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Effect of Convertible Bond on the Logistics and Shipping Industry: Focusing on the HMM Case

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Abstract

Purpose: This study examines the role of perpetual convertible bonds (CBs) as restructuring instruments in Korea's logistics and shipping industry. It specifically focuses on the dilution of shareholder value upon CB conversion into equity and the resulting conflicts between creditors and existing shareholders. Despite these risks, perpetual CBs are frequently used to stabilize distressed firms, especially through state-owned financial institutions. **Research Design, Data, and Methodology:** A qualitative case study method analyzes the case of HMM. The analysis draws upon academic literature, analyst reports, public disclosures, and financial news. The study investigates how the issuance and conversion of perpetual CBs affected HMM's corporate governance, market valuation, and investor sentiment. **Results:** The findings reveal that while CBs offer short-term liquidity and balance sheet improvement, their conversion leads to substantial equity dilution and loss of value for minority shareholders. HMM's case highlights how ambiguous dividend policies, excessive cash reserves, and concentrated public ownership contribute to continued undervaluation. Unresolved CB **obligations** further hinder attempts at privatization. **Conclusion:** The study recommends policy reforms to strengthen disclosure standards, enhance governance transparency, and protect shareholder rights. These measures are critical for improving the effectiveness and sustainability of mezzanine financing in corporate restructuring practices.

Keywords: Logistics and Shipping Industry, Convertible Bond, Non-Capital acquisition, Mezzanine, Shareholder Value

JEL Classification code: P33, P45, M40.

1. Introduction

In the early stage of perpetual bonds, they were mostly issued in general corporate bonds that were settled in cash and did not include stock conversion rights. With the development of the financial industry, there has been an increase in the issuance of equity-related bonds that can be converted into stock, such as convertible, bond with warrant,

and exchangeable (Shin, 2019; Kim et al., 2023). Therefore, the increased complexity of bond structures creates ambiguity in calculating the bond's value, generating conflicts between creditors and shareholders.

This study aims to examine the conflicts between policy financial institutions and shareholders in the logistics and shipping industry through the case of HMM and examine the impact of perpetual convertible bonds on the stock price.

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This study allows policy financial institution authorities to reconsider whether perpetual CBs are a valid tool for restructuring marginal companies.

2. Convertible Bond

2.1. Definition and Characteristics

A convertible bond, which is often abbreviated as CB, is a bond that has the right to be converted into shares. Considering the right that can be converted into shares, it has both the stock and bond characteristics.

The bonds can be classified as convertible bonds (CB), bond with warrants (BW), and exchangeable bonds (EB). Convertible bonds can be converted into shares, bond with warrants are bonds with the right to buy shares, and exchangeable bonds can be exchanged for other shares in the company. Exchangeable bonds are similar to convertible bonds in that the status of a bondholder is established when the rights are exercised. However, convertible bonds have rights to shares of the issuing company through conversion, while exchangeable bonds hold other shares held by the issuing company.

The main reason for issuing CB is to raise capital as a regular bond. Companies can lower their interest rates in exchange for offering the right to convert their status from creditor to shareholder. Additionally, companies' debt will be converted into equity when bondholders exercise their rights, resulting in a low debt ratio.

There are several different characteristics between regular bond and CB. The first is the right to redemption. This redemption right is called a put option if held by investors and a call option if the issuer holds it. If the put option is exercised, the issuer is obligated to repay the bond's principal amount to the investors even before the bond matures. Investors use the put option to recover their principal when the company's financial condition deteriorates. Conversely, issuers use call options to reduce cash flows used for interest payments when the company's financial condition improves. In most convertible bonds, the creditor has the put option and vice versa, as the reason for issuing the convertible bond is to facilitate the flow of funds by giving investors an additional option.

