

Financial analysis on GEELY major acquisition on Volvo

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Abstract: His paper analyzes Geely's financial performance after its acquisition of Volvo, focusing on indicators such as net profit margin, return on total assets, market share, sales volume, and export volume. The study found that Geely experienced a consistent increase in sales volume following the acquisition, especially in terms of export volume. This expansion has further strengthened Geely's position in both domestic and foreign markets. Moreover, Geely's net profit margin has shown steady growth, indicating improved profitability and efficient resource management. The company's ability to effectively control costs and optimize operations has contributed to its enhanced financial performance. This, in turn, has boosted investor confidence and solidified Geely's reputation as a financially stable automotive company. In addition, the return on total assets has been positive, indicating that Geely has been able to generate higher returns with its increased asset base. The incorporation of Volvo's technological expertise and brand value has played a vital role in this success. By leveraging Volvo's resources and capabilities, Geely has been able to offer innovative and high-quality vehicles, which have resonated well with consumers.

1. Introduction

China plays an increasingly important role in the global market and with this process, Chinese capital is gradually accumulating and the Chinese enterprises are increasing their acquisition of foreign technology, R & D and high-quality brands from time to time. Geely's acquisition of Volvo, the largest overseas M&A in China's automotive industry, has always attracted much attention. Geely's acquisition of Volvo did not only obtained a number of technologies from Volvo, but also improved Geely's brand image. Through the financial report of Geely Automobile, this paper analyzes the changes of relevant financial data before and after Geely's acquisition, and analyzes the details in the process of their integration.

In 2008, the global financial crisis broke out and Ford made huge losses. After selling Jaguar and Land Rover to Tata Motors in India, Ford decided to sell Volvo business in December 2009, which would reduce the production costs and fully ensure the fluentness of the development and operation of Ford brand. At the end of 2008, Ford's business debt was US \$25.8 billion. Even if the debt reduction was successful, there was still a shortage of more than US \$10 billion. Selling Volvo can quickly return the funds and avoid further difficulties for Ford. This is also one of the major strategic decisions for Ford to reduce costs and debt, improve its financial situation and regain profitability. In 1999, Ford invested US \$6.4 billion to acquire Volvo cars, making this luxury

passenger car brand headquartered in Sweden as a wholly-owned subsidiary of Ford, but then it had to make a loss deal and sell it at a price of less than US \$2 billion. On August 2, 2010, Geely Group acquired 100% equity and related assets (including intellectual property, production line, supplier system, etc.) of Ford's Volvo car company with us \$1.8 billion. According to the agreement signed by both parties, Geely Group has not only acquired all the equity of Volvo, but also will own the core technology, patents and other intellectual property rights of Volvo. The patented technology was mainly referred to automobile safety technology, such as anti-skid braking system, emergency brake light, intelligent driving information system, emergency brake assist system and anti-lock braking system.

Judging the performance of the acquisition from Geely's financial reports in recent years, so far Geely's acquisition is successful. Since the case occurred in 2010, this study mainly analyzes the financial report data before and after the M&A. From 2009 to 2013, Geely's turnover continued to grow. After the acquisition, with the application of Volvo's advanced technology to Geely's auto products, the expansion of the market share and the brand effect brought by the acquisition of advanced brands, its turnover showed a rapid growth trend after 2011.

By 2015, Geely's turnover had exceeded 30000 million yuan. By analyzing the indicators and data related to Geely Automobile's solvency from 2009 to 2013, we can judge the changes of Geely's financial data after the acquisition and analyze the impact of the acquisition on Geely's solvency. Geely's current ratio decreased from 2009 to 2011. The current ratio was reduced due to the increase of current liabilities caused by the acquisition, indicating that the solvency of current liabilities caused by the acquisition decreased. After 2011, the increase of current assets was greater than that of current liabilities, and the current ratio rebounded, indicating that the company's solvency rebounded with the completion of the acquisition. From the perspective of quick ratio, the quick ratio in 2011 is lower than that in 2010 and 2009. From the analysis of financial statements, the main reason is that the inventory in 2011 was 1.35 billion yuan, while in 2010 and 2009 it was 0.966 billion yuan and 0.727 billion yuan respectively, indicating that the inventory of Geely had increased due to M&A and its reduced short-term solvency. After 2011, the quick ratio has rebounded and the solvency has increased. From a long-term perspective, M&A has little impact on Geely's short-term solvency. Before and after the merger, the biggest change in Geely's solvency index was the interest cover ratio while the profit before interest tax increased slightly, which significantly reduced Geely's solvency. Although the interest cover ratio rose to 8.00 in 2011, it is still lower than that in 2009, indicating that the impact of interest expenses caused by M&A continues. After 2011, the interest cover ratio increased steadily, indicating that its long-term solvency gradually recovered after a long time after the acquisition, and the company's debt repayment situation improved.

