epidemic, the transportation of Yili's liquid milk was hindered, sales were slow, inventory liquidity was poor, and the inventory squeeze made the inventory realisation capacity decline.

Accounts receivable turnover ratio reflects the speed of realisation of accounts receivable and collection of sales revenue. Yili declined quarterly from June 2021 to the end of 2022. The existence of the epidemic, the slow flow of funds from various enterprises, the breakage of the enterprise's capital chain, and the increase in accounts receivable due to M&A led to this phenomenon; with the end of the epidemic, the market gradually returned to the right track, and the turnover ratio improved, and may gradually improve in the future.

The total asset turnover rate reacts to the sales capacity of the enterprise to drink the efficiency of asset utilisation. The data shows that it is also going downhill line, but not obvious, which is linked to the sales realisation ability. Overall, Yili merger and acquisition of Australia to make Yili group scale expansion, product quality has been improved, but a short period of time the quality of enterprise management and the use of efficiency is still to be improved, it can be said that the merger and acquisition of the operating capacity in the aspect of the financial synergies did not produce obvious.

2.3.2 Solvency Analysis

Table 2. Solvency Indicators for Yili

	Time							
norm	2021.6	2021.9	2021.12	2022.3	2022.6	2022.9	2022.12	2023.3
current ratio	0.88	0.85	1.16	1.11	1.03	1.09	0.99	1.02
Quick ratios	0.73	0.70	0.95	0.91	0.82	0.89	0.75	0.80
asset-liability ratio	0.63	0.57	0.52	0.55	0.57	0.58	0.59	0.61

Solvency is the key to judging whether a company's financial capital position is good and how risky it is to repay.

Current ratio reflects the liquidity of enterprise assets, for enterprises, the current ratio is not the higher the better, generally speaking, its value should be greater than 2, half of the current assets in the short term can not be realised, but also to ensure that all current liabilities can be repaid, the current asset ratio is too large to affect the enterprise's operating profit or investment profitability. From the table, we can see that the overall change of current ratio after Yili's acquisition of Ausnutria is not significant, slightly increased, which means that the enterprise's current assets utilisation rate is limited, and the ability to repay short-term debts has not changed significantly. Through the overall data shows that Yili short-term debt service capacity is weak, there is the impact of the new crown epidemic, with the disappearance of the epidemic and the integration of M&A, showing a slow upward trend.

When the quick ratio is greater than 1, the enterprise can maintain a better short-term debt repayment ability and financial stability. Its trend is similar to that of the current ratio, the quick ratio and the current ratio do not change much, slightly rising, which indicates that the short-term debt repayment ability of Erie after the acquisition of Ausnutria is still not substantially improved, and there is a greater possibility of not being able to repay the current liabilities in a timely manner, which also implies that the financial risk of the enterprise is rising.

After Yili's acquisition of Ausnutria, the gearing ratio is on an upward trend, and it is also around 61% after the integration, which indicates that Yili's long-term solvency has weakened. To sum up, Yili used cash payment in the merger and acquisition of Ausnutria, which led to a significant reduction in its current assets, an overall decline in short-term and long-term solvency, and no positive financial synergies in terms of solvency after the merger and acquisition.

2.3.3 Profitability Analysis

Table 3. Profitability Indicators for Yili

Unit: %

Norm	Time							
	2021.6	2021.9	2021.12	2022.3	2022.6	2022.9	2022.12	2023.3
Sales margins(ROS)	8.55	9.20	2.97	11.33	8.06	6.34	4.67	10.81
return on assets(ROA)	11.55	12.17	3.28	12.57	8.70	6.34	4.28	10.39
return on net assets (ROE)	30.38	31.26	7.37	28.48	21.35	16.27	11.15	27.87

The profitability ratio reflects the profitability of an enterprise. The higher the ROA, the greater the creativity and the significant results achieved by the enterprise in terms of increasing revenue and saving the use of capital, etc. The level of ROE reflects whether the enterprise is able to utilise its own capital profitably. As can be seen from the table, all three data have the same trend of change, and all of them have declined after M&A. There are a few factors: firstly, the market is not favourable due to the impact of the new Crown Pneumonia; secondly, the business undergoes integration activities during the merger and acquisition process, which generates additional higher economic costs. Costs rise yields and vice versa, Ausnutria has also issued an announcement to indicate that: the company's own brand Hepunokai 1897 provides a series of sales strategy adjustments to the distributor to provide all aspects of support, so that the performance has been affected. Chain reaction Yili is also bound to be implicated. Thirdly, the supply of domestic milk sources in China is tight, the price of raw milk has risen, and the cost of some imported raw materials has only risen. In addition, competition in the industry continues to intensify, the major dairy industry in the promotion of their own products to increase investment, the cost of a substantial increase in the above and other reasons make the rate of return reduced. As of March 2023, the end of the epidemic coupled with a period of integration of the business has resulted in a gradual recovery of the figures, but the merger did not produce the expected financial synergies in terms of profitability.

2.3.4 Analysis of Tax Savings

This is a merger and acquisition between different enterprises in the same industry. After the merger and acquisition, the size of Erie will be enlarged, the operating income will be increased, and the incentive share will be more, and the enterprise will need to pay more taxes. Generally speaking, the merger and acquisition of enterprises will choose the enterprise that is in a large number of losses but in good operating condition. On the basis of legal taxation, the acquirer can achieve tax savings by offsetting the company's profits and losses to delay taxation. Ausnutria's revenue and net profit fell sharply in the second half of 2022, but it did not operate at a loss. Yili's consolidation of Ausnutria's statements does not reduce the company's tax burden, has no tax-saving effect, and does not create financial synergies.

3. Enlightenment

3.1 Reasonable Selection and Strengthening of Core Competitiveness

M&A is to enable enterprises to achieve further long-term development, to achieve the effect of 1+1>2, M&A must be in line with the development trend of the times. Enterprises in M&A should be clear about their future strategic layout, directed to find a suitable target company, fully understand the advantages of the target company, potential risks and whether it is consistent with their future development goals. In addition, it should choose the appropriate payment method for M&A to diversify the financial risks brought by the acquired party. After the merger and acquisition, both parties will complement each other's advantages, give full play to their strengths, rationally allocate their existing resources, realise all-round complementarity, enhance their core competitiveness, and further solidify their position in the market.

3.2 Integrate Resources and Exploit Synergies

Enterprise M&A is not only the success of the merger of the two enterprises, but also focus on the merger and acquisition of the head office can get the expected benefits, the key to the success of an enterprise merger and acquisition of the merger and acquisition of the proceeds of the merger and acquisition of the proceeds of the merger and acquisition of the two are greater than the total proceeds of the merger and acquisition of the two before the performance of synergistic effect is also where the performance of the play. Enterprises in the realisation of M&A after the integration of their existing resources, to achieve complementary, play "1 + 1 > 2" synergistic effect. The highlights of the cooperation between the two companies to carry out comprehensive resource integration, and jointly promote the development of enterprises to play a more powerful synergistic effect.

4. Conclusion

Yili acquired Ausnutria with a large amount of cash payment, and at the time of acquisition, there was a share price premium for Ausnutria, and the large amount of cash outlay led to the weakening of Yili's ability in terms of debt servicing. Ausnutria has been having problems with inventory build-up and pressure on stock, and Yili has also been affected in terms of operations. In terms of profitability, although earnings per share improved slightly, various yield indicators showed a downward trend. The tax saving effect is also not reflected. Overall, the merger and acquisition did not achieve significant financial synergies. However, the data show that there is a tendency to turn back, the future may produce the expected synergies, the merger and acquisition will take some time to break in.

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