

# The Stock Pledge business of Listed Companies in China: An Empirical Analysis

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## Abstract:

This paper provides a comparative analysis of on-site and off-site pledge financing of listed company shares in China. The study aims to help shareholders and lenders reduce information asymmetry and identify transaction risks. The analysis focuses on the differences between the two models in terms of definition, transaction structure, operating process, transaction elements, lending speed, and funding sources. By comparing these aspects, the study enables the loan party to assess transaction risks before lending and allows lenders to choose the appropriate trading model based on their conditions and preferences. Ultimately, the research aims to increase the success rate of financing lending and improve the lender's recovery of the principal and interest. Understanding the differences between on-site and off-site pledge financing can assist shareholders and lenders in making informed decisions and potentially reducing unnecessary losses.

**Keywords:** Stock pledge business, listed companies, decision-making, On-site pledge financing, Off-site pledge financing.

## 1. Introduction

According to the data from National Bureau of Statistics, in 2022, the number of listed companies in China, which included A-share listed companies and B-share listed companies was 4,917[1]. In the capital market, the stock pledge business of listed companies is a common and simple -operating financing business. The market demand for stock pledge business is huge because the top ten shareholders of each listed company will use stock pledge to make financing or they may have the potential demand to make financing. The pledge business of listed companies generally refers to: shareholders holding the stock of listed companies, in order to obtain loan funds from the capital party, they pledge the stock to the lender, and register the stock pledge procedures in China. Analyzing the model and transaction structure of stock pledge financing business could help shareholders of listed companies to confirm the transaction elements, thereby reducing the asymmetry of information caused by industry differences during the transaction. At the same time, these analysis may reduce unnecessary losses of lenders as the lenders will identify the trading risks in the financing business before lending [1].

## 2. Two stock pledge financing models in China

The model of stock pledge financing of listed companies

includes On-site pledge financing and off-site pledge financing. Shareholders of listed companies choose to use On -site pledge financing or Off -site pledge financing methods depends on various factors, such as the amount and rate of financing, the speed of obtaining funds, and the financing information provided by financial intermediaries, which has obvious characteristics of asymmetric information in financial consultation.

### 2.1. On-site pledge financing of listed company shares

Definition: Listed company shareholders commissioned securities company to remotely handle the stock pledge business, this process is called On-site pledge financing. The specific process is that the securities company conducts transaction declarations to the Shenzhen Stock Exchange's trading system based on the entrustment of the incorporated and fusion parties; the trading system confirms the transaction declaration in accordance with the relevant rules and send the transaction result to the Shenzhen Branch of the China Settlement Company. The confirmed transaction results provides the corresponding business processing services such as securities pledge registration and clearing settlement for the stock market [2].

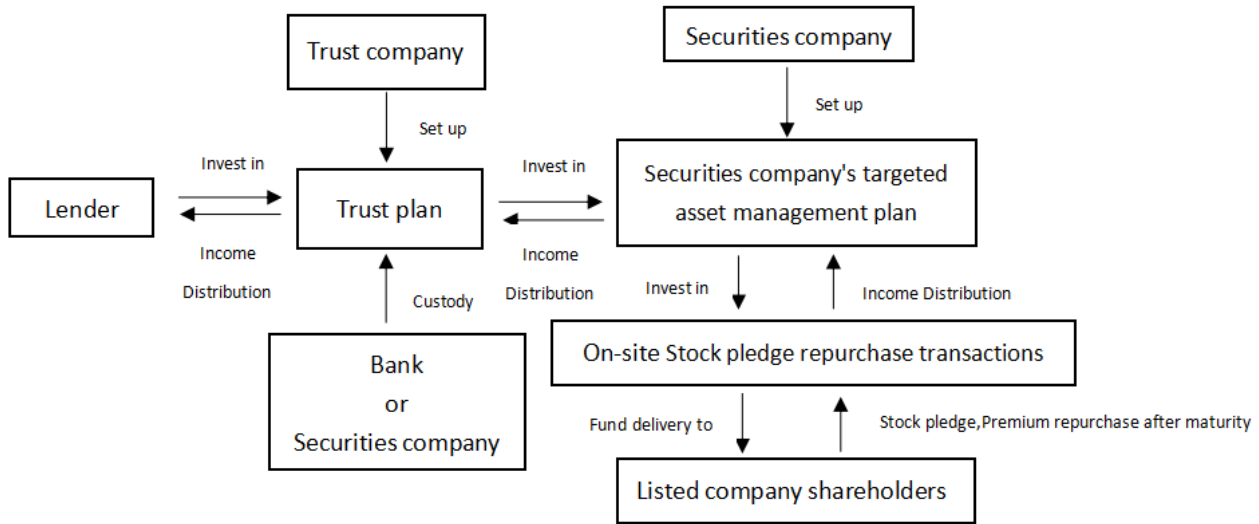


Figure 1. Transaction structure case of On-site pledge financing of listed companies