2. Literature Review

Corporate finance is a theory about corporate financial management. Firstly, from the aspects of financing, investment and profit distribution, combined with the example of Geely's acquisition of Volvo, this paper analyzes the role of corporate finance theory in various financial decisions and evaluation of the company's financial situation. Through specific discussion, this paper analyzes the importance of rational use of corporate finance theory in corporate financial management. Secondly, through the research of other scholars, it puts forward some suggestions on how to use corporate finance theory to manage Chinese companies^[1].

The efficiency theory holds that M&A improves the efficiency of enterprises, improves the respective operating efficiency of both parties, and thus improves the performance. As a sorting analysis, the overall efficiency and value after M&A are not simply the sum of all parts, and the

value created is far greater than the sum of the values of all parts, resulting in potential value-added. Efficiency theory can be further classified into management synergy, operation synergy, financial synergy and so on^[2].

Some scholars discuss related or unrelated mergers and acquisitions with comprehensive effect theory, organizational learning and resource-based theory. For example, Zeng Zhenzhen (2010a) and Xu Mingjun (2000) explore the comprehensive effects of mergers and acquisitions, while Wang Zhusan, Zhou Dewei, and Chen Hongrong (2006) analyze the impact of M&A payment methods on performance using agency theory. Other scholars, such as Xu Peiji, Ye Yinhua, Qiu Qilun, and Wang Wanting (2013), study the influence of managers' overconfidence and characteristics on M&A from the perspective of behavioral finance and senior management theory. Additionally, some literature adopts network theory to investigate the relationship between a CEO's network core degree within a company and M&A (EL Khatib, Fogel, and Jandik, 2015).

Apart from the comprehensive effect theory, there are numerous studies focusing on the internal characteristics of companies based on resource-based theory, organizational learning, and agency theory. These studies examine the impact of strategic resources, R&D stock, M&A experience, or knowledge transfer ability on M&A (Qiu Yijia and Zeng Weiguo, 2014). Furthermore, the external characteristics of companies are predominantly explored through network/relationship theory, investigating how factors such as banking relationships, political connections, and intercompany networks affect M&A behavior and performance (Ishii and Xuan, 2014).

In the part of corporate governance, some scholars study institutional legal persons, the degree of good and bad corporate governance, equity / board structure from the perspective of corporate governance, or explore their impact on M&A from the perspective of investor protection and corporate social responsibility (Deng, Kang, and Low, 2013). Industrial level research takes market power, M&A boom, herding, political hot period, or environmental richness and environmental dynamics in the perspective of organizational ecology as the theoretical point of view (Zhou et al., 2015; Qiu Yijia and Zeng Weiguo, 2014).

In addition, some studies use multinational samples to discuss the relationship between national level factors, such as legal or cultural differences and M&A (Wang and Wang, 2012). Some scholars also use the behavioural finance perspective to explore how investors or managers in different countries affect M&A (Ferris, Jayaraman, and Sabherwal, 2013). Because cross-border M&A involves differences at the national level, previous studies have discussed various aspects related to this issue. For instance, researchers have explored topics such as entry mode selection into the host country and value creation based on transaction cost or compromise theory (Shimizu et al., 2004). Additionally, some studies have examined the impact of cross-border M&A on the host company from the perspectives of the law and reputation constraint hypothesis or cultural and legal differences (Ahern, Daminelli, and Fracassi, 2015).

Previous M&A studies not only discussed M&A topics with single or comprehensive multiple theories, but also conducted literature analysis and review on M&A performance, factors affecting M&A and cross-border M&A (Shimizu et al., 2004; Butler, Perryman, and Ranft, 2012; King et al., 2004; Krug et al., 2014; Tuch and O'Sullivan, 2007).

In terms of performance, the relevant review literature points out that M&A will not only affect the financial (long-term, short-term stock price and accounting performance) and operating performance (innovation, market and productivity performance), but also affect the company's stakeholders, payment premium and management changes. In terms of influencing factors, it focuses on factors such as transactions, managers, companies, environment and national characteristics.

