Universe Scientific Publishing Volume 7 Issue 08

Research on the Application of Financial Risk Control in Real Estate Enterprises

Zhaoxia Zhou
Nanjing Anju Affordable Housing Construction and Development Co., Ltd., Nanjing 210000

Abstract: In recent years, the trend of China's real estate industry has gradually stabilized from its previous overheating, and the risks that come with it have become increasingly apparent. From the current situation, domestic real estate enterprises have a very high demand for funds, and at the same time, due to factors such as limited purchasing, they are facing enormous pressure in terms of capital turnover, which undoubtedly puts greater risk on the company's finances. Financial risk control is becoming increasingly important for the operation of enterprises. Therefore, in order to promote the sustainable development of enterprises, it is necessary to have a reasonable financial risk control plan in place. This article takes ZZ Group as an example to delve into the financial risks faced by enterprises during their operation, and based on data analysis, find reasonable processing methods to propose some suggestions for controlling financial risks in real estate enterprises. The research in this article has certain reference significance for the financial risk control of similar real estate enterprises.

Keywords: real estate industry; Financial risks; Risk Management

1. Introduction

How to control the financial risks of enterprises has always been considered an important research topic in the field of financial management. In recent years, with the continuous improvement of China's market economy system and the gradual deepening of reform, the willingness of enterprises to actively participate in the economic market has also deepened. While real estate companies have achieved rapid development, they have also encountered many financial problems in the fierce competitive environment, among which financial risk occupies an important position. Chinese real estate enterprises have a relatively weak awareness of financial risk control, and there are also errors and deficiencies in their understanding of it. In view of this, this article takes ZZ Group as an example and proposes some reasonable financial risk control suggestions through case analysis of some financial data of the company.

2. Analysis of the current situation of ZZ Group

2.1 Introduction to ZZ Group

ZZ Group is currently a professional comprehensive investment enterprise in China that integrates multiple business processes such as real estate project development, investment and operation, engineering design and construction, marketing strategic planning, information services, property management, etc. It has 24 years of experience in real estate investment, development, operation and management services and has long been focused on commercial development of real estate, Adhering to the business strategy of rapid development for nationally renowned high-quality real estate commercial projects, we have been awarded the title of "China's Top 100 Real Estate Enterprises" multiple times.

2.2 Analysis of the Financial Situation of ZZ Group

1. Current situation in fundraising

Table 1 Financial Data Analysis of ZZ Group in terms of Funding Risk

Indicator/Year		2016	2017	2018	2019	2020
capital structure	Asset liability ratio(%)	90.64	88.22	87.13	83.48	82.68
	Long term debt ratio(%)	9.65	14.58	12.41	14.72	14.31
Long-term solvency	Cash to current liability ratio(%)	8.26	24.59	3.83	3.71	3.26
	Interest coverage ratio	3.19	2.86	2.38	2.31	2.46
short-term solvency	current ratio(%)	119.82	126.77	130.96	141.65	121.37
	quick ratio(%)	119.82	126.77	109.1	93.2	90.11

Source: Financial Statements of ZZ Group from 2016 to 2020

Firstly, from the perspective of capital market structure, a high asset liability ratio is a characteristic of real estate enterprises. Due to the relatively long construction and sales periods, and apart from land acquisition and sales of buildings, some design and construction projects are outsourced, requiring huge funds as support, and also facing significant financial risks, such as the risk of fund chain breakage. From the above data, it can be clearly seen that the asset liability ratio of ZZ Group is decreasing year by year, indicating that its annual capital turnover ability is gradually improving, and the proportion of borrowed funds in all funds has decreased. This is a good phenomenon for the enterprise itself, investors, and debtors. Secondly, in terms of interest coverage ratio, it is greater than 1 every year, so the current ability to repay debts and interest is not very large, and the long-term debt repayment ability is still relatively stable. Finally, from the perspective of short-term debt repayment ability, the cash flow ratio of ZZ Group is increasing year by year, and the annual indicator exceeds 1. This statistical data shows that ZZ Group has sufficient funds and ability to help it repay its current short-term liabilities. But in the past two years, the quick asset ratio of the company has been decreasing year by year, which also indicates that the total growth rate of quick assets is far lower than the growth rate of current liabilities. From the comprehensive analysis, although the short-term solvency of ZZ Group is relatively good at present, the quick ratio is decreasing year by year with the increase of current ratio, which indicates that the inventory is decreasing year by year, and the overall short-term solvency is still declining year by year.

2. Current situation in investment

From a micro perspective, investment risks are presented through some financial data. From 2017 to 2019, ZZ Group has been increasing its investment management efforts in construction projects, with total investment amounts of 9.9 billion yuan, 1.37 billion yuan, and 3.888 billion yuan, respectively. At the end of 2019, the total level of land storage was 9.54 million square meters, and the same type of real estate enterprises had reached about 15 million square meters. Under the enormous pressure of insufficient grain reserves, ZZ Group is still significantly increasing its support and budget for land acquisition, which undoubtedly brings great investment risks.

Current situation in terms of operations (daily operations)

Table 2 Financial Data Analysis of ZZ Group in terms of Operational Risk

Indicator/Year	2016	2017	2018	2019	2020
Days of account receivable turnover	136	144	139	132	136
Inventory turnover rate	0.0017	0.0069	0.011	0.018	0.026
Revenue growth	41.8	1443.2	-45.3	1375.6	1289.2

Source: ZZ Group Financial Statements 2016-2020

Accounts receivable turnover days overall showed a horizontal trend, indicating that the enterprise accounts receivable recovery time control in a reasonable range, there will not be too many bad debt risk. In terms of revenue growth rate, ZZ Group as a whole still shows a rapid upward trend, the growth rate is relatively obvious, this is because ZZ Group has been seeking expansion in recent years, for example, the development of other counties and cities in the province as well as projects outside the province, the growth is relatively rapid, but still need to pay attention to the control of related risks.

