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The Reasons and Economic Consequences of Guizhou Bailing's Major Shareholders Pledging Their Shares

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Abstract. As an important financing tool for shareholders, equity pledges are widely used in the domestic capital market, but high-ratio pledges can easily trigger liquidation risks and harm the interests of small and medium investors. This article takes the private traditional Chinese medicine listed company Guizhou Bailing as a case study to explore the real reasons behind the controlling shareholder pledging a high proportion of shares and the economic consequences that result. The study found that Guizhou Bailing's controlling shareholder, Jiang Wei, carried out rolling share pledges due to personal investment financing needs, with most of the pledged funds used for personal project investments, and maintained the size of the pledges by borrowing new funds to repay old ones. Research shows that short-term stock pledges by shareholders don't directly increase a listed company's financial risk, but long-term high-ratio rolling pledges combined with investment failures can, through negative market expectations, raise corporate risk and cause the company's market valuation to drop. The personal risks of shareholders can spill over to listed companies, but the consequences are shared by the company and minority shareholders, making the constraints on controlling shareholders themselves relatively weak. This study can serve as a case reference for identifying the stock pledge risks of controlling shareholders in private listed companies and protecting the interests of small investors.

Keywords: Economic consequences, Guizhou Bailing, major shareholders pledging

1. Introduction

With the continuous development of the domestic capital market, equity pledging has become a common financing tool for shareholders [1].

Shareholders can use their shares in a listed company as collateral to get loans from financial institutions. It is a quick and convenient process, but it also comes with risks like interest costs and the stock being liquidated. The biggest feature of equity pledge is that after shareholders pledge their shares, they don't lose their shareholder status and still enjoy rights like control, while also being able to get a lot of funds [2].

But when the stock price of a listed company keeps falling and the value of the pledged shares gets close to the margin call line, the pledgee has the right to dispose of the pledged shares. If there is a large-scale forced liquidation of pledged shares, the controlling shareholder’s pledged shares

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might be sold off, which could easily cause big swings in the stock price and end up hurting the rights of small and medium investors.

Guizhou Bailing is a privately-owned company listed in traditional Chinese medicine. The founder has long had a high proportion of shares pledged, and later nearly all the pledged shares were frozen. It is a typical case of a controlling shareholder in a private listed company having a high share pledge. This article selects Guizhou Bailing as the research subject to study the real motives behind the controlling shareholder's equity pledge behavior and the various economic consequences it brings, which has certain reference and research value for studying equity pledge risks.

2. Theories related to equity pledges

Equity pledge is when shareholders of a listed company use their shares in that company as collateral with a financial institution to get loan funds. During the period of a stock pledge, the shareholder who pledged the shares generally still retains control corresponding to those shares; as for who gets the stock dividends or payouts, it can be agreed upon by both parties in the pledge agreement. If the pledged shares reach maturity and the shareholder can't repay the principal and interest on time, or if the stock price falls to the warning or liquidation line, the financial institution has the right to handle the pledged shares according to the agreement, selling the shares to cut losses, which could lead to the controlling shareholder losing control passively. There are a few reasons for pledging equity: to satisfy personal interests. According to the separation of two rights theory, after pledging the equity, the controlling shareholder's control does not change, but the economic benefits of the pledged shares have already been converted into cash through a loan. After pledging equity, the controlling shareholder still has full control over the shares, but the cash flow benefits from the pledged portion are restricted. The controlling shareholder can use the funds obtained from pledges for personal investments or to pay off personal debts. In such cases, the financing money won't go into the listed company, allowing them to meet their own personal financing needs [3].

Maintaining control: According to the private benefits of control theory, a controlling shareholder's gains are divided into property rights and control rights. They have a strong incentive to hold onto control and are reluctant to raise funds by selling shares, and the share pledge system happens to fit this need. After completing the equity pledge registration, the property rights of the pledged shares are restricted; as long as there’s no default handling, the voting rights still belong to the controlling shareholder; but if a default occurs later and the shares get sold, the shareholder will lose control over those shares [4].

Equity pledges can have various impacts: on a company's finances, listed companies where controlling shareholders pledge their shares are more likely to face higher financial risks. The likelihood of these risks usually increases as the pledge ratio goes up. However, since a shareholder's equity pledge is a personal action, it does not necessarily increase the company's own financial risk. Although raising funds through stock pledges helps fill the company's cash gap, if the company can't repay the loan or quickly cover the position, it poses some risk to both the company and investors.