3. Impact on financial performance

Previous M&A literature points out that in addition to acquiring the resources required by the company through M&A to improve operating efficiency and increase the profitability of the company, M&A activities also hide the agency problem of managers seizing personal interests, which will further affect the operating performance of the company after M&A. On the contrary, it negatively affects market performance and reduces operating performance. The empirical results of Huang Zhiren and Wen Yihao (2008) also pointed out that the parent company did not produce comprehensive operational, market and financial effects after the merger of subsidiaries, so the parent company produced negative short-term abnormal returns, and there were no significant long-term abnormal returns one year after the announcement. Chen Anlin et al. (2000) found that M&A announcement has a significant positive short-term cumulative abnormal return. Wang Zhusan et al. (2006) also found that the short-term shareholder wealth of the merging company was significantly positive on the day before and after the announcement of M&A activities, but the cumulative abnormal returns on the 20 days before and after the announcement were not significant. However, the financial industry had positive short-term abnormal returns during this announcement period. The long-term remuneration and operating performance of state-owned merger companies are better than those of private enterprises. Higgins and Beckman (2006) pointed out that due to the high complexity of the reconciliation between corporate policies and transnational environment, Japanese enterprises had no significant short-term abnormal returns before the deregulation of M&A regulations, whether domestic or cross-border M&A. even after the deregulation of regulations, they had positive short-term abnormal returns only when merging domestic target companies^[3].

M&A not only affects the company's long-term and short-term financial or innovation performance, but also affects the payment premium in M&A activities, the change of senior managers, the performance of creditors, competitors and marketing, as well as subsequent M&A behaviour. The research on the change of senior managers in M&A mainly focuses on how the network or relationship of directors and senior teams affects and changes of managers after M&A (Ishii and Xuan, 2014); The impact on creditors part discusses how the rights protection actions of hedge funds and the degree of creditor's rights held by informed traders or managers affect the bond value of the main and target companies (Klein and zur, 2011; Phan, 2014). There are also studies on whether M&A affects the competitiveness of rival companies in the industry (offenberg and pirinsky, 2015) and how M&A affects the company's marketing expenditure (fee, hadlock, and pierce, 2013).

4. Financial Analysis

4.1 Analysis of Geely Automobile operation capacity from 2009 to 2013

The operating capacity indicator is used to measure the turnover rate of assets, and aims to explain the extent to which the company can use assets intensively and effectively to obtain income. By analyzing the inventory turnover rate and asset turnover rate of Geely Automobile before and after the acquisition, we can judge the impact of the acquisition of Volvo on Geely's operating capacity. There was little difference in the inventory turnover rate of Geely in 2009 and 2010. The reason reflected in the financial report is that the change range of inventory and sales cost is almost the same, it shows that Geely has maintained a good inventory turnover capacity before the acquisition. The inventory turnover rate of Volvo and Geely continued to rise in 2012, indicating that the inventory turnover rate of Geely continued to decline significantly after the acquisition of Geely in 2011. By 2013, the inventory turnover rate began to pick up, indicating that Geely began

to adopt positive sales strategies to improve sales. Further research on the financial reports of 2014 and 2015 shows that its inventory turnover rate continues to rise, indicating that the acquisition of Volvo has affected Geely's operating capacity in the short term, but it is not difficult to find from its long-term financial indicators that the acquisition has a certain effect on Geely's brand image^[4].

Similarly, the asset turnover rate in 2011 and 2012 decreased compared with that in 2010, and the growth rate of sales (turnover) in these two years was much lower than that in 2010, which shows that after Geely acquired Volvo, its efficiency of using assets for profit decreased, affecting its profitability. In 2013, its turnover began to pick up, indicating that its ability to use assets for profit has been restored.

4.2 Profitability analysis of Geely Automobile from 2009 to 2013

Profit is the ultimate goal of an enterprise. Whether an enterprise can make profits will have an extremely important impact on the development of the company. The profit index is the most intuitive embodiment of the company's profitability. In terms of profitability, Geely's profitability declined after the acquisition, but with the dust of the acquisition settled, Geely's profitability began to rise. In the long run, Geely's acquisition of Volvo will have a positive effect on its future development^[5]. During the transition period of Geely's acquisition of Volvo, i.e., 2010 and 2011, the acquisition had a negative impact on Geely's relevant financial indicators, such as the slowdown of net profit and sales growth. After 2011, Geely's financial data gradually improved. With the smooth progress of the acquisition and the change of the company's strategy, the acquisition of Volvo promoted Geely's own brand effect and the progress of related technologies, and further promoted the development of the company^[6].