2.2. Off-site pledge financing of listed company shares

Definition: Shareholders of listed companies and lenders go to the business hall of China Securities Registration and Settlement Company and to handle the stock pledge business directly, this process is called Off-site pledge financing. The specific process is that the shareholders of the listed company directly go to the business hall of the Shenzhen Branch of China Settlement Corporation. Applicants pick up numbers in the business hall and

wait for the call to handle the business according to the prompts at the corresponding counter; the counter business personnel of the investor business department of China Settlement Shenzhen Branch shall review the materials submitted by the applicants. China Settlement Shenzhen Branch has completed the relevant registration procedures within 3 working days after receiving the application and received the handling fee (if required), The pledgee can choose to mail or receive the registration certificate document on the next working day.

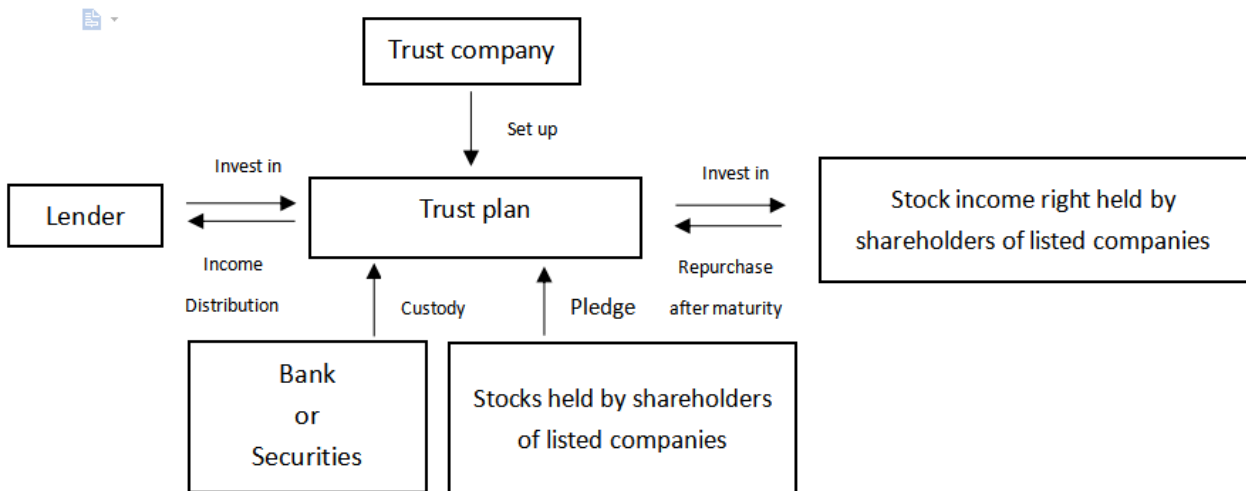


Figure 2. Transaction structure case of Off-site pledge financing of listed companies

2.3. The difference between On-site pledge financing and Off-site pledge financing of

listed companies shares

2.3.1. Financing speed

The speed of Off-site pledge financing is fast, and the speed of On-site pledge financing is slow, and the same On-site pledge financing of listed company stock is generally two weeks slower than the Off-site pledge financing.

### 2.3.2. Operation process

The procedure of the Off-site pledge operation is very short, the shareholders and lenders of the listed company only need to bring specific materials to go to the trading hall of the Shanghai Branch or Shenzhen Branch of China Securities Registration and Settlement Company. While the procedure of the On-site pledge operation is very long, generally, this business needs to open a shareholder card in the name of special channel of financial institutions. The stock accounts of the custodian, the shareholder card, and the shareholders of listed companies must be associated with the three parties. Only after the association is completed, it can be carried out in the field of On-site pledge transaction.

