The Impact of Equity Division Reform on Investors

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Abstract. For a long time, there are two forms of shares in China's security market, tradable shares and non-tradable shares. The excessive of non-tradable shares has aggravated the market imbalance. In 2005, the State Council approved a pilot reform of listed companies' equity division reform, which is the beginning of the reform. The equity division reform can eliminate some difference of circulation advantage between the two shares in the stock market, so as to make the stock market more internationalized. At the same time, reform can affect the interests of investors and bring benefits to them, so that more people will have confidence in the market and be more willing to participate in the market. In addition, the equity division reform can add more vitality to the listed company, so that the company can form a better operation mechanism and develop prosperously. The reform can also promote the prosperity of the market with a relatively fair mechanism, thus promoting the prosperity and development of the society. This paper will focus on the impact of equity division reform on small and medium-sized investors and institutional investors. By analyzing the benefits and the problems, different situation of investors before and after the reform, the corresponding countermeasures are put forward.

Introduction

The equity division is a legacy of China's planned economy. This system is very unreasonable in which two thirds of the shares are not negotiable. So, solving the equity problem is the first problem of healthy economic development. In 2005, China embarked on a comprehensive reform in order to form a more equitable and efficient investment environment. The significance of the reform is enormous, and its influence comes to investors, market and company, etc. This paper mainly introduces the influence of equity division reform on investors, including small and medium investors and institutional investors. They have a common purpose for profit, but institutional investors have large scale, strong influence and obvious advantages. They can represent the interests of small and medium investors and speak up for them when necessary. At the same time, the reform has greatly enhanced the company's operating efficiency, increased the company's transparency, and enhanced the company's strength, so that the company can provide more benefits for investors, especially small and medium-sized investors. Equity division reform has also brought great vigor and economic benefits the market directly, make the market structure more reasonable, and promote the development of the whole national economy. The more standard system makes the market more and more international, which is conducive to the future development of our market.
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Types of Investors

The normal operation of the securities market cannot be separated from the participation of investors. In the secondary market, investors can be divided into small and medium-sized investors and institutional investors. Small and medium investors are investors who are relatively small in investing in the securities market. They are individuals who engage in securities trading. The purchasing power of these investors is not the strongest, but it is a major player in China's securities market. Small and medium-sized investors, though numerous, are more dispersed and less concentrated. They can't get the right information accurately and in time, and when the rights are damaged, they maybe don't know how or have no way to protect the rights and interests. Therefore, the ability to protect small and medium-sized investors is an important criterion to measure the effectiveness of the market. The purpose of the reform is to protect the legitimate rights and interests of small and medium-sized investors. Only by protecting the legitimate rights and interests of minority shareholders can the market be stable, fast and healthy.

Institutional investors are legal entities that conduct securities trading, such as commercial banks, insurance companies, fund organizations and charities. Compared with individual investors, institutional investors tend to have larger capital and better access to the market. They can collect the market information more comprehensively, realize the effective allocation of resources, promote the supervision of management, and improve the corporate governance and other aspects. Of course, only in a good market environment can the institutional investors play their positive role.

The Impact of the Equity Division Reform on Small and Medium-sized Investors

Analysis of the Situation before the Equity Division Reform.

People are concerned that the shareholding of listed companies will drain the capital and influence the dominant position of the public economy. Therefore, in the past two thirds of the shares cannot be circulated, so as to prevent the loss of assets, and the state-owned economic system can be developed as planned. Before the reform, because the state-owned shares and legal shares were not to be traded, the executives of the corporation were not very concerned about the firm's actual profits and its position on the market. Investors only held tradable shares that take a third of the whole shares who have a relatively small voting rights. Because the shareholders of the tradable shares are scattered, the shares are relatively small, and each shareholder's shares are relatively small. There are also differences between the interests of the tradable and non-tradable shareholders. Non-tradable shares are more profitable. The holders of non-tradable shares may only see their immediate interests and ignore the big development of the whole economic system and disregard the overall interests of the company. The shareholders of tradable shares will be liable for losses incurred by the shareholders of non-tradable in pursuit of their own interests. This mechanism lead to the interest conflicts of the tradable shareholders and non-tradable shareholders.