From 1999 to 2007, Volvo's global sales volume was more than 400000, reaching a peak of 458000 in 2007. In 2008 and 2009, the sales volume has decreased to 374000 and 335000 respectively. In 2005, Volvo car company made a profit of about US \$300 million, but the company suffered losses in the following three years. In 2008, due to the spread of the international financial crisis, Volvo car suffered a huge loss of US \$1.5 billion, and its sales volume decreased by more than 20% compared with 2007.

4.3 Details of financing channels selected by Geely Group:

Geely Group mainly chooses debt financing, but why not choose the priority theory of "internal financing" before "external financing". Geely has its own reasons: Although internal equity financing has the advantages of relatively low cost, low risk and independent and flexible use, it is sometimes difficult to implement, such as issuing shares; Equity financing is easy to reduce the efficiency of capital use; The new equity financing will dilute the operating performance of the enterprise, reduce the earnings per share and damage the interests of investors; In addition, with the continuous improvement of China's capital market system, the threshold of enterprise equity refinancing will be raised and the refinancing cost will increase. According to the balance sheet, Geely's asset liability ratios in 2007, 2008 and 2009 were 44%, 19.7% and 52% respectively, indicating that Geely Group's asset liability ratio is low and there is still a lot of room for debt financing, so as to make full use of financial leverage. In addition, Geely's daring to borrow comes from its confidence in its own production capacity and more accurate market forecast: through detailed cost calculation, it is accurately predicted that Volvo can turn around its losses by selling 350000 vehicles. Geely believes that the strong development momentum can ensure the repayment of the above debts, and the brand effect of Volvo will also enable Geely to develop in the high-end car market^[7].

It can be seen from Geely's specific financing that debt financing accounts for a large proportion.

First, the asset liability ratio has increased, which has greatly improved the financial leverage had positive effects on the initial acquisition, Geely's share price will soar further. Secondly, Geely's corporate valuation will also rise. In the next round of financing negotiations or selling enterprises, it will be in a very favourable position. Thirdly, Geely's financial risks will surge. After financing, the asset liability ratio reached 69%, which has exceeded the international warning debt ratio of 65%. Therefore, Volvo turned loss into profit in 2011. If Volvo's cash flow still cannot "feedback" Geely in the next three years, Geely will face great debt repayment pressure. In view of the development of Volvo, Geely put forward the concept of "reducing scale cost": (Volvo) forms a large number of intellectual property rights and a large number of technologies. Due to its relatively small scale, the cost of each car is relatively good, so it loses money. Therefore, Geely should find ways to give full play to these technologies and expand the sales of these products. Only when the scale is expanded, the cost of each car will fall and profits will appear.

According to the third quarterly report of Geely holdings in 2017, as of the end of September last year, Geely holdings had a total revenue of 192.148 billion yuan and a net profit of 12.318 billion yuan, exceeding the net profit of 11.617 billion yuan in 2016; According to the corporate bond rating report of Geely holdings, in 2016, the operating revenue of Geely holdings group was 208.799 billion yuan and the gross profit was 45.852 billion yuan, a year-on-year increase of 26.31%. Among them, the revenue from Volvo vehicle series products is 140.26-billion-yuan, accounting for 67.18%; Geely vehicle series contributed 30.138 billion yuan of revenue, accounting for 27.05%. According to the announcement of Geely Automobile listed in Hong Kong, a total of 1247100 Geely series vehicle products were sold in 2017, a year-on-year increase of 63%. According to the global sales statistics issued on the official website of Volvo Group, Volvo sold 114400 vehicles in China last year, a year-on-year increase of 25.8%.

According to the rating report, the strategic coordination between Geely Automobile and Volvo in parts procurement has been gradually strengthened. Since November 2013, Geely and Volvo had started joint procurement to reduce costs. In recent years, Volvo has increased the number of parts purchased in China. For example, some auto parts required by Volvo's manufacturing plant in Chengdu, China are purchased directly from China, and the auto parts purchased by its European plant from China have also increased significantly. In addition, Geely also directly transferred its Chengdu plant to Volvo cars as the land for its vehicle manufacturing base in China, which ensured that the construction of Volvo Chengdu plant could start in July 2011.