3. Financial Risk Analysis and Control of ZZ Group Company

3.1 Financial risks and their control in fundraising

Based on the above analysis, the asset liability risk of ZZ Group is relatively severe, although it is decreasing every year, it is still severe. According to the latest data, the debt to cash ratio of the company is higher than 70%, and the asset liability ratio is too high, causing huge pressure on the company's funds. In 2015, ZZ Group acquired all the shares of an industrial company listed in Hong Kong and successfully entered the Chinese capital market through capital increase and backdoor lending. Since then, from 2016 to 2019, there has been a significant net outflow of actual cash flow in the process of operating and carrying out production activities, and it was not until the first half of 2020 that there began to be a small-scale net inflow of 1.11 billion yuan. In such a situation, one's own business activities lack the ability to replenish blood and have been expanding vigorously, which inevitably leads to a significant demand for fundraising and thus brings about significant fundraising risks.

3.2 Financial risks and their control in investment

The investment risks of ZZ Group are currently within a controllable range. However, statistical data shows that in 2019, ZZ Group successfully acquired 10 plots of land for a land price of 3.8 billion yuan. Among them, one new construction plot had a land use area of approximately 460000 square meters, and the total planned new construction plot area was 1.13 million square meters. At the press conference of the company's performance analysis report in 2019, it was clearly stated that "the company plans to invest 14 billion yuan in new land acquisition in 2020, with 50% -60% of the funds used for new and old renovation, and the other part used for bidding, auction, and listing." Therefore, it can be seen that ZZ Group is at risk of being "short of money and land" and does not have the ability to self generate. The large-scale expansion of ZZ Group resulted in the purchase of some land rights that should not have been purchased, resulting in a huge cash flow and increased investment risks.

3.3 Financial risk control in operational (daily operations) aspects

At present, the cash flow shortage and annual decline in gross profit margin of ZZ Group are urgent issues that need to be addressed, which have brought huge financial risks to ZZ Group. The main reason for this risk is that the asset liability ratio is too high and the fund recovery cycle is too long. ZZ Group should reduce its debt ratio and strengthen equity financing. Firstly, indirect equity investments in individual enterprises or joint ventures can be used to quickly raise enough working capital for the company to improve its operational qualifications and economic benefits; Secondly, funds can be effectively raised through the public issuance of common stocks by listed companies. This type of stock is also a financing measure often adopted by real estate project development and investment enterprises to effectively raise funds. By subscribing to common stocks publicly issued by listed limited companies, the liquidity and financing difficulties of real estate project development and operation can be reduced; Finally, it is possible to consider raising funds by issuing preferred shares. Due to the fact that preferred stocks do not have a fixed maturity date and do not require repayment of the corresponding debt principal, they do not cause financial pressure or risk to the enterprise. They control the debt capacity of real estate enterprises to a controllable extent, promoting the healthy development of the enterprise itself.

4. Suggestions on Financial Risk Control for Small and Medium sized Real Estate Enterprises

4.1 Enhance awareness of fundraising risk prevention

In order for small and medium-sized real estate enterprises to obtain long-term benefits, they must comprehensively and fully consider the problems and risks that they may encounter during the fundraising process, and continuously enhance their awareness of preventing fundraising risks. Improve the accuracy and scientificity of the funding budget, and avoid the direct risk of fundraising caused by errors in fundraising decisions.

4.2 Enhancing awareness of investment risk control

At present, real estate companies need to face a consumer market that is full of limitations and extremely challenging in the market. In order to minimize these investment risks, real estate developers must first conduct a comprehensive investigation and analysis of the supply and demand relationship in the current market before formulating and implementing project investments, in order to choose investment projects that create expected returns.

4.3 Emphasize the business risk assessment system

Real estate enterprises should strengthen their analysis and exploration of the operational system of each project, while also collecting the operational status and financial risk status of similar projects both domestically and internationally. When creating a specific financial evaluation index system, it is first necessary to fully value the comprehensive, comparable, independent, and ability evaluation characteristics of financial risk indicators. At the same time, it is also necessary to measure the credibility and evaluation effectiveness of the indicators to ensure the completeness and accuracy of the established financial risk evaluation system.

5. Research Conclusion

In today's rapidly developing society, real estate enterprises play an important role, and financial risk control in the industry is inevitably of utmost importance. Only by continuously and reasonably controlling risks can enterprises develop in a healthy and long-term manner. Small and medium-sized real estate enterprises should diversify their financing methods to prevent fund chain breakage; At the same time, invest cautiously and conduct a reasonable and effective assessment of project risks; Finally, it is necessary to develop and continuously improve a reasonable risk assessment system, and take preventive measures to ensure the long-term and continuous development of the enterprise.

Reference:

[1] Su Yanni. Reflection on Real Estate Financial Liquidity Risk from the Perspective of Full Process Risk Control [N]. Financial and Accounting Information Report, 2023-06 (006)

[2] Ma Zichen. The Impact of ESG on Credit Risk and Financial Performance of Real Estate Enterprises [J]. Journal of Modern