The impact on the company's value is that, on one hand, stock pledges reduce the amount of shares circulating in the market, and when the company grows, its value tends to increase. When shareholders pledge their shares, it can make the separation between ownership and management even worse, deepen conflicts between principals and agents, increase the company's agency costs, and ultimately affect the company's value.

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3. Case analysis of equity pledge by the controlling shareholder of Guizhou Bailin listed company

Guizhou Bailing Enterprise Group Pharmaceutical Co., Ltd. was founded on March 25, 1999, and after restructuring and standardizing its operations, it successfully got listed on the Shenzhen Stock Exchange on June 3, 2010.According to Guizhou Bailing's 2023 annual report, the company's top ten shareholders hold a relatively concentrated share. Among them, Jiang Wei is the largest shareholder, controlling shareholder, and actual controller, directly holding 17.39% of the shares. Apart from directly holding a large stake in Guizhou Bailing, Jiang Wei does not have any other indirect shareholdings through platforms. His early partner, Jiang Yong, used to hold a significant number of shares, but later, due to judicial equity handling, pledged share liquidation, and other factors, his shareholding dropped sharply, and he no longer counts as a major shareholder. Jiang Wei has always maintained absolute control over the company, leading business decisions, strategic planning, and personnel appointments. According to the old exchange business rules, there's a regulatory reference limit that says a controlling shareholder can only pledge up to 60% of their own shares. Jiang Wei has pledged all of the shares he personally holds, meaning 100% of his shares are under pledge, which hits the regulatory limit, leaving almost no shares available for further pledging.

3.1. Share pledge situation

From 2010 to 2015, the controlling shareholder Jiang Wei frequently conducted share pledges, using a 'release and re-pledge' rolling operation model. According to information disclosed in the company's announcements, the funds raised from the pledges were mainly used for the shareholders' personal investment activities. As shown in Table 1, 2012 was the year with the highest pledge balance, and on March 9, 2012, as many as 246.4 million shares were pledged, almost all of the equity. From 2014 to 2015, the company continuously carried out pledge, release, and extended repurchase operations. Later on, Jiang Wei mainly used the funds obtained from pledging for personal investments and repaying old, pledged debts. From 2015 to 2019, the scale of Jiang Wei's pledges kept expanding, and the risks grew bigger. Between 2020 and 2022, with Guizhou Bailing's stock price dropping, the pledges hit a concentrated margin call, the pledged shares were disposed of. By 2025, all shares were pledged, all debts matured, lawsuits broke out, and eventually Jiang Wei's shares were disposed of, causing him to lose control of the listed company.

Table 1. Equity pledge situations from 2010 to 2025

Time	Pledged Shares (10,000 shares)	Share of individual ownership	Proportion of the company's total shares	Number of pledges per year
2010-09-29	700	9.03%	4.76%	2
2011-11-28	3000	12.10%	6.38%	12
2012-03-09	24640	99.35%	52.38%	6
2013-11-25	2325.7	9.38%	4.94%	2
2014-12-17	17443	70.33%	37.08%	3
2015-06-12	16305.7	65.74%	34.66%	2

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Table 1. (continued)

2016-12-31	17122.42	68.99%	36.37%	2
2017-12-31	18674.15	75.30%	39.67%	3
2018-12-31	21906.51	88.33%	46.54%	4
2019-12-31	22741.34	91.71%	48.31%	5
2020-12-31	23126.88	93.27%	49.13%	3
2021-12-31	23642.57	95.35%	50.23%	2
2022-12-31	24011.26	96.84%	51.01%	4
2023-12-31	24235.74	97.74%	51.49%	3
2024-12-31	24418.62	98.47%	51.88%	2
2025-04-11	24500	100.00%	52.05%	1

3.2. Analysis of reasons for equity pledge

Jiang Wei wanted to gain personal benefits without losing control of the company. After pledging his shares, he used the funds to invest about 1.68 billion yuan in a medicinal herb planting base project and a cultural tourism hotel project. Investing about 480 million yuan in a medicinal seed base. After the project investment started losing money and the pledged debts kept maturing, Jiang Wei used new pledges to borrow new funds to pay off the old ones; the publicly disclosed information makes it hard to accurately distinguish how much of the new financing was used to pay off old debts versus new investments [5].

3.3. The consequences of pledging shares

Increasing financial risk, the Z-score model mainly calculates the potential financial risk of a company from five aspects: company asset size, profitability, debt-paying ability, financial structure, and asset utilization efficiency. According to the formula, it can be seen that the Z-score is driven by multiple factors [6].