Analysis of the Situation after the Equity Division Reform.

After the reform, non-tradable shares will get more benefits such as the
appreciation of stocks, the ability to avoid risk and the growth of the company's market value. Through reform, non-tradable shareholders also participated in the market, which promoted the stability and development of the market. Dominated by the government, the mechanism of all the listed shares can be traded has formed. It protected the legitimate rights and interests of investors, especially small and medium-sized ones. To some extent, it has protected the legitimate rights and interests of investors, especially the small and medium-sized ones, and eliminated the unequal conditions among shareholders, thus further alleviating the relationship between the tradable shareholders and the non-tradable shareholders. The investment enthusiasm of small and medium-sized shareholders is higher, and the confidence of the public in the securities market will increase, so as to attract more funds to participate in the circulation of the market. With more money, the securities market will move better, the listed companies will gain more gains, the market value of the shares will rise, and investors will gain more revenue.

The Impact of the Equity Division Reform on Institutional Investors

Analysis of the Situation after the Equity Division Reform.

Before the reform, the public company's governance environment is bad, and institutional investors will adopt a more negative attitude. They are indifferent to all the company things and will not be able to play a positive role in the market.

Analysis of the Situation after the Equity Division Reform.

With the attention of all sectors of the society to institutional investors, the superior also gives institutional investors a lot of encouragement and support, which makes the institutional investors work better. These institutional investors are more likely to invest in companies with successful equity division reform that will give investors more benefits. First, it increases the stakes in institutional investors, giving them more power in the company. With these power, they can be more powerful to strive for their profits, while also raising the interests of small and medium investors. Institutional investors would be more concerned about their shares, and they would be more concerned about the movements of the stock, as they would expect their stock to be better, so to adopt a more positive action.

Some Problems in Equity Division Reform

The Negative Impact of the Major Shareholders with Natural Advantages to Small and Medium-sized Shareholders

Major shareholders are individuals who have more shares. They tend to have corporate governance and more voting rights. They can take their advantage to get priority to effective information and promote the maximization of their own interests. After the reform, the shares of major shareholders were also in circulation, which provided a convenient channel for them to get profits. They have a very easy way of creating a monopoly on both sides of the market, and it's very easy to manipulate the price of stock, causing the market to be volatile. With their strength, they might have the illusion that stocks would go up by deliberately buying stocks. As a herd effect, other small and medium investors will follow to buy stocks. In this way they achieve the purpose of controlling the market.
The Problems of Small and Medium-sized Shareholders Themselves

Small and medium-sized shareholders are more scattered with non-fixed securities trading. Sometimes when they discover problems, they only expect others to solve it. As their access to information is relatively closed and the cost of obtaining information is high, sometimes they prefer not to know the information. Some even give up voting at the shareholders' meeting and do not care about the company's supervision. Their rights are hard to express because of their low shareholding and the spread of equity.

Inconsistent Interests between Institutional Investors and Small and Medium Investors

The purpose of institutional investors to enter the securities market is to pursue the maximization of their own interests which are the same with small and medium investors. Although they bring benefits to small and medium-sized investors, if institutional investors are also on the side of big shareholders, it will be a big disadvantage for small and medium-sized investors. Compared with small and medium investors, institutional investors can go deeper into the company's management, understand the company's internal information and know how to do the best. If they are not on the line with small and medium investors, they will be more detrimental to small and medium investors. Therefore, the existence of institutional investors is a double-edged sword, which has advantages and disadvantages.

Negative Impact of the Incomplete Implementation of Equity Division Reform to Investors

The equity division is a helpless decision in the planned economy system, which was a unique system in China at that time. It only adapted to the economic situation at that time. After the equity division reform, whether the interests of small and medium shareholders were actually protected may need further observation. Sometimes the shareholders' meeting has not really played its part. At the shareholders' meeting, it is impossible to verify whether shareholders can actually get legitimate voting rights, voting rights, etc. Shareholders' rights of control, supervision and ownership cannot be properly implemented.