The second is the conversion price. The conversion price is compromised at the time of issuance based on a forecast of the future stock price. Based on the forecast, the issuer and the bond underwriter negotiate the final conversion price. Investors can benefit from converting their bonds into shares if the price of the company's stock is higher than the conversion price. Therefore, if the conversion price is too high, the investor's chances of benefiting from the bond will decrease, and if it is set too low, the issuer's shareholders

will lose money. Therefore, the conversion price changes according to the stock price fluctuation, which is called refixing. Refixing is not allowed indefinitely, and the timeframe is usually around three months.

Finally, convertible bonds are often issued in private placements rather than public offerings. Because of the complex terms and conditions attached to convertible bonds, it is common for investors (usually financial institutions) to negotiate the terms of the issuance beforehand. The difference is that both public and private offerings are more common for conventional bonds.

2.2. Valuation

The following graph shows the price change of a convertible bond based on the stock price. As shown in the graph, when the conversion price (the point where parity and bond floor meet) is less than the stock price (right side of the graph), the convertible bond price increases proportionally to the stock price as the stock price increases. When the conversion price is higher than the stock price (left side of the graph), the convertible bond price does not reflect the increase in the stock price. Therefore, the difference between the conversion price and the stock price determines the convertible bond's price. In other words, investors can either sell the convertible bond as it is or sell the stock after converting it into a stock.

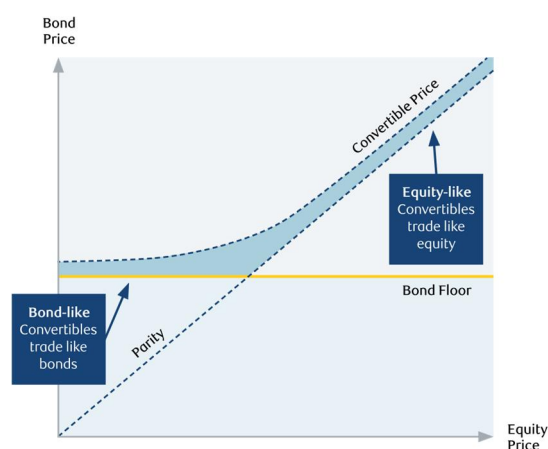


Figure 1: Convertible Bond and Stock Price

Source: <https://www.rbcgam.com/en/ca/learn-plan/investment-strategies/what-are-convertible-bonds/detail> [RBC GAM] What is Convertible bonds?

The most attractive convertible bonds for investors are those with strong earnings growth and without dilution risk, which reduces the disconnect between the stock price and the convertible bond. Earnings growth is a factor that affects both convertible and ordinary debt, but issues related to

share dilution are a major headwind for convertible bonds, referring as overhang issues. An overhang issue is when a large amount of shares, such as treasury stock, stock held by institutions, creditors, or employees, is sold to the market immediately. If the overhang is sold in the stock market at once, the stock price will drop dramatically, which can have a very large negative impact on the price of convertible bonds. In the HMM case discussed in this paper, the overhang issue is the most debatable. This is because Korea Ocean Business Corporation (KOBC), HMM's second-largest shareholder, has converted its convertible bonds into shares, which has caused the stock price to plummet. Therefore, in Chapter 3, we will discuss the issue of HMM's convertible bonds in more detail.

3. A Case of HMM

3.1. Background

HMM is a comprehensive shipping and logistics company founded on March 25, 1976, under Asea Merchant Marine Corporation. It changed its name to Hyundai Merchant Marine in 1983 and was listed on the securities market in 1995. (Kim et al. 2022)

