

# Case study of Sunac China's diversified mergers and acquisitions

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**Abstract:** The Party in the 1990s merger boom into China, the real estate industry in the "merger and acquisition of the road" can be said to be in full swing. With the change of social policies, "business transformation", that is, seeking diversified development, has become one of the important motivations for M&A in the context of increasingly difficult and expensive "land acquisition". And Sunac China by virtue of the amazing speed and scale of mergers and acquisitions, in the real estate industry of mergers and acquisitions boom to stand out, people's attention. Therefore, this paper classifies the series of M&A cases of Sunac China according to the M&A motivation, mainly discusses the two M&A cases based on the "business transformation" M&A motivation, analyzes the M&A performance respectively, summarizes the problems that enterprises tend to ignore when making cross-industry investment, and puts forward the corresponding investment countermeasures, which has certain reference significance for enterprises' cross-industry investment.

## 1. Introduction

Since the reform and opening up in 1978, people's living standards have continued to improve, the scale of investment has also expanded rapidly, capital accumulation in various industries has been rapid, and production capacity has been greatly enhanced. In today's fierce competition and great policy changes, how to implement strategic transformation and better development of the real estate industry has become the focus of people interested in real estate. At present, housing has become the rigid demand of the people, and the real estate industry has also become the pillar industry of the national economy. As the problems of "difficult housing" and "expensive housing" in big cities become more and more prominent, the government pays more and more attention and intervenes more and more.

Since the Central Economic Work Conference in December 2016 for the first time put forward the phrase "house is for living in, not for speculation", it has been strongly echoed and supported by the public, and the domestic real estate regulation policies are also gradually changing. In recent years, the central government has carried out frequent real estate regulation and control policies in order to curb the excessively rising housing price. In order to get a piece of land, it needs to pay more and more, so the financing cost of the real estate industry is also getting higher and higher. However, the government still does not relax its initial positioning and resolutely stabilize the housing price. With the increase of real estate enterprises, the market is becoming more and more saturated, forcing many real estate enterprises to change their development mode in order to reduce the

risks brought by policy changes and seek diversified development of enterprises. For example, Wanda, Evergrande, Vanke are actively integrating with other fields except real estate, which is in line with the transformation trend of diversification of the real estate industry. However, compared with the investment performance of the same industry, the investment performance of cross-industry investment is still relatively low. Therefore, under the inevitable trend of diversification and integration, it is urgent to sum up the experience and lessons to improve the success rate of investment.

## 2. Introduction to Sunac China

Sunac China is an enterprise with comprehensive development of residential and commercial real estate as its main business. Founded in 2003, its brand concept of "Zhizhi Zhiyuan" is deeply rooted in the hearts of the people, striving to pursue the development and management of high-end properties, adhering to the regional focus and high-end boutique development strategy, and is committed to integrating high-quality resources (such as real estate development, property services, conferences and exhibitions, tourism and vacation, theme parks, commercial operations, hotel operations, medical care, IP development and operation, film and television content production and distribution, etc.) through high-quality products and diversified services. A complete solution for a better life for Chinese families.

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### 3. Sunac China acquires Wanda Tourism

#### 3.1. M&A process

On July 10, 2017, Wanda Commercial and Sunac China issued a joint announcement that Wanda transferred 91% of the equity of cultural tourism projects in 13 cities to Sunac, namely 29.575 billion yuan; Total equity of 76 hotels, or 33.595 billion. Although Wanda transfers most of the equity, it still retains the actual control of Wanda, that is, both parties agree to keep the brand unchanged, the planning content unchanged, the project plan unchanged and the project construction unchanged after the completion and delivery of all projects. Despite the acquisition value of more than 60 billion yuan, Wanda agreed to Sunac pay for the acquisition in four installments. After Wanda paid all the money, a third party, R&F Real Estate, signed a strategic cooperation agreement on July 19, 2017, to undertake 77 hotel projects of Wanda Group. This eye-catching merger case also came to an end.

#### 3.2. M&A performance analysis

##### 3.2.1 Solvency analysis

**Table 1.** Solvency Analysis Table

	Current ratio	Quick ratio	Debt to asset ratio
2016	1.50	0.72	87.92%
2017	1.3	0.48	90.27%
2018	1.17	0.45	89.80%
2019	1.17	0.39	88.12%
2020	1.17	0.38	86.56%

As can be seen from the table 1, Sunac China's current ratio before the merger was 1.5, the quick ratio was 0.72, and the short-term solvency could still meet the normal requirements, but the current ratio dropped to 1.3 in the year of the merger and the quick ratio dropped to 0.48, and continued to decline in the following three years, the short-term liquidity of the enterprise declined, and the short-term solvency was reduced. Sunac China's debt to asset ratio before the merger was 87.92%, which was already higher than the average level of the general real estate industry, but it reached almost 90% after the merger, and the long-term solvency of the enterprise was also low, and the financial risk was large, and with Sunac China's attention and control of its debt to asset ratio in the past two years, the Debt to asset ratio has decreased, and the financial risk of the enterprise has also been reduced. And profitability continues to rise.