### 2.3.3. Restrictions on stocks

Off-site pledge is business relatively flexible because they do not need to pass securities company channels and they are not limited by securities companies' risk control, this business only requires the consent of the lender. However, On-site pledge business needs to strictly check the stocks, because the pledge on the venue needs to involve the participation of securities companies, and securities companies will strictly screen the stocks pledged stocks from the perspective of controlling risks and prevent disputes. Generally speaking, the following listed companies cannot do the pledge financing in the On-site pledge business market: ST stocks, \*ST stocks; company's profit was negative in the last year, and the situation of this year may still lose money; listed companies with long-term suspension of stocks; listed companies belong to the shell listed company of sensitive industries with unstable performance in the sunset industry and unstable performance; listed companies with high valuations and high stocks pledge rate, such as the shareholders of listed companies have pledged and financing stocks with a total stock market value of more than 70%; listed companies were investigated, warned, and involved in lawsuit.

### 2.3.4. Source of funds

The funds used in On-site pledge business include: the funds owned by the securities company; the funds raised by asset management plan; the targeted asset management plan funds (the source of fund is generally entrusted by banks). All the funds used in the On-site pledge business are the funds of financial institutions' investment standardization business, so securities companies

have strict reviews of standards on borrowers and the companies. However, the funds for the Off-site pledge business are more diverse, and the sources of funds can be individuals, institutions and other special financial products.

### 2.3.5. Trading elements

Risk control: The standard of control in the On-site pledge business is an industry practice, and there will be no obvious changes. Generally speaking, the early warning line of stock pledge financing in the field is 150% to 170%, and the liquidation line is 130% to 150%. Early warning lines and stop loss lines of Off-site pledge business need to be determined according to the specific items. There are no specific standards, and even Off-site pledge business can set up no warning lines or liquidation line.

Financing period: The On-site pledge financing period in the market must not exceed 3 years, and the Off-site pledge financing period does not have restrictions of clear legal and regulations.

Stock pledge rate: The pledge rate of On-site pledge financing in the market is about 30% to 60%. The pledge rate of Off-site pledge financing does not have specific standards, which can exceed the standard for pledge rates of On-site pledge financing stocks.

Financing interest rate: The interest rate of On-site pledge financing in the market fluctuates up and down within the range of the industry's charging standards. While the source of Off-site pledge financing in the market is non-standardized funds, interest rates may be much higher than the interest rate of On-site pledge financing.

### 2.3.6. Stock disposal risk

Under normal circumstances, the risk of disposal of Off-site stock pledge financing is higher than the risk of disposal of On-site pledge stock financing in the market. The On-site pledge stock financing is changed by the securities company's supervision of the stock price. If the stock price falls to reach the warning line or liquidation line, the borrower has not paid the security deposit on time, the borrower is breaking the contract. Then the securities companies can sell the stocks directly in the stock market. And if the stock is limited to sales, securities companies can find institutions that specialize in buying stocks in the market, allowing institutions to purchase stocks through the form of large transactions.[3]

Off-site stock pledge financing is generally supervised by the prices of the pledgee. If the stock price falls and reaches the warning line or liquidation line, the borrower has not paid the security deposit on time, the borrower is breaking the contract. And then the pledgee has the right to sell the stocks according to the stock pledge and

repurchase agreement. In general, before lending, the stock pledge and repurchase agreement must be notarized by the notary office. When the borrower breaks the contract in the future, the pledgee must bring the stock pledge and repurchase agreement and stock notarization to handle the compulsory execution of shares in relevant institutions, and then follow the judicial procedure to prosecute the borrower, and finally sell the stock through judicial auctions to achieve the withdrawal of the funds, and the process of this disposal operation is relatively long. [4]

### 3. Conclusion

This paper compares the differences between On-site pledge financing and Off-site pledge financing of listed companies shares. It specifically compares the differences between the two stock pledge models in definition, transaction structure, operating process, transaction elements, lending speed and funding sources. Through the comparative analysis of the two models, it helps the loan

party to identify the transaction risk in the stock pledge financing business before lending, and help the lenders to choose the trading model of stock pledge financing based on their own conditions and preferences, thereby increasing the the success rate of financing lending and the success rate of the lender's recovery of the principal and the interest. In addition, This paper helps shareholders and lenders reduce information asymmetry and identify transaction risks.

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