The economic recession that followed the global financial crisis caused a decline in the profitability of the shipping industry due to the oversupply of ships. HMM reported negative operating income since 2011 and negative retained earnings since 2012. At the end of 2013, HMM reported an operating loss of KRW 362.7 billion (270 million USD) and a net loss of KRW 714 billion (530 million USD), with a debt-to-equity ratio of 1,186%. HMM signed a special agreement with the major creditor Korea Development Bank (KDB) to refinance its corporate bonds. In addition, HMM disclosed a plan in December 2013, which included a plan to raise equity capital through the sale of shares in Hyundai Securities Co. and other businesses such as the port terminal business and bulk carriers, as well as the sale of domestic and foreign real estate and securities, and restructuring (HMM voluntary disclosure 2013). Although HMM diligently implemented the planned restructuring and self-rescue plan and Hyundai Group's then-Chairwoman Hyun Jeong-eun participated in improving the company's financial structure by contributing KRW 30 billion (22 million USD) to a third-party capital increase on February 23, 2016, market participant concerned the forced HMM's acquisition. However, on July 23, 2016, HMM was incorporated as a KDB subsidiary by issuing new shares through a convertible bond. HMM issued the 189th General CB of KRW 200 billion (148 million USD) on August 2, 2016, and the 190th General CB of KRW 300 billion (222 million USD) on December 19, 2016. The 189th

CB was underwritten by multiple creditors, including KDB, and the 190th CB was underwritten by KDB only. As a result of issuing CB from KDB, HMM's debt ratio decreased from 2,499% at the end of 2015 to 362% at the end of 2016 (Kim et al., 2023)

3.2. Perpetual Convertible Bond Conversion

Table 1 shows the issuance information of general CBs, perpetual CBs, and perpetual BWs issued by HMM from 2016 to 2020. General CBs were issued in a public offering of KRW 500 billion to industrial banks and creditors, and 240 billion won was issued in a public offering, totaling KRW 740 billion. The perpetual bonds issued by HMM to the KDB and KOBC are all perpetual bonds with a 30-year maturity and an unlimited option to extend the maturity, totaling KRW 3.28 trillion. In March 2017, KWR 600 million was issued in perpetual BW by KDB and KOBC.

Table 1: The Amount of Issued CB

	CB	Perpetual CB	Perpetual Bw
Amount	KRW 740 billion (549 million USD)	KRW 2.68 trillion (1.98 billion USD)	KRW 600 billion (445 million USD)
Investor	KDB	KDB, KOBC	KDB, KOBC
Maturity	3~5 years	30 years	30 years

Source: Financial Disclosure of HMM from 2016 to 2020'

HMM's share price, which started to rise in the second half of 2020, has continued to rise in 2021. The rise in HMM's stock price is related to the expansion in the global container shipping market during the Covid-19 pandemic. The expansion in the global shipping market is attributed to the increase in freight rates due to the increase in the demand for cargo during the economic lockdowns in various countries. HMM's operating performance improved rapidly in the first quarter of 2021, with KRW 1.192 trillion (884 million USD) operating profit, following a turnaround in operating profit to KRW 980.8 billion (727 million USD) in 2020.

Due to the stock price surge, HMM's stock price is higher than the conversion price of perpetual CBs, representing all CBs are within the conversion period. KDB and KOBC can exercise the conversion right, but they hesitated to do so for any CB. The main reason for not converting the perpetual CB into shares is that since HMM's rehabilitation was planned with public funds from KDB and KOBC, it is difficult to maximize the interests of public institutions without considering the interest of minor shareholders. However, as the interest rate of perpetual CB increases (from March 8, 2022, five years after the issuance date), it is inevitable to consider converting the perpetual CB into shares.

In contrast, from the HMM perspective, there is also an advantage to converting CB into shares. If HMM converts the perpetual CBs into shares, HMM will no longer have to pay interest expenses (dividends). The perpetual CBs previously classified as equity will be reclassified as contributed capital, resulting in unchanged total capital. In other words, the CB is the equity with an early redemption risk, which becomes equity that does not have redemption risk, improving capital strength. Furthermore, KDB, HMM's largest shareholder, has announced that it would be a breach of duty if they did not convert the HMM CBs into shares. In addition, the conversion gains represent the signified success of restructuring program using public funds.