##### 3.2.2 Profitability analysis

**Table 2.** Profitability analysis table

	Net operating interest rate	Net interest rate of equity	Earnings per share growth rate
2016	8.31%	11.72%	-26.8%
2017	17.71%	32.81%	288.73%

2018	13.98%	32.92%	37.73%
2019	16.63%	37.21%	58.05%
2020	15.13%	12.17%	1.69%

As can be seen from the table 2, in the year of Sunac's acquisition of Wanda Cultural Tourism, the net operating interest rate of the enterprise increased by two times, the net interest rate of equity increased by about three times, and the growth rate of earnings per share growth rate also changed from negative to positive 288.73%, and the three financial indicators reached the maximum in the year of acquisition, indicating that the acquisition of Wanda Cultural Tourism has a positive impact on the enterprise. Improve the profitability of enterprises, shareholders' equity level has also been greatly improved. However, all three indicators declined to some extent between 2018 and 2020, which may have been influenced by the COVID-19 pandemic, when many businesses shut down production and had no source of income.

##### 3.2.3 Operation capacity analysis

**Table 3.** Operation capacity analysis table

	Inventory turnover rate	Accounts receivable turnover rate	Total assets turnover
2016	1.50	0.72	87.92%
2017	1.3	0.48	90.27%
2018	1.17	0.45	89.80%
2019	1.17	0.39	88.12%
2020	1.17	0.38	86.56%

As can be seen from the table, the inventory turnover rate of Sunac China decreased by 10 percentage points in the year of the merger and acquisition, increased by 5 percentage points in 2018, and failed to rise back to the level before the merger and acquisition in 2019, indicating that although the merger and acquisition of Sunac China improved the profitability of the enterprise, it also led to the problem of inventory accumulation. Since 2017, all three ratios have improved significantly. This shows that the company quickly adapted to the operation of the new business and made timely strategic adjustments. Therefore, the merger and acquisition behavior still plays a positive role in Sunac China's operation capacity in the long run.

Through the performance analysis of Sunac China's merger and acquisition of Wanda Tourism, it is not difficult to conclude that although merger and acquisition has improved the profitability of the enterprise, it is followed by the increase of the debt to asset ratio of the enterprise, the expansion of financial risks, the lack of cash in the hand of the enterprise will inhibit other daily business activities of the enterprise, and the inventory backlog caused by the merger and acquisition to cater to customers is also a problem that the enterprise needs to solve.

## 4. Sunac China M&A Raycom

### 4.1. M&A process

On the evening of September 18, 2016, Sunac China and Legend Holdings issued a joint announcement announcing that on September 16, Sunac Real Estate, a subsidiary of Sunac China, signed two framework agreements with Legend Holdings and its subsidiary Raycom. According to the agreement, Sunac China will acquire the relevant equity and debt rights of 41 target companies under Raycom for a total consideration of approximately RMB13.788 billion. According to the announcement, these 41 property projects are located in 16 cities including Beijing, Tianjin, Chongqing and Hangzhou, with a total area of about 6.937 million square meters, a total construction area of about 18.022 million square meters, and an unsold area of about 7.3 million square meters. Upon completion of the transaction, Beijing Rongyan, Beijing Rongrong, Rongke New Landmark and First Pacific Rongke will become joint ventures of Sunac China. On October 12, 2016, Sunac China registered and established Beijing Sunac Roycom, a wholly-owned subsidiary, to operate the real estate business acquired from Legend Holdings. Legend Holdings will continue to hold its interest in the Rongke Information Center Park in Beijing and its 60% stake in Wuhan Zhigu Investment Co., Ltd.

### 4.2. M&A performance analysis

#### 4.2.1 Solvency analysis

**Table 4.** Solvency Analysis Table

	Current ratio	Quick ratio	Debt to asset ratio
2014	1.50	0.74	81.33%
2015	1.45	0.68	83.19%
2016	1.49	0.72	87.92%
2017	1.30	0.48	90.27%
2018	1.23	0.47	90.52%

As can be seen from the table 4, Sunac China's current ratio has remained at a relatively healthy state of about 1.50 from 2014 to 2016, but it has dropped to 1.30 or even less in the two years after the completion of the merger; the quick ratio has also dropped from about 0.7 before the merger to 0.47 in 2018, which indicates that Sunac China's short-term solvency has declined after the completion of the merger and acquisition activities, and there is certain pressure. Since 2014, Sunac China's debt to asset ratio has also been increasing, even exceeding 90% after the completion of the merger, and its long-term solvency has also declined. This shows that the acquisition of Sunac China is to obtain land resources through a large amount of debt, which also expands Sunac China's financial risks.