The Interests of Small and Medium Investors are Possessed by the Company

Equity division reform caused the merger and reorganization of listed companies. In this case, insider trading and other behaviors that harm small and medium shareholders’ rights are highly vulnerable, and the information tends to become opaque. The company may protect its interests by sacrificing the interests of minority shareholders. With reform, the company is also prone to mergers and acquisitions. At this time, it is very likely that the listed company will deliberately inflate the share price, and then occupy the interests of the small and medium-sized investors to realize their own interests. After the major shareholder get benefit form the original company, they are likely to invest to other companies in the market. While the original company was dragged down as its capital and human resources were transferred to other places, and the interests of small and medium-sized shareholders will be infringed. The equity division also raises the problems of the complexity of corporate governance, amplifying the problems caused by the separation of ownership and management rights.
Suggestions for the Equity Division Reform

**Strengthen the Legal Construction and Create a Healthy Market Environment**

The government and relevant departments should supervise the information disclosure of security market and listed companies, to make it timely and fair. The market gradually transfers from weak effective market to strong efficient market, that is, the transmission of information is more and more timely, which can reflect the market environment at that time. Strengthen supervision of the company and management of the internal environment. The company should protect the information and prevent insiders from taking advantage of information to get profit, and strengthen the regulation of law to make full use of the law weapon to arm itself. Any person who has divulged or incurred losses before the publication of the information shall be punished. Investors who violate the law are not allowed to serve as directors, supervisors and supervisors for a period of time. Criminal liability shall also be borne for some serious crimes.

**Strengthen the Positive Role of Institutional Investors**

Institutional investors' interests are similar to those of small and medium-sized investors. We should vigorously develop institutional investors' beneficial role to small and medium-sized investors. Institutional investors can manage companies, and their management actions can benefit small and medium-sized investors.

The market should protect the basic rights and interests of investors. The government should advocate, control, lead a stable investment environment, and should not be eager to seek success, constantly formulate rules for improving the stock market, and should grasp the steering wheel of macro economy. We should protect investors' rights and interests in all aspects, establish a protection mechanism that is in line with the market system, improve the legal system, and protect the legitimate rights and interests of investors.

**Strengthen the Government’s Protection for Basic Rights and Interests of Investors**

When investors enter the securities market to buy and sell securities, they have the right to know the information of the market and the stock, and have the trading rights and trading options of the securities. We should constantly improve the corporate governance structure of listed companies and pay special attention to the accuracy and timeliness of the company's report. Since the initial positioning of the securities market is to raise funds for state-owned enterprises, the market is inevitably has some deficiencies in the process of development due to the inaccuracies of positioning. The government should strengthen the supervision ability. The CSRC is the body that supervises the behavior of the securities market, and the state council, as the regulator of the CSRC, should impartially and objectively supervise the actions of the CSRC. The process of supervision should be more complete, which is the rule constraint in advance, the rule control in the matter and the responsibility to be investigated afterwards. It also encourages the public to pay attention to, report and even criticize the supervision of the stock market.

**Increase Oversight of Institutional Investors and Market Segments**

With the reform of the stock market, the securities market has also made corresponding adjustment, such as information disclosure system, issuance and
trading system, merger and withdrawal system, etc. Market should continue to establish an early warning system for the supervision, improve the efficiency of the market, clear the responsibility of the parties, and perfect the market system to realize the strong effectiveness of information and increase the transparency and accuracy, such as disclosing the company's financial information and predictive information, etc.

Summary

The equity division reform can indeed bring benefits to investors, and it can promote the development of companies and markets in a better direction and be integrated in the world. The equity division reform is a powerful driving force for China's economic development. However, it has some potential problems. For example, after the reform, the priority of large shareholders will continue to exist; the decentralization of small and medium shareholders makes the rights unfocused; and institutional investors and companies may harm the rights of small and medium investors, etc. This paper also analyzes these problems, and expounds corresponding countermeasures and Suggestions. Of course, these will require further observation and analysis. The government and relevant departments should continue to make the lead to ensure that the equity division reform is truly effective.

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References