3.3. HMM Acquisition

The main purpose of the sale of HMM is to decrease the bank for international settlements (BIS) ratio for KDB up to the global standard. The BIS ratio reached 16.0% by the end of 2021 due to the net losses from the subsidiary (KEPCO) and assets revaluation losses from the decrease in stock price(HMM). The KDB Chairman Kang Seok-hoon has also emphasized the need to sell HMM to manage its balance sheet. He said that if HMM's stock price moves by KRW 1,000 (0.9 USD), the BIS ratio changes by 7 bp (1 bp = 0.01%), which ultimately affects the funding capacity of KRW 1.8 trillion (1.3 billion USD).

The final candidates for the HMM acquisition have been narrowed to four companies, including Harim, Dongwon, LX Group, and German shipping line Hapag-Lloyd. The main problem with the acquisition is the acquisition amount. The sale includes 398,879,156 shares of HMM held by the KDB and KOBC, as well as 200 million shares of convertible bonds and bond with warrants. KRW 4 trillion to 5 trillion (up to 3.7 billion USD) will be required for HMM acquisition. If the interest on the remaining perpetual bonds is added, the actual amount of HMM's sale is expected to be higher. Additionally, falling shipping rates have caused HMM's earnings to plummet this year, and global shipping companies' competition has been increasing. This means that even a successful acquisition would require additional funding on top of the sale price.

As there is hemorrhagic competition among shipping companies, the market is concerned that a company with strong financial status should join the acquisition for sustainable operation. The rating of final candidates based on total assets is lower than HMM (19th) than Harim Group (27th), LX Group (44th), and Dongwon Group (54th), respectively. Even if they succeed in acquiring HMM with all their financial resources, it is still being determined whether they will sustainably manage the company. Market strongly believes that Hapag-Lloyd would not be considered

a final candidate because KDB prefers not to sell HMM to a foreign company.

On December 18, 2023, HMM's creditors, KDB and KOBC, selected the Harim Group-JKL consortium as the preferred acquirer of HMM. When the deal is finalized, Harim Group will become Korea's No. 1 bulk carrier, and HMM will be the world's No. 8 container carrier. However, the acquisition has a negative aspect regarding the Harim Group's financial strength, raising concerns that it may fall into the winner's curse. The winner's curse refers to a company that wins a fierce competition but pays excessive costs to achieve victory. Harim Group's proposed acquisition price for HMM is about KRW 6.4 trillion (4.7 billion USD). However, Harim has only KRW 1.6 trillion (1.2 billion USD) in cash. Therefore, relying on funds from private equity firms such as JKL Partners or other financial institutions is inevitable, leading to be criticized as an unreasonable investment. Additionally, Harim Group requested during the acquisition process that the perpetual CB owned by KDB not be converted into shares for three years. If KDB converts the Perpetual CB into shares, Harim Group's stake in HMM will drop from 57.9 percent to 38.9 percent. In case the conversion is delayed, Harim Group's stake will remain high, and it will be able to receive up to KRW 285 billion (211 million USD) in additional dividends for three years.

In response to ongoing questions about Harim Group's financial status, Harim Group withdrew the request to mitigate the market concern as the controversy grew. On December 26th, 2023, Harim Group introduced the report that HMM's cash reserves should be prioritized for preparing for the current recession and building future competitiveness.

However, the question of financial strength would not be easily resolved. HMM labor unions, which opposed Harim's acquisition, indicate that Harim Group is exploding the risk of cascading bankruptcy by excessively borrowing to utilize its reserves and excessively increasing its capital increase to Pan Ocean, emphasizing that the acquisition is effectively a non-capital acquisition.

According to the Financial Supervisory Service, the non-capital acquisition represents the acquisition of a company primarily borrowing rather than owning capital. This is not illegal, but the likelihood of engaging in unfair transactions, such as spreading false information and manipulating the market price. As explained above, non-capital acquisition is not much different from leveraged buyouts. However, the definition of non-capital acquisition has recently been changed to utilize the acquiree company's assets rather than externally borrowing funds. If the non-capital acquisition is suspected of an unfair transaction, it leads to the dismantling of the company's assets and the delisting of the company, causing damage to investors (Choi et al. 2018). Therefore,

Harim Group's acquisition of HMM faced opposition from HMM shareholders and labor union.