#### 4.2.2 Profitability analysis

**Table 5.** Profitability analysis table

	Net operating interest rate	Net interest rate of equity	Net interest rate of total assets
2014	12.89%	15.41%	2.88%
2015	15.68%	18.58%	3.12%
2016	8.31%	8.30%	1.00%
2017	17.71%	19.24%	1.87%
2018	14.55%	32.00%	3.04%

As can be seen from the table 5, the net operating profit margin in the year of completion of the merger decreased from 15.68% to 8.31%; Net interest rate of equity from 18.58% down to 8.30%; The net interest rate of total assets fell from 3.12% to 1.00%, and all three indicators showed a sharp decline, which shows that Sunac China's performance in the year of the acquisition of Raycom is not optimistic. However, in 2017 and 2018, all three indicators showed a "recovery", and there was a certain improvement compared with the two years before the merger, so it was judged that this M&A activity had a certain positive impact on Sunac China's business performance.

#### 4.2.3 Operation capacity analysis

A company's accounts receivable play a pivotal role in current assets. If the company's accounts receivable can be collected in a timely manner, the company's efficiency in the use of funds can be greatly improved. Accounts receivable turnover ratio is the ratio that reflects the speed of a company's accounts receivable turnover. The turnover rate of accounts receivable should also be considered in conjunction with the business mode of the enterprise, and it is not the shorter the better.

**Table 6.** Operation capacity analysis table

	Turnover	Accounts receivable	Account receivable turnover rate
2014	2507195.9	37297.8	67.22
2015	2301094.3	9221.1	249.55
2016	3534349.2	81986.3	43.11
2017	6587351.5	123515.9	53.33
2018	13974834.3	180197.3	77.55

As can be seen from the table 6, the account receivable turnover rate increased significantly from 67.22 in 2014 to 249.55 in 2015, an increase of about 3.71 times, which is due to the fact that there are fewer accounts receivable in 2015 and the return of corporate funds is faster. In the year of the completion of the merger, the turnover rate of accounts receivable plummeted to 43.11, and the company's accounts receivable in that year became more and the return of funds slowed down. Fortunately, in 2017 and 2018, the accounts receivable turnover rate has improved, although it has not returned to the previous level, but compared with the year of mergers and acquisitions, the operating capacity is still somewhat improved.

Through the analysis of Sunac China's profitability, solvency and operating capacity after the merger, it can be seen that its solvency has decreased compared with

before, and it faces certain financial risks. In the year when Sunac China acquired Raycom, the operating situation did not improve significantly, and the profitability, operating capacity and development ability of the enterprise were not optimistic on the whole. In the following two years of the merger, with the expansion of the company in the market, Sunac China has improved its profitability, operation and development capabilities compared with before the merger, so it can be concluded that the merger and acquisition of the two will still help improve Sunac China's performance.

## 5. Conclusion

This paper analyzes the performance of Sunac China's acquisition of Wanda Cultural Tourism and Sunac Smart Land, and concludes that although M&A activities can help enterprises improve their profitability and create profits for enterprises in such a competitive environment to a certain extent, due to the high acquisition consideration, the financial leverage of enterprises is large, which increases the financial risks faced by enterprises, especially in today's rapidly changing society, weak liquidity of funds will make enterprises fall into potential risks. The diversified development of enterprises is of course important, but more important is the issue of how to take the road of diversified development in merger and transformation, and how to use better mechanisms and synergies to resist risks. Based on this, I believe that future business combinations should focus on:

(1) Select the appropriate company according to the M&A motive to maximize synergy.

We need to think about what kind of diversified companies do we need in today's society. A diversified merger is not just a simple combination of two companies with different business areas, but a synergy between complementary companies under the premise of market needs. For example, when the new crown epidemic was serious, many businesses closed their stores for several months, resulting in negative operating profits and even many stores closing their doors, but at that time, a snack company reached an agreement with a supermarket that was still open during the epidemic to sell its own product buying and selling rights to supermarkets, so that customers could buy snacks from this store when resources were scarce, and the store's business performance was even better than before the epidemic.

(2) Payment methods can be combined with multiple methods.

On the one hand, the outflow of too much cash at once will lead to the shortage of funds of the enterprise, the financial leverage of the enterprise is large, the financial risk is high, on the other hand, the small amount of funds retained in hand inhibits other investment management activities of the enterprise, although the one-time payment in cash can solve the problem of the capital difficulties of the invested enterprise to some extent, but the long-term goal of the invested enterprise is still to hope that its own enterprise

can do better and better under the leadership of the investor, so the investment and financing methods should be as diversified as possible. Or the payment method and term can be more flexible.

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