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## Study on the Economic Consequences of Shareholders' Equity Pledge Behavior

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### Abstract

Compared with bank loans, private lending, pawn, borrowing and other financing methods, shareholders' equity pledge is faster, and the cost of borrowing costs is lower. According to this characteristic, this paper is divided into three parts. First, the literature of domestic and foreign equity pledge is sorted out, and the motivation of equity pledge is analyzed again, divided into malicious pledge and goodwill pledge, and finally analyzed the economic consequences of equity pledge. It provides a theoretical basis for minority shareholders to prevent major shareholders from encroachment on their interests.

**Keywords:** Shareholder pledge, economic consequences, motive

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### 1. Introduction

In recent years, the stock market has set off a surge of the controlling shareholder equity pledge, along with the emergence of this phenomenon, has been widely concerned by the academic circles. Equity pledge is a kind of financing behavior whereby shareholders use their shares in listed companies as the target of the pledge to apply for loans from financial institutions or provide guarantee for third-party loans. In short, it is a means for company shareholders to use their equity to obtain funds from banks, securities companies and other institutions. For the controlling shareholders of listed companies, why will take the way of equity pledge to obtain funds? As long as equity has a fast approval process, shareholders can obtain the required funds in a short time, and the use of funds is not restricted, and the control and voting rights of equity pledged shareholders are not affected in any way. For loan companies, the equity of shareholders has strong liquidity in the secondary market, and the company's information disclosure is relatively complete and its supervision, so the way of equity pledge is favored by both parties. But any transaction is double-edged. In recent years, when the stock price "crash" continued to occur, the capital market began to evaluate the risk index of equity pledge, and the results showed that equity pledge has still become one of the important reasons for the stock price "crash".

In view of the behavior of shareholders' equity pledge, the existing literature analyzes and demonstrates it from different perspectives and directions, and finally obtains two analytical perspectives: — agent cost and control transfer risk. From the perspective of agency cost, the behavior of controlling equity damages the interests of minority shareholders, and then affects the interests of the whole company. The risk of control transfer believes that the equity pledge of major shareholders will seriously affect the normal business activities of the company and change the actual controlling shareholder of the company. But in the relevant research analysis ignores the influence of its own factors and external macro factors on the research conclusion. therefore. This paper first reviews the literature related to equity pledge, and then constantly explores the motivation of shareholders (malicious motive, goodwill motive) on the basis of relevant research literature of equity pledge behavior, and then analyzes the research on economic consequences.

### 2. Objectives

This study aims to: This paper sorts out the research context of equity pledge and points out its future research direction in order to provide theoretical and empirical reference for further standardizing equity pledge behavior.

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### 3. Methodology

This paper is Theoretical analysis, this study will refer to a large number of domestic and foreign theoretical literature on equity pledge and economic consequences of major shareholders, and further extend and discuss on this basis, in order to use a more complete theory for research. It shows that the pledge behavior of major shareholders affects the value of enterprises through various aspects.

### 4. Review of Equity Pledge Literature

#### 1. International research on equity pledge

As early as 2012, international scholars have noticed the purpose of shareholder equity pledge. After this, a large number of studies on this behavior were started. Three conclusions were finally drawn.

The behavior of shareholder equity pledge of the company is not conducive to the long-term development of the company. Research results show that the major shareholders through equity pledge to obtain certain money, but at the same time damaged the interests of the minority shareholders, external shareholders, share prices fell, loan companies to pledge shareholders further margin, not only increase the management risk of the company, but also may affect the shareholders 'own cash flow, even shareholders give up holding the company's shares, exacerbated the risk of price crash .Moreover, the higher the pledge ratio, the higher the risk of the company's stock price collapse, so it is believed that the company shareholders' equity pledge behavior is not conducive to the long-term development of the company.

The behavior of shareholder equity pledge of the company is not conducive to the long-term development of the company. Huang (2016) <sup>[2]</sup> and wang (2018) <sup>[13]</sup> derive from normative and empirical research and analysis that major shareholders, on the one hand, can obtain their required capital flow through equity pledge and relieve the capital pressure. On the other hand, by providing funds for shareholders, it is necessary to supervise the operating conditions of the listed company at all times. At the same time, shareholders will also supervise the efforts of the company managers and increase double-sided supervision, which is conducive to the company's operating efficiency, improve economic profits and enhance the value of the enterprise.

Company shareholders equity pledge behavior of the company's long-term development, shareholders to equity pledge this behavior is belong to shareholders' personal behavior, equity pledge just the power of the shareholders as collateral to obtain shareholders use funds, does not involve the overall management of the company, will not affect the company's shareholding structure, at the same time to the macro economic environment cannot play a stimulating role.

#### 2. Domestic research on equity pledge

Domestic research is different from the international research methods on equity pledge, mainly through the motivation, influencing factors and economic consequences of equity pledge. Most scholars consider the behavior of equity pledge from the perspective of economic consequences as having a negative impact. Shareholders 'pledge equity affects the company's innovation ability and surplus management level, and the higher the pledge ratio, the greater the impact on the company's value is. Xia Ting (2018) <sup>[5]</sup> and other scholars used the empirical research and analysis of the enterprise value of the pledge scale, which shows that the lower the pledge ratio, the stock price of enterprises increases. The

higher the pledge ratio, the lower the share price.