Consequently, KDB, the creditors' representative, announced that the negotiations were terminated. KDB and KOBC are planning to resume the HMM acquisition; however, as in the previous negotiation, the presence of the perpetual CB owned by KDB and KOBC will be a burden to the new acquirer.

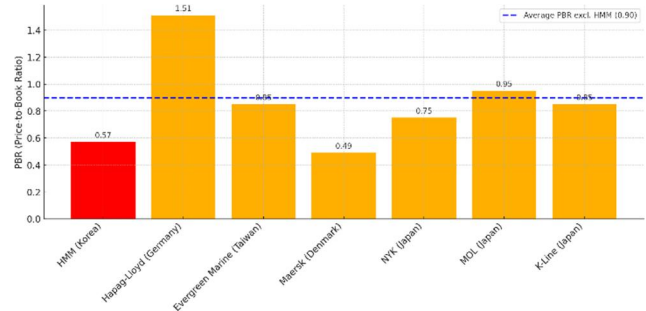
4. HMM Valuation

4.1. HMM's Undervaluation

HMM is the largest shipping company in South Korea and ranks among the leading global shipping companies in terms of operational scale and revenue generation. Despite this prominent industry standing and robust operational profitability, HMM remains notably undervalued when compared to global industry peers. According to Bloomberg, HMM's price-to-book ratio (PBR), a critical metric assessing market valuation relative to net asset value, stood at merely 0.57 as of early 2024. This valuation places HMM among the lowest of the world's top ten shipping companies, raising considerable concerns about its market perception.

To contextualize the severity of this undervaluation, a PBR below 1.0 typically indicates that investors believe liquidating the company's assets would generate more value than the current market capitalization implies. In other words, investors implicitly signal skepticism about HMM's management strategy, long-term profitability, and capital allocation efficiency. This scenario suggests that shareholders may theoretically realize higher returns by discontinuing company operations and distributing the remaining assets rather than sustaining the company as a going concern, an unfavorable and alarming signal.

This undervaluation becomes even more striking when comparing HMM with its global peers. Germany's Hapag-Lloyd, for instance, maintains a PBR around 1.51, nearly triple HMM's valuation. Taiwan's Evergreen Marine similarly exhibits a notably higher PBR of approximately 0.85. Although Maersk, the global leader in maritime logistics, reports a lower overall PBR (approximately 0.49), this figure is skewed downward by poor performance in non-container shipping divisions. Analysts consistently emphasize that isolating only the container shipping segment directly competing with HMM—Maersk significantly surpasses HMM's valuation. Such comparative analysis unequivocally highlights the severity of HMM's undervaluation issue in the global market.



Source: Bloomberg

Figure 2: PBR Comparison of Major Shipping Companies

More illustrative is the case of major Japanese shipping companies Nihon Yusen Kaisha (NYK), Mitsui O.S.K. Lines (MOL), and Kawasaki Kisen Kaisha (K-Line). These companies previously shared similar valuation challenges, with PBRs hovering around 0.4, even below HMM's current level. However, these firms have successfully implemented targeted value-up strategies, primarily through aggressive share buybacks, drastically improving their market valuations. Today, these companies boast significantly enhanced PBR levels, ranging from 0.75 to 0.95. This dramatic improvement demonstrates that proactive capital allocation, specifically reducing excess assets and increasing shareholder returns, can fundamentally realign market perceptions and correct systemic undervaluation.

Contrary to such proven strategies, HMM has adopted policies that exacerbate its undervaluation. In September 2023, HMM unveiled its ambitious medium-to-long-term strategic initiative to become an integrated logistics enterprise, involving significant capital investments totaling approximately KRW 24 trillion by 2030. While ambitious, this strategy inherently increases the company's total asset size, effectively expanding the denominator in the PBR calculation and thereby negatively affecting valuation metrics unless simultaneously accompanied by proportionate increases in stock price. However, HMM has failed to articulate a complementary plan to enhance shareholder value, resulting in continued skepticism among investors and analysts alike.