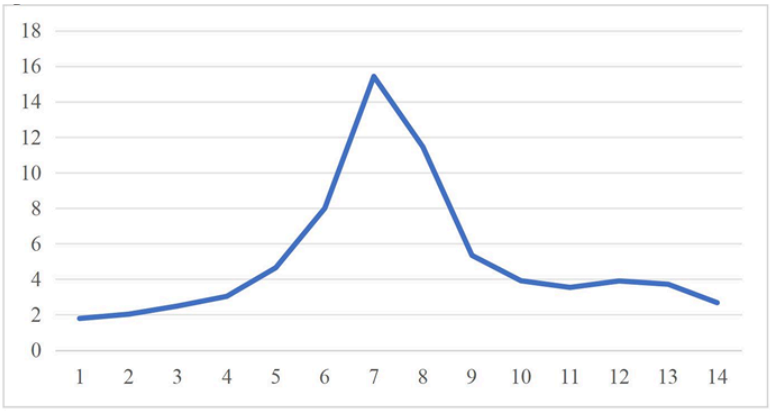

Figure 1. Z-value variation for Guizhou Bailing from 2010 to 2023

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Picture credit: Original

As shown in Figure 1, from the Z-score calculation results, we can see that in some earlier years the Z values were in the financial risk gray warning zone, while in some years the Z values went higher. From 2014 to 2018, the Z-value rose in stages, due to a combination of factors like rising stock prices, changes in share capital, and relatively stable total liabilities; during this period, Jiang Wei carried out large-scale stock pledges. In terms of timing, the Z-score started to decline after 2016; from a theoretical perspective, the negative market expectations caused by a high proportion of pledged shares by major shareholders could potentially transmit personal shareholder risks to the listed company. However, the Z-score itself includes stock market prices and is influenced by various market sentiments, so a simultaneous change over time can't directly prove that share pledging caused an increase in financial risk. As shown in Figure 1, in the short term, the risks from Jiang Wei's stock pledge have nothing to do with the company's own risks. But after 2016, Jiang Wei's pledging to offset other pledges indirectly made investors less confident in the company, causing the stock price to start falling. On top of that, the subsequent sale of the pledged shares by the mortgage institutions drove the stock price down even further. In the first half of 2024, the company's stock was labeled ST; by 2025, it completed the delisting removal. Looking at this case over time, in the short term, just having shareholders pledge their shares does not necessarily increase the financial risk of the listed company. However, in this case, after long-term high-ratio rolling pledges combined with investment failures and other negative events, the company's risk increased significantly. This observation is specific to this case and can’t be directly applied to all listed companies that have pledged shares [7].

Using Tobin's Q to represent company value, this article analyzes changes in this indicator to see whether shareholders pledging their equity affect the company's value. Tobin's Q reflects the market valuation of a company's assets. When Q is greater than 1, it means the company's market value is higher than the replacement cost, indicating that buying new assets is more beneficial for investors and they are likely to invest more, which will also increase the company's value. On the other hand, when Q is less than 1, the company's market value is lower than the replacement cost, so buying new assets is not a good move, investors will hold back on investing more, and the company's value will decrease.

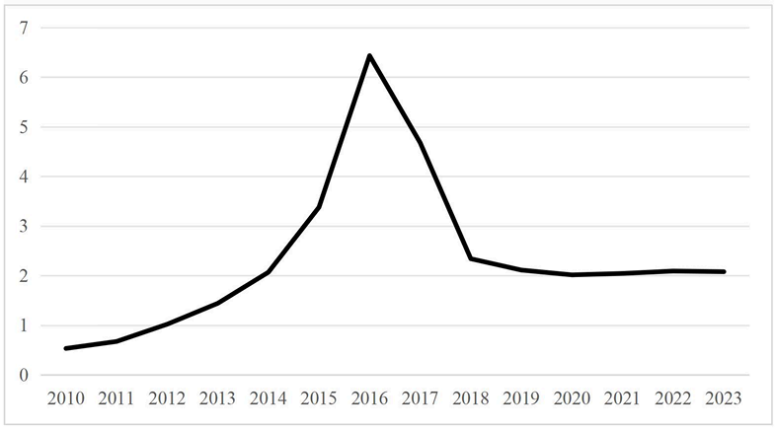

Figure 2. Q-value variation for Guizhou Bailing from 2010 to 2023

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As shown in Figure 2, the company's stock price was undervalued in the first three years. The reason for the surge between 2014 and 2016 was the increase in the number of shares and the crazy rise in stock price. During the same period, Jiang Wei pledged a lot of his shares, but it was probably more due to the overall market cap boost from the stock price at that time. Although the scale of pledged shares is increasing, the capital market hasn't considered it a very high risk, so Guizhou Bailing's valuation is still high. After 2017, it started to decline, possibly because the proportion of pledged shares climbed even higher and the debt risk gradually became apparent, leading the market to develop a negative outlook. This also reflects how shareholder-level risks are passed on to the market. After that, the company's stock price stabilized around 2. Observations from this case's time-series data: When short-term shareholder stock pledges occurred, the market valuation didn't immediately drop; but after long-term high-percentage pledges combined with investment failures and debt defaults, the market valuation of the company did decline. This is a case-specific phenomenon and does not represent the general outcome for all listed companies with stock pledges [8].

