The Economic Consequences of The Sale of Intco Medical's Major Shareholders

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Abstract. Since the implementation of the reform of non-tradable shares, the scale of major shareholders' reduction has been continuously expanding. The emergence of the COVID-19 pandemic in 2020 has exacerbated the problem. Taking Intco Medical Company as an example, this paper reviews the whole process of the holding reduction event from the actual situation of its controlling major shareholder through the event study method, analyzes the economic consequences brought by the major shareholder's holding reduction, and puts forward the corresponding management method suggestions as understood by the author, in order to provide theoretical support for the relevant personnel to carry out research in the later stage.

Keywords: Shareholders' reduction; Economic consequences; Event study.

1. Introduction

After the implementation of the reform system of non-tradable shares in the Chinese market, the profit method of the major shareholders of listed companies has been changed. The majority shareholders used to make profits from the development of the company and now they make profits from the stock market. China's securities market is still developing gradually, and relevant laws and regulations are becoming more and more perfect. There is information asymmetry in the market, which is reflected in the internal and external public of the company. For example, when the company is not operating well, large shareholders will know the relevant information in advance of the external public, and some shareholders may choose to sell their shares quickly to obtain benefits and reduce losses [1]. The reduction behavior of major shareholders is one of the unfavorable factors affecting the smooth operation of China's stock market, and also brings negative effects to the management of listed companies. We choose Intco Medical as a case company to study the behavior of its controlling shareholder's reduction.

2. The overview of the Intco Medical major shareholder reduction

2.1. Company profile

The Intco Medical is a manufacturer committed to the research and development, production and marketing of medical device consumables, the vast majority of its operating income from personal protection products, mainly disposable PVC gloves and nitrile gloves, the global demand for disposable gloves during the epidemic surge, Inke Medical's share price is also rising. In the first half of 2020, the operating income and net profit of Intco Medical showed a leap growth, the operating income increased from 558 million yuan at the end of 2019 to 3.673 billion yuan, an increase of nearly 7 times, and the net profit increased by more than 30 times.

2.2. Major shareholder reduction process

Intco Medical issued an announcement on June 1, 2021, to pre-disclose the shareholding reduction plan of major shareholder Liu Fangyi. According to the announcement, Liu Fangyi plans to reduce his stake of no more than 6% of the company's total shares in the next six months. According to the subsequent announcement of equity change disclosure, Liu Fangyi's trading activities took place from July to November. The termination of the reduction plan was announced in the announcement on...
December 7, 2021, after Liu Fangyi reduced his shares by a total of 3.44% of the total number of shares in the company, obtaining an income of 1.354 billion yuan.

3. The economic consequences of the major shareholder’s reduction of Intco Medical

3.1. Market reaction

By using the event study method, the relevant market data in a window period before and after the event can be quantified, which can directly reflect the specific impact of this economic event. In this paper, the short-term market reaction is analyzed, and the econometric model is CAR model.

The announcement of the reduction plan was released on June 1, 2021, and the paper selected June 1 as the event date, the event period was 31 days, that is, 15 days before and 15 days after the announcement, and 31 trading days before the event period to 180 trading days before the event period as the estimated period. The data source is Intco medical stock market and Shenzhen component index market data obtained by Cninfo.

Firstly, the expected returns of the window period are obtained by using the market model method through the data of the estimated period. The correlation coefficients α and β are estimated by substituting the data of the estimated period into the following formula (1):

\[ R_{it} = \alpha_i + \beta_i R_{mt} + \varepsilon_i \]  

R_{it} represents the return rate of company i's stock in period t, R_{mt} refers to the market return rate on day t, α is the intercept, β is the regression coefficient of the stock return rate to the market return index, ε_i is the regression residual term.

Then the coefficient is substituted into formula (2) to calculate the expected rate of return.

\[ E(R_{it}) = \alpha_i + \beta_i R_{mt} \]  

Finally, formula (3) is used to calculate the daily excess rate of return, and the cumulative excess rate of return can be obtained by adding up the values during the window period.

\[ AR_{it} = R_{it} - E(R_{it}) \]  

\[ CAR_i(t_1,t_2) = \sum_{t=t_1}^{t_2} AR_{it} \]  

During the event window period [-15,15], the calculated excess rate of return and cumulative excess rate of return are shown in Table 1 below:

<table>
<thead>
<tr>
<th>t</th>
<th>AR_{it}</th>
<th>CAR_i</th>
<th>t</th>
<th>AR_{it}</th>
<th>CAR_i</th>
</tr>
</thead>
<tbody>
<tr>
<td>-15</td>
<td>-2.92%</td>
<td>-2.92%</td>
<td>0</td>
<td>0.01%</td>
<td>-10.65%</td>
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<tr>
<td>-14</td>
<td>2.20%</td>
<td>-0.72%</td>
<td>1</td>
<td>-19.02%</td>
<td>-29.67%</td>
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<tr>
<td>-13</td>
<td>1.07%</td>
<td>0.35%</td>
<td>2</td>
<td>-6.33%</td>
<td>-36.00%</td>
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<tr>
<td>-12</td>
<td>-2.23%</td>
<td>-1.88%</td>
<td>3</td>
<td>-0.80%</td>
<td>-36.80%</td>
</tr>
<tr>
<td>-11</td>
<td>0.60%</td>
<td>-1.28%</td>
<td>4</td>
<td>-0.71%</td>
<td>-37.51%</td>
</tr>
<tr>
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<td>-5.63%</td>
<td>-6.91%</td>
<td>5</td>
<td>-3.97%</td>
<td>-41.48%</td>
</tr>
<tr>
<td>-9</td>
<td>-0.92%</td>
<td>-7.83%</td>
<td>6</td>
<td>0.22%</td>
<td>-41.26%</td>
</tr>
<tr>
<td>-8</td>
<td>2.41%</td>
<td>-5.42%</td>
<td>7</td>
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<td>-43.62%</td>
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<tr>
<td>-7</td>
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<td>8</td>
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<td>-10.76%</td>
<td>9</td>
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</tr>
<tr>
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<td>10</td>
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<tr>
<td>-4</td>
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<td>11</td>
<td>-0.65%</td>
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<tr>
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<td>12</td>
<td>-0.05%</td>
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<tr>
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<td>-11.52%</td>
<td>13</td>
<td>5.32%</td>
<td>-38.26%</td>
</tr>
<tr>
<td>-1</td>
<td>0.86%</td>
<td>-10.66%</td>
<td>14</td>
<td>-2.75%</td>
<td>-41.01%</td>
</tr>
<tr>
<td>-1</td>
<td>0.86%</td>
<td>-10.66%</td>
<td>15</td>
<td>-3.02%</td>
<td>-44.03%</td>
</tr>
</tbody>
</table>
Before the event date, the excess rate of return of Intco Medical was in a state of uniform fluctuation above and below 0, and the cumulative excess rate of return decreased from 0 to -10%. Since the announcement of the reduction on the day of the event was issued in the evening, the trading had been stopped that day, so the change began to appear from the next day. AR dropped sharply from 0 to -19.2% on the first trading day after the event. Correspondingly, the continuous decline of Intco Medical CAR continued from the day of the incident to the 12th trading day, reaching a minimum of -43.58%. Then it changes to a fluctuating state.

The above changes indicate that the market has a strong negative reaction to the announcement of the reduction of holdings by the major shareholders of Intco Medical. Some investors regard the reduction as an indirect signal that the future performance or development prospects of Inke Medical are worrying, so they follow the behavior of the major shareholders and sell their shares, which has caused a certain impact on the stock price. However, the impact did not last long, mainly concentrated in the first three trading days after the event.

### 3.2. Influence on the interests of minority shareholders

The pre-disclosure announcement of Liu Fangyi, the major shareholder of Intco Medical, once released, triggered a hot discussion in the market. At the same time, the share price of Intco Medical plummeted, after the opening of Intco Medical's share price fell by 20%, according to the data of Choice finance Database, as of the noon close of June 2, Intco Medical fell by the limit, the company's share price closed at 114.12 yuan, the market value of 41.38 billion yuan, compared with the previous day evaporated 10.34 billion yuan. Since then, Intco Medical's stock has also been falling all the way, until the termination of the reduction plan, Intco Medical's share price has fallen to 58.55 yuan/share. Figure 1 below shows the share price movement during the period when the majority shareholders of Incorp Medical sold their holdings. It is obvious that the reduction plan of Liu Fangyi, the major shareholder of Intco Medical, has seriously damaged the interests of the company's minority shareholders.

![Fig. 1 Stock price chart of Intco Medical](image)

### 4. Governance suggestions for major shareholders’ reductions

#### 4.1. Build a stronger legal system

In order to regulate the behavior of major shareholders’ reduction, protect the legitimate rights and interests of minority shareholders, and maintain the stability and fairness of the securities market, it is necessary to establish and improve the legal system of major shareholders' reduction, and clarify and standardize the subject, method, quantity, time, price, information disclosure and other aspects of major shareholders' reduction from the legal level [2].

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4.2. Increase the share of institutional investors in the market

Institutional investors can restrain the problem of major shareholders' reduction, and they usually have strong professional ability and market sensitivity and can timely discover and judge the motivation and impact of major shareholders' reduction [3]. If institutional investors believe that the reduction of major shareholders is based on the company's future development is not optimistic or there are potential risks, then they may choose to follow the reduction or reduce the position, resulting in a decline in the company's stock price, causing losses to major shareholders [4]. In this way, a market restraint mechanism can be formed, so that major shareholders must carefully weigh the advantages and disadvantages when considering reducing their holdings.

4.3. Help minority shareholders improve their awareness of rights protection

Investor rights protection refers to the behavior of minority shareholders seeking compensation or relief to relevant departments or institutions through legal ways and means when they find that their legitimate rights and interests are infringed. Investor rights protection can help minority shareholders safeguard their own interests, punish illegal acts, promote market fairness and justice, and maintain market order.

5. Summary

After the major shareholders of Intco Medical reduced their holdings, they obtained a lot of excess profits, but led to the company in trouble. The plunge in share prices hurt other investors. In order to protect the healthy development of China's securities market, it is necessary to establish more strict restrictions on major shareholders to restrain their impulse to reduce their holdings and cash out. At the same time, it is necessary to strengthen the education of small and medium-sized shareholders and improve their awareness of rights protection, so as to help them protect their rights and interests.

Acknowledgements

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References