Compounding the valuation issue further is HMM's inconsistent and unpredictable approach to shareholder returns, notably dividends. For example, in 2022, when HMM achieved an unprecedented net income exceeding KRW 10 trillion, the dividend payout ratio was merely 5.8%. In sharp contrast, despite significantly reduced profits in 2023, the company's dividend payout ratio surged unexpectedly to approximately 43%. Such unpredictable dividend policies severely diminish investor confidence by increasing uncertainty around future shareholder returns. Predictable and transparent dividend policies are

foundational to effective corporate governance and valuation improvement strategies, yet HMM continues to neglect this crucial practice.

Additionally, HMM currently possesses approximately KRW 16 trillion in liquid assets, almost equivalent to its entire market capitalization. Although HMM's primary state-affiliated stakeholders KOBC and KDB justify this large cash reserve by referencing the inherent volatility of the maritime shipping industry, financial analysts broadly regard this justification as excessive. Even during HMM's historically worst financial conditions, cumulative deficits never surpassed KRW 5 trillion. Thus, maintaining cash reserves as high as KRW 16 trillion is considered inefficient and economically irrational, detracting significantly from corporate valuation. Market observers argue that such substantial liquidity should be proactively deployed for strategic share repurchases or convertible bond redemption, which could simultaneously reduce asset size and elevate stock prices, substantially enhancing valuation metrics.

Moreover, HMM's complex governance structure, predominantly led by state-owned entities such as KDB and KOBC, adds complexity and barriers to active value management. Internal conflicts have emerged regarding privatization or corporate restructuring initiatives. For example, KDB, as a financial institution prioritizing restructuring success and market-oriented value maximization, actively favors the privatization of HMM. Conversely, KOBC and its supervising authority, the Ministry of Oceans and Fisheries, appear hesitant about privatization initiatives, possibly due to institutional interests and concerns about diminished organizational roles post-privatization. Such conflicting positions create strategic ambiguity, hampering HMM's ability to implement decisive actions to enhance shareholder value.

To address these systemic issues effectively, market experts consistently recommend clear and decisive value-up strategies, particularly share buybacks and consistent dividend policies. Active share buybacks would enhance valuation by reducing assets while increasing stock price, effectively improving HMM's low PBR. Furthermore, predictable dividend payments aligned with earnings would significantly bolster investor confidence and attract sustained market interest.

4.2. HMM's Value-up Program

On January 22, 2025, HMM announced a formal 'value-up' strategy, focusing primarily on enhancing shareholder returns. Central to this announcement was a commitment to significantly increase dividends and undertake substantial share repurchases, including potential stock retirement. Specifically, the company revealed its intention to maintain a dividend payout ratio of approximately 30% of annual net

profits. It also targeted a minimum dividend yield of 5% based on market value, whichever figure is lower. Additionally, HMM declared its plan to distribute approximately KRW 2.5 trillion to shareholders over one year through dividends and share repurchases, highlighting an aggressive approach to capital distribution that contrasts sharply with its prior conservative dividend policy.

Table 2: HMM Dividend Policy Comparison by Year

Year	Net Profit	Dividend Payout Ratio	Dividend Yield Target
2022	KRW 10+ trillion	5.82%	Not specified
2023	KRW 1 trillion	~41%	Not specified
2025	Projected KRW 1 trillion	~30%	Minimum 5% of market value

Source: Financial Disclosure of HMM from 2022 to 2025'

While on the surface, this substantial increase in shareholder returns might be perceived positively by the market, several critical issues and potential consequences arise from this policy shift. Firstly, the announced capital return scale—KRW 2.5 trillion—reflects a significantly accelerated approach to capital distribution, raising immediate concerns regarding the underlying motivations and potential long-term implications. Given that HMM's major shareholders are government-related institutions, notably KDB and KOBC, which collectively own nearly 70% of the company's shares, this aggressive shareholder return policy could effectively serve as a strategic means for these entities to recover previously invested capital rapidly.