In short, it can be seen that the controlling shareholder is using their control improperly to push the company's stock price up or maintain it, making it easier for them to pledge shares again [9]. Relevant departments should provide a environment for listed companies' equity pledge activities that meet the pledgor's requirements while protecting the interests of most people [10].

4. Conclusion

This study discusses its conclusions and limitations. All the data in this paper is based on publicly published information, and the data itself has potential limitations.

Based on the theories related to equity pledges, and by analyzing the process, motivations, and consequences of the equity pledge by the major shareholder of Guizhou Bailing Holding, this paper can draw the following conclusions.

First, from 2010 to 2023, Jiang Wei, the major shareholder of Guizhou Bailing, repeatedly pledged his shares, and later the pledged shares accounted for 100% of his personal holdings; the funds from these pledges were mainly used for the shareholder's personal investment projects. Second, the company's controlling shareholder has pledged a large amount of shares, separating financial rights and control rights. The subsequent impact of a shareholder personally pledging shares is mostly borne by the company and minority shareholders, so the shareholder's own losses are reduced. This makes the company's losses less of a constraint on the controlling shareholder.

By analyzing the case of Guizhou Bailing's shareholders pledging their shares, it turns out that preventing risks from share pledges should start with both internal company governance and external supervision:

Improving internal governance: First of all, Guizhou Bailing is clearly a family-run listed company, with the Jiang Wei family holding over 70% of the shares, which makes it really easy for Jiang Wei to pledge shares. Therefore, the company should boost small shareholders' participation in voting, improve the shareholder meeting and independent director oversight mechanisms, and keep the controlling shareholder's improper actions in check. Preventing the problem of a 'one-voice rule'; improving information disclosure to reduce the likelihood of interest appropriation and protect the rights of small and medium investors. This not only safeguards the rights of minority shareholders but also curbs the appropriation behavior of major shareholders, fundamentally reducing the problems caused by equity pledges.

Secondly, it is important to set up a system to monitor equity pledges. When a company’s controlling shareholder frequently pledges a large portion of their shares, it can increase the risk of

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the company's value being harmed. Having a solid internal monitoring mechanism for equity pledges can help ease some of the negative economic impacts, but internal supervision can't completely eliminate the risks associated with pledges. The company should set up a supervision system, considering all aspects involved in the whole process of equity pledges, and comprehensively monitor shareholders' personal pledge actions to promote the lasting and healthy development of the business.

Strengthen external supervision. First, people need to boost third-party oversight. To effectively protect the interests of outside participants and ensure the market runs steadily, the government and relevant agencies should increase monitoring of listed companies, closely track their business conditions and major events, and promptly make related information public. This way, other investors can better react and adjust their own investments.

Secondly, limit the pledge ratio and increase the severity of penalties. Currently, there are no specific laws in China that directly restrict the pledge ratio of controlling shareholders' shares. Most related constraints come from self-regulatory rules of the stock exchanges, and there are special regulatory requirements in the state-owned and financial sectors. Although these self-regulatory rules have regulatory power, there's still room for improvement in legally enforcing strict limits on high-ratio, high-frequency pledges. Therefore, it is necessary for national laws to clearly limit the proportion of stock pledges and put necessary restrictions on the stock pledge activities of controlling shareholders to address the problem at its root. Relevant authorities should also step up punishment for such behavior, warn company controlling shareholders, and raise legal awareness.

In short, stock pledges give individual shareholders a way to get financing, but they also bring multiple risks to the listed company and, in extreme cases, can trigger changes in control and big swings in the stock price. A listed company itself can't use stock pledges as a way to raise funds; the company should improve its internal governance and set limits on high-level pledges by controlling shareholders to prevent all kinds of risks from them. At the same time, to protect the legitimate rights and interests of small and medium investors, relevant regulatory authorities should also strengthen the management of stock pledges by shareholders of listed companies, standardize the disclosure requirements for stock pledge information, and improve the relevant rules and regulations for stock pledges.

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