4.4 Potential problems in Geely's financial integration

In order to successfully acquire Geely, we must raise enough funds. Geely Group itself only contributes a small part, and most of the acquisition funds come from various external financing channels. There are three main financing channels: first, domestic bank loans; 2, Low interest bank loans guaranteed by local government agencies in Sweden mainly come from Europe, America and other places; 3, Raise funds through equity. Most of Geely's funds come from abroad. Without the support of relevant governments, it is difficult to successfully finance. Faced with such a huge financing loan problem, Geely Group has a huge financial risk. The repayment of interest alone will make Geely face a huge debt repayment risk every year. Before Volvo was acquired, Volvo's global sales continued to decline, and the company was facing huge capital losses. Therefore, after the acquisition of Volvo, Geely must bear the huge debt accumulated by the company. Therefore, before the recovery of the company's business at the initial stage of M&A, a huge amount of funds must be invested. After M&A, the company is faced with huge changes in the company's financial structure, huge pressure on debt repayment interest, operating costs and later capital investment. Therefore, if the capital chain breaks, the company will face great financial payment difficulties.

4.5 Financial performance analysis after Geely's acquisition of Volvo

By analyzing the financial indicators before and after M&A, we can analyze and evaluate the performance after M&A integration. Geely completed the M&A of Volvo in 2010, so it selected the operation and management situation before and after the M&A for comparative analysis to evaluate the financial performance after the M&A. The following analysis takes 2008-2012 as the analysis interval to analyze the financial performance. Profitability is the ability of enterprises to obtain profits, that is, the appreciation ability of capital. There are usually many indicators to examine profitability. Here we mainly analyze the net profit rate and return on total assets, and then analyze the performance of Geely's acquisition of Volvo. In terms of market share the auto sales volume showed a rising trend after Geely's acquisition of Volvo, and its market share increased continuously, especially the auto export volume increased significantly. In 2010, the export volume was 415800 vehicles, with a year-on-year increase of 6.22%. In 2011, that is, the first year after M&A, the automobile export volume was 421600 vehicles, with a year-on-year increase of 93.17% and a year-on-year increase of 157.32% in 2012, reaching the peak of the growth rate of exported automobiles in recent years.

Geely's sales volume also increased year by year, reaching 415800 in 2010 and 483400 in 2012, with a year-on-year increase of 14.66% in 2012. After the merger, the output and sales volume increased compared with the previous ones, the most prominent being the surge in export volume. After the merger and acquisition, Geely has strengthened its export and continuously expanded its share in the foreign automobile market. It is Volvo's brand image that has greatly promoted Geely's entry into foreign markets and improved brand awareness and brand image. Moreover, Geely's acquisition of Volvo also expanded Geely's domestic market. In 2008, Geely's domestic market share was only 2.54%. After M&A in 2010, the market share increased to 3.8% compared with that in 2012 and more than 4.8% after 2013. It can be seen that Geely's M&A has expanded its domestic and foreign markets.

5. Conclusion

Geely acquired advanced core technology from Volvo. Volvo not only has considerable brand value, but also grasps the two biggest trends in the future of the automotive industry which are safety and new energy. Drawing on high-end talents, Geely Automotive has always given people the impression of grassroots solidarity in terms of price and appearance. To change this image, Geely must have excellent industrial design talents and brand planning talents. Learn the marketing model of the system. Volvo closely connects its brand with "gentleman spirit, challenging limits and noble life" through sports marketing and high-cost marketing, and locks in the user group who pursues quality of life, pays attention to safety and environment. Being able to learn the marketing strategy of foreign brands closely is a prerequisite for Geely and Chinese auto enterprises with independent brands to go to the world in the future.

Through the changes of Geely's total assets and total shareholders' equity, it can be seen that Geely is obviously in the expansion period and developing rapidly. Due to the lack of average data of domestic automobile industry, Dongfeng Motor is selected for comparison. Take the data of 2009 as an example: the current ratio and quick ratio of Dongfeng Motor are 1.19 and 1.02 respectively, and that of Geely Automobile Holding Group are 1.37 and 1.30 respectively, which are higher than the former. It can be inferred that its short-term solvency is strong. In terms of profitability, Geely's pre-tax profit margin is 12.83%, Dongfeng Motor is 7.92%, and Geely's profitability is strong. In terms of inventory turnover, Geely is 11.18% and Dongfeng is 5.81, indicating that Geely has less inventory backlog and strong sales and inventory management ability

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