Historically, these government institutions heavily invested in HMM through CBs, providing crucial financial support during severe financial distress between 2014 and 2016. Initially, the bonds were converted into equity at prices significantly below the current market price, thereby yielding substantial unrealized gains. With HMM's recent profitability and accumulation of substantial cash reserves, the announced dividend and repurchase plan may provide an opportunity for KDB and KOBC to effectively monetize these unrealized gains. Thus, market skepticism arises regarding whether this aggressive capital return strategy genuinely represents a commitment to sustainable shareholder value enhancement or if it primarily serves the short-term interests of the state-run institutions as majority shareholders.

Furthermore, such a substantial dividend policy could paradoxically introduce long-term valuation challenges. Although dividend increases generally lead to positive market reactions in the short run, the decision to distribute significant proportions of accumulated cash might limit the company's strategic flexibility, potentially weakening HMM's ability to pursue essential long-term investments and growth opportunities in a highly competitive global shipping market. As an industry, shipping is cyclical,

characterized by substantial volatility in profitability, freight rates, and global trade volumes. Therefore, maintaining adequate liquidity and financial flexibility is essential for sustained long-term competitiveness. However, the announcement of aggressive short-term dividend and buyback policies may compromise HMM's future operational resilience, as excessive distribution of cash reserves could reduce the company's ability to withstand inevitable market downturns.

Additionally, the timing and nature of these capital distribution plans strongly suggest that HMM's major shareholders, particularly KDB and KOBC, are effectively abandoning previous attempts to privatize the company. In the past, privatization attempts faced considerable difficulty primarily due to the heavy ownership by state-affiliated entities and unresolved complexities related to convertible bonds. Aggressively reducing circulating shares through repurchases and subsequent cancellations—while significantly increasing dividend distributions—will inherently consolidate existing shareholders' stakes, notably KDB and KOBC. Consequently, their equity ownership proportion will likely increase even further, surpassing the already significant 70% level. This consolidation may render privatization increasingly challenging, as potential private-sector acquirers might be reluctant or financially unable to acquire a company with such a large and concentrated government stake.

Moreover, given HMM's historical context, this strategic direction toward becoming a fully state-controlled, dividend-focused entity raises significant concerns regarding corporate governance, operational efficiency, and global competitiveness. Evidence from other publicly controlled corporations globally suggests that firms with heavy state influence typically face reduced competitive agility, slower decision-making processes, and increased inefficiencies due to the bureaucratic nature of government-affiliated management. These inefficiencies often manifest through less effective capital allocation, limited innovation, and a constrained ability to adapt rapidly to evolving market conditions. As such, the shift toward more extensive government control and a dividend-oriented policy, rather than fostering market-driven growth and innovation, could diminish HMM's operational efficiency and international competitiveness in the long run.

Another critical aspect is the proposed methodology behind dividend calculation. The announced policy of targeting either a 30% dividend payout ratio or a minimum 5% dividend yield based on the stock's market value, whichever is smaller has created ambiguity regarding actual dividend predictability. While such a policy attempts to reassure investors by providing a minimum yield benchmark, it also introduces uncertainty during periods of exceptional profitability, as the company retains the flexibility to

minimize dividend payouts despite high earnings. Conversely, during periods of weak profitability, dividends could theoretically fall sharply, potentially destabilizing investor expectations. Market analysts typically advocate clear, stable, and predictable dividend policies to enhance market confidence. Thus, this somewhat ambiguous dividend policy formulation might inadvertently maintain, rather than alleviate, investor uncertainty surrounding HMM's future dividend levels.

From a valuation perspective, this policy could also significantly alter investor perceptions of HMM's future earnings potential. Considering typical industry multiples and expected profit trajectories, sustained dividend distributions at this announced level would imply a significantly constrained valuation ceiling. Specifically, if HMM's annual net profits normalize around KRW 1 trillion as currently projected by analysts, maintaining a 30% payout ratio would result in annual dividends of approximately KRW 300 billion. Assuming investors seek a dividend yield of around 5%, this scenario would imply an implied market capitalization ceiling of approximately KRW 6 trillion. Given that HMM currently maintains a higher market capitalization, such a scenario could put downward pressure on stock prices over the medium to long term, further exacerbating the company's valuation challenges.

In summary, despite the immediate positive response triggered by the significant increase in shareholder returns, HMM's newly announced value-up plan raises substantial long-term strategic and governance-related questions. The aggressive distribution of capital, driven largely by the interests of majority government shareholders, risks limiting the company's long-term strategic flexibility, operational efficiency, and global competitiveness. Additionally, the ambiguous dividend formulation policy and the structural reinforcement of state ownership further complicate the path toward privatization, potentially creating sustained barriers to achieving higher market valuations and enhanced investor confidence. Therefore, while the immediate market reaction may reflect optimism toward enhanced shareholder returns, investors and analysts must carefully consider the longer-term strategic and valuation implications embedded within HMM's aggressive capital return initiatives.

5. Conclusions

This study explored the strategic use of CBs as a restructuring instrument in Korea's logistics and shipping industry, focusing on the case of HMM. The analysis reveals that while such instruments can effectively provide emergency liquidity and reduce debt ratios during corporate crises, they also carry significant long-term implications,

particularly when issued and managed by state-owned financial institutions.

The case of HMM illustrates both the immediate stabilizing effect and the lingering complications associated with perpetual CBs. The conversion of CBs into equity significantly diluted shareholder value, which not only led to tension between public creditors and private investors but also triggered a prolonged period of governance uncertainty. Moreover, the opaque nature of Korea's perpetual CB market—especially the lack of disclosure regarding privately placed, cash-settled bonds before 2021—has limited the ability of market participants to assess associated risks fully.

Beyond the financial instrument, the HMM case underscores the structural challenges of prolonged state ownership and inconsistent capital allocation strategies. Although the company has achieved strong profitability in recent years, it remains significantly undervalued compared to global peers, indicating persistent market skepticism toward its governance and long-term strategy. This skepticism is fueled by vague dividend policies and the maintenance of excessive cash reserves, which signal inefficiencies in capital deployment. While ostensibly aimed at correcting undervaluation, the recently announced KRW 2.5 trillion capital return program is structured around either a 30% payout ratio or a 5% dividend yield—whichever is lower—thereby introducing ambiguity and limiting predictability in shareholder returns. Such unpredictability can undermine investor confidence and constrain the potential for stock price revaluation. Additionally, concentrated ownership by state-affiliated institutions further hampers privatization efforts and may restrict the company's strategic flexibility. Historical evidence suggests that firms under substantial government control are prone to bureaucratic inertia, delayed decision-making, and reduced competitiveness. In HMM's case, these governance inefficiencies—compounded by unresolved convertible bond issues—have deterred potential private-sector acquirers and continue to weigh on the company's market performance.

In conclusion, while perpetual CBs can play a vital role in stabilizing distressed firms, their design and deployment must be coupled with robust governance, transparent disclosure practices, and a commitment to market-based

principles. Without these safeguards, the risk of long-term shareholder value erosion and systemic inefficiencies will remain. This study highlights the need for regulatory and institutional reforms to ensure financial innovation, such as mezzanine financing, contributes to sustainable corporate recovery and capital market integrity in Korea.

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Appendixes

Appendix 1: Summary of the Main Contents of Previous Research

Previous research	Theoretical Background
Choi et al. (2018)	Definition and explanation regarding non-capital acquisition
Kim et al. (2022)	Explanation regarding HMM establishment
Kim et al. (2023); Shin et al. (2019)	The development of equity-related bond
Kim et al. (2023)	Explanation regarding perpetual convertible bond in HMM