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Perspective on Mergers and Acquisitions: Exploring Financial Management Issues and Forward-looking Management Strategies

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Abstract: This article focuses on financial management issues in mergers and acquisitions (M&A). It provides an in-depth analysis of the financial risks and management challenges faced by contemporary businesses during various stages of M&A, such as pre-merger valuation pricing difficulties, unreasonable financing structures, risks in payment method selection, obstacles to financial integration, and lack of risk management. Targeted management strategies are proposed to address these issues. This paper suggests strengthening due diligence and valuation management, optimizing financing structures, rationally selecting payment methods, deepening financial integration, and improving tax planning. These strategies aim to enhance the level of financial management in M&A, promote economic synergies and management effects, help companies quickly achieve M&A goals, and drive sustainable business development.

Keywords: Mergers and acquisitions; Financial management; Management strategies; Financial risks; Synergies

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1. Introduction

In the context of economic globalization and increasingly fierce market competition, companies often choose mergers and acquisitions (M&A) to integrate resources and expand their market presence to achieve rapid expansion and breakthroughs in a complex and changing business environment, thereby enhancing their core competitiveness [1]. M&A has become a crucial strategic tool for businesses. Financial management, as the core component of M&A activities, permeates every stage of the process, from valuation of the target company and financing planning before the merger to the choice of payment methods and tax planning during the merger and, finally, to financial integration and risk monitoring after the merger. Decisions made at each stage directly impact the success or failure of the M&A [2]. Therefore, a deep analysis of financial management issues in corporate M&A, coupled with the development of scientific and effective management strategies, not only helps to optimize resource allocation, reduce financial risks, and increase the success rate of M&A, but also has significant practical implications for the long-term development and sustainable operation of businesses.

2. Overview of relevant theories on corporate mergers and acquisitions

2.1. Forms of corporate mergers and acquisitions

Classification based on industry relationship: Corporate mergers and acquisitions can be divided into horizontal M&A, vertical M&A, and conglomerate M&A. Among them, horizontal M&A refers to mergers and acquisitions between enterprises that produce or operate similar products within the same industry, aiming to enhance market competitiveness through "strong alliances." Vertical M&A involves enterprises at different stages of production and operation, with forward M&A expanding downstream and backward M&A extending upstream. Conglomerate M&A, on the other hand, involves parties from different industries, aiming to diversify risks through diversified operations [3].

Classification based on payment methods: Corporate mergers and acquisitions can be categorized into cash M&A, equity M&A, and mixed M&A. Cash M&A refers to the acquisition of target company shares or assets by paying cash. Equity M&A involves the issuance of shares to acquire the equity of the target company, avoiding large cash outflows. Mixed M&A, on the other hand, utilizes a combination of cash, equity, bonds, and other payment methods, flexibly adjusting the payment ratio to balance funding pressure and equity dilution risk. Additionally, it can expand funding sources through bond financing to meet different M&A needs.

Classification based on M&A attitude: Corporate mergers and acquisitions can be divided into friendly M&A and hostile M&A. Friendly M&A is achieved through friendly negotiation and consensus, with the M&A process proceeding according to mutually agreed-upon conditions and procedures. Hostile M&A, also known as a malicious takeover, involves making a takeover offer directly to shareholders without negotiating with the target company's management. It is often accompanied by anti-takeover measures from the target company, such as poison pills or white knight strategies. The M&A process is often full of twists and turns and may even lead to legal disputes.

2.2. Basic process of corporate mergers and acquisitions

In the early stage of corporate mergers and acquisitions, companies need to clarify their M&A strategy, goals and assemble a professional M&A team consisting of internal executives, financial and legal personnel, as well as external investment banks, accounting firms, law firms, and other relevant personnel. Simultaneously, market research should be conducted to screen potential target companies, followed by due diligence covering various aspects such as finance and legal issues [4]. Afterwards, valuation methods like discounted cash flow should be employed to assess the value of the target company, determine a reasonable acquisition price range, and provide a reference for subsequent negotiations.

In the mid-stage of corporate mergers and acquisitions: Based on the results of due diligence and valuation, companies develop negotiation strategies, clarify key terms such as acquisition price, payment methods, and equity structure, and conduct multiple rounds of negotiations with the target company. After reaching an agreement, an M&A agreement is signed, stipulating transaction terms, delivery conditions, transitional arrangements, etc.

In the later stage of corporate mergers and acquisitions, following the signing of the M&A agreement, the company submits the M&A plan to the board of directors and shareholders' meeting for review and approval according to internal decision-making procedures, ensuring alignment with the overall interests and development strategy of the company. If external procedures such as anti-monopoly review and industry regulatory approval are involved, an application needs to be submitted to the government authorities for approval. Meanwhile, a financing plan is developed based on the payment method and funding requirements, raising funds through internal fund allocation, bank loans, bond issuance, equity financing, and other means [5]. Finally, in the later stage of corporate mergers and acquisitions, asset delivery and debt undertaking are completed according to the M&A agreement, assets of the target company are inventoried and evaluated, and debts are sorted and integrated. Both parties' businesses are integrated, processes are optimized, and resource sharing and synergistic effects are achieved. The organizational structure is adjusted based on the company's strategic planning and business needs, responsibilities and authorities are clarified, personnel are reasonably arranged, and operational efficiency is improved. Emphasis is placed on corporate culture integration, conflicts are resolved through communication and training, staff placement and incentives are implemented, the staff team is stabilized, and sustainable development of the company is ensured.

2.3. Synergistic effects of corporate mergers and acquisitions

One of the core motivations of corporate mergers and acquisitions is to achieve synergistic effects, which mainly cover three key aspects: Operating synergy, financial synergy, and management synergy. Taking *Midea Group*'s acquisition of *Little Swan* as an example, the explanation is as follows.

Operating synergy: After corporate mergers and acquisitions, economies of scale can be achieved by expanding production scale [6]. After *Midea*'s acquisition of *Little Swan*, the operating synergy effect was significant. In terms of manufacturing, production resources were integrated, the production line layout was optimized, economies of scale were achieved, and unit production costs were reduced. Simultaneously, utilizing *Midea*'s extensive sales channels, the market coverage of *Little Swan* products was further expanded, increasing sales. In the research and development phase, technical teams from both sides exchanged and cooperated, accelerating the development speed of new products and launching more innovative products that meet consumer demands.

Financial synergy: Through mergers and acquisitions, companies can allocate funds reasonably. Relying on its strong financial strength and financing capabilities, *Midea* improved *Little Swan*'s financial status and reduced its financing costs. By reasonably allocating funds, it improved fund usage efficiency and provided strong financial support for business expansion on both sides.

Management synergy: When a company with a higher management level acquires a company with relatively weak management, excellent management experience can be disseminated and shared [7]. *Midea* introduced mature and advanced management experience and operating models into *Little Swan*, optimizing its internal management processes, improving management efficiency, making various aspects of *Little Swan*'s business operations more standardized and efficient, and significantly improving its overall operational level.

3. Common financial management issues in contemporary corporate mergers and acquisitions

3.1. Valuation and pricing challenges before mergers and acquisitions

Due to information asymmetry, it is difficult for the acquirer to fully understand the true financial status and potential risks of the target company, leading to valuation deviations [8]. The target company may mislead the acquirer by concealing debts, inflating assets, or other means, increasing the risk of mergers and acquisitions. Additionally, improper selection of valuation methods, such as the price-earnings ratio method being greatly affected by industry fluctuations or the discounted cash flow method relying on inaccurate predictions, can all lead to valuation deviations.

3.2. Dilemma of unreasonable financing structure

Corporate mergers and acquisitions often require significant financial support, and the choice of financing channels and financing structure directly affects the success or failure of mergers and acquisitions and financial stability [9]. Over-reliance on debt financing can increase the asset-liability ratio, leading to financial risks, while over-reliance on equity financing can dilute the control of original shareholders, causing conflicts of interest and affecting the stable operation of the company. Furthermore, improper timing of financing, such as conducting debt financing when market interest rates are high, can also increase financing costs.

3.3. Risks of payment method selection

Although cash payment is simple and direct, it can increase financial pressure and affect liquidity. Equity payment, while avoiding cash outflow, can dilute equity, weaken the voice and decision-making power of original shareholders, and may even lead to battles for control. Mixed payment, while combining the advantages of cash and equity payments, can expose the drawbacks of both if the proportion of cash to equity is not properly balanced, increasing the risk of mergers and acquisitions [10].

3.4. Obstacles to financial integration

Financial integration after mergers and acquisitions is a key link to achieving synergistic effects involving various aspects such as accounting systems, financial management systems, and fund management. Inconsistent accounting policies and estimation methods among different companies may lead to a lack of comparability in financial data, affecting the financial analysis and decision-making of the company. In terms of fund management, if funds cannot be effectively integrated, problems such as fund dispersion and inefficient use may arise.

Corporate mergers and acquisitions involve complex tax issues, and reasonable tax planning can reduce merger and acquisition costs and improve merger and acquisition benefits. However, improper tax planning may lead to increased tax burdens or tax disputes [11]. For example, if the tax impact is not fully considered during the transaction structure design phase and a higher tax burden scheme is selected, or if the tax treatment in asset transfers, debt restructuring, and other aspects does not comply with relevant regulations, it may increase the tax risk of companies having to pay additional taxes, late fees, or even heavy fines.

3.5. Lack of risk management

There are various risks in the process of mergers and acquisitions, such as market risk, credit risk, and operational risk. If companies underestimate risks before mergers and acquisitions and lack effective risk management measures, it may lead to risk events and bring huge losses to the company.

4. Management strategies for financial management in contemporary corporate mergers and acquisitions

4.1. Strengthening due diligence and valuation management before mergers and acquisitions

To achieve accurate valuation and pricing, enterprises need to collect target enterprise information from all directions and channels [12]. In addition to consulting regular materials such as financial statements and audit reports, it is also necessary to deeply investigate the business operation details, market reputation and upstream and downstream partnerships of the target enterprise. You can communicate with the suppliers and customers of the target enterprise to understand its real operating conditions and latent risks. In the process of mergers and acquisitions, to ensure that the value evaluation of the target enterprise is scientific and reasonable, the comprehensive application of multiple value evaluation methods can effectively reduce the limitations of using a single method. At the same time, it is necessary to have a comprehensive and in-depth understanding of the financial status, operating results, and asset quality of the target enterprise. Carefully review the authenticity and accuracy of financial statements, verify the ownership of assets, investigate potential liabilities, and avoid falling into the trap of value assessment. In the financing process, it is crucial to reasonably determine the scale of financing. Taking into account factors such as merger price and integration cost, accurately estimate the required financing amount to prevent excessive financing from increasing costs or insufficient financing leading to merger failure. In addition, it is also necessary to optimize the financing structure, and consider the ratio of debt financing to equity financing in combination with the company's own financial situation and market environment.

4.2. Optimizing the financing structure of enterprises

Enterprises should formulate scientific and reasonable financing plans according to their own financial situation, business objectives, and risk tolerance. Enterprises can broaden financing channels, rationally arrange financing structures, and reduce financing costs and risks [13]. On the other hand, the rational use of the tax shield effect of debt financing can reduce financing costs, but to avoid an excessive asset-liability ratio, a reasonable debt ceiling needs to be set to ensure that enterprises still have sufficient solvency in the face of operating fluctuations. On the other hand, it is necessary to use equity financing cautiously and fully evaluate the impact of equity dilution on existing shareholders' equity and corporate control. Diversified financing channels can be tried. In addition to bank loans and the issuance of stocks and bonds, strategic investors can also be considered. While obtaining funds, they can use their industry resources and management experience to help enterprises develop.

4.3. Reasonable choice of payment methods

When choosing M&A payment methods, enterprises should fully consider their own capital status, equity structure, and M&A goals. Cash payments are a good option if the company is well-funded and wants to maintain stable control, but ensure that it does not put too much pressure on subsequent operations. Equity payments can relieve capital pressure if the company's cash flow is tight and the acceptance of equity dilution is high. However, for most M&A transactions, hybrid payment methods are more flexible. Companies can flexibly adjust the proportion of payment instruments such as cash, equity and bonds according to the negotiation results and actual needs of the two parties to the acquisition.

To achieve accurate valuation pricing, companies need to collect comprehensive information about the target company through multiple channels. Besides reviewing financial statements, audit reports, and other routine materials, in-depth investigations into the target company's business operations, market reputation, and upstream and downstream partnerships are also required. Communications with the target company's suppliers and customers can provide insights into its true operating conditions and potential risks.

4.4. Deepening financial integration after mergers and acquisitions

After the completion of mergers and acquisitions, it is crucial to quickly unify the accounting system [14]. Firstly, a unified financial strategy and system should be established, and communication and integration between financial personnel should be actively promoted to enable both teams to work together. At the same time, clear and unified accounting policies and estimation methods should be established to ensure the consistency and comparability of financial data, laying a solid foundation for financial analysis and decision-making. In terms of fund management, a centralized fund management platform should be established, and the financial information system should be integrated to achieve real-time sharing of financial data. This allows corporate management to effectively monitor the capital situation and fully leverage financial synergies. Regarding financial system integration, the financial accounting system, approval process, and financial reporting system of both parties in the merger and acquisition should be unified to provide a unified standard for financial management and ensure the accuracy and consistency of financial information. Additionally, companies need to establish a financial risk monitoring mechanism, set warning lines for key financial indicators such as asset-liability ratio, current ratio, and net profit growth rate, and pay close attention to the company's financial situation in real-time. Once potential risks are identified, early warning signals should be issued promptly. Furthermore, continuous evaluation of M&A performance is essential. Regular financial performance evaluations should be conducted on the merged company, and the results should be compared with the expected goals before the merger to identify deviations and adjust business strategies and financial management measures promptly to achieve the expected value of the merger.

4.5. Improving tax planning

Before the merger, the company should establish a professional tax team to study national and local tax policies, especially preferential policies and special provisions related to mergers and acquisitions [15]. When designing the transaction structure for mergers and acquisitions, the tax impact of different options should be fully considered, and the option with the lightest tax burden should be selected [16]. For example, by utilizing special tax treatment provisions, reasonable arrangements can be made for the transfer of assets and equity, deferring tax payment time and reducing the tax burden during the current period of the merger. In the integration process after the merger, continuous attention should be paid to changes in tax policies, and tax planning schemes should be adjusted promptly to ensure compliance with tax treatments and avoid tax risks.

The financial management issues in corporate mergers and acquisitions are complex and diverse, spanning various stages of the merger and acquisition process. Companies need to fully understand the importance of these issues, adopt effective management strategies, strengthen financial management in all links, reduce financial risks, achieve the expected goals of mergers and acquisitions, and enhance the comprehensive competitiveness and sustainable development capabilities of enterprises. In practice, companies should continuously adjust and improve their financial management strategies based on their own characteristics and market environment to adapt to the changing merger and acquisition environment.

Disclosure statement

The author declares no conflict of interest.

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