### 5. Discussion

#### 1. Good motive

The behavior of equity pledge is essentially a kind of financing behavior, in which the major shareholders or the company take the equity as collateral to obtain the funds needed by the company and the shareholders, which in a sense, expands the financing method of the enterprise. Through the form of equity pledge, shareholders can convert their "power" into usable funds, solve the financial difficulties of major shareholders, help shareholders out of the crisis and difficulties, and then better supervise and manage the company's business. Xu Shoufu (2016) <sup>[7]</sup> analyzes from the perspective of credit market that major shareholders obtain flexible funds through equity pledge to solve the current financial difficulties of individuals or enterprises, and to solve the problem of capital chain. Although the shareholders' equity is pledged, the shareholders themselves still did not lose the control and voting rights of the company. It is precisely because the shareholders obtain the short-term available funds while not losing their equity status, so the behavior of equity pledge has been welcomed by the controlling shareholders in the stock market.

#### 2. Malicious motive

In the guarantee law regulation, which defines the right of pledge, "the pledgee has the right to collect the fruits of the pledge". That is to say, when the major shareholders pledge their equity, the third-party financial company has the right to collect the company's profits, dividends and other profits during the pledge period. In a sense, although the shareholders have not lost the control right and decision-making power of the listed company. However, the shortage leads to the loss of cash flow of shareholders, which increases the number of shareholders to damage the rights and interests of minority shareholders through "tunnel mining" and encroach on their interests of .When shareholders, on the other hand, equity pledge behavior, in a sense, also illustrates the listed company management or shareholders have financial risk, the company's internal management problems, just solve the problem of capital flow by pledge, can only solve the temporary capital difficulties, cannot essentially solve the problem of the company's operation. This also conveys a negative message to shareholders, increases the motivation of major shareholders to occupy minority shareholders, and reduces their own losses to the minimum by infringing on minority shareholders.

### 6. Results

Enterprise value. Different scholars have different conclusions on the influence on enterprise value. Through the transfer of control risk, the equity pledge of major shareholders causes the inner panic of minority shareholders, disrupts the normal operation of the company, and is not conducive to the stability of the stock price of the listed company, thus reducing the value of the enterprise. Mr (2014) shared the same view, arguing that major shareholders flee existing capital markets by acquiring capital flows. Foreign scholar Andersona Puleoa holds the opposite view, believing that the equity pledge behavior is conducive to the promotion of the company's value. It can effectively alleviate the conflict between shareholders and enhance the value of

enterprises. other scholars believe that equity pledge does not necessarily promote the shareholders' hollowing out, in private enterprises, shareholders of listed companies in the face of company operating difficulties, will not hesitate through equity pledge, obtain temporary flow to reduce the financial risk of the enterprise, efforts to improve the management of the enterprise, improve the enterprise's stock price, enhance the value of the enterprise. Therefore, the behavior of shareholders' equity pledge can supervise and promote the operation of enterprises. transfer of control. The behavior of equity pledge is only to temporarily keep the equity to the pledgee in the form of mortgage, and the ownership and control remain unchanged, why is the transfer of control? Unlike real estate, the stock price fluctuates greatly, and the risk borne by the pledgee is higher. In order to reduce such a risk, the early warning line of the stock price is established to bear the pressure of the stock decline. If the price of stocks in the capital market is lower than the early warning line of the stock price, the pledgee has the right to ask the pledgee to increase the pledge and increase the stock equity in equal proportion. If all the shares in the hands of the shareholders have been pledged as collateral. Financial companies are likely to sell their shares to get liquidity to reduce their risk. The shareholders have lost this part of the stock, indirectly leading to the transfer of control of the company, the actual controller of the company has changed. In order to firmly grasp the shares in their hand, the pledged shareholders usually carry out a series of operations to stabilize the company's share price. And through the listed companies earnings management and information disclosure means of the majority. The controlling shareholder better "hides the real surplus" through the surplus management in the statement. Xie Deren (2016)<sup>[11]</sup> further refined the surplus management, that is, increase the development expenditure of the intangible assets of the enterprise, and try to include the development expenditure into the intangible assets, indirectly change the annual profit of the enterprise, and change the real surplus management of the enterprise. Through the information disclosure of listed companies, actively shows the capital market the news conducive to the development of enterprises, uses information asymmetry to stabilize the stock price of listed companies, and even improves the company's stock price through information disclosure. While Wang Xiongyuan (2018)<sup>[13]</sup> uses the perspective of tax revenue, tax avoidance reduces the outflow of enterprise funds, and uses more funds to develop enterprises. Therefore, through this perspective can also improve the performance and value of enterprises.

### Conclusion

In a word, as shareholders' equity pledge can increase the capital flow of the company or shareholders, equity pledge has attracted wide attention from scholars at home and abroad. Studying equity pledge from multiple perspectives, different research conclusions are drawn. This paper first sorts out the literature of equity pledge, which can find that

equity pledge has attracted the attention of more and more scholars. Subsequently, the motive of equity pledge was divided into malicious pledge and good faith pledge, which concluded that equity pledge could provide sufficient cash flow for the company and shareholders, and solve the current possible financial problems and financial difficulties. Finally, the economic consequences of the equity pledge are discussed, and undoubtedly the equity pledge has brought positive or negative effects on the enterprise value and the transfer of control right. Although there are many studies on equity pledge, there are still great deficiencies. That is, most research on the behavior of equity pledge is limited to the internal impact on the enterprise, while there are few studies on the external capital market and external stakeholders. At the same time, the capital flow obtained by shareholders through the pledge is used for enterprise operation or to solve the financial crisis of shareholders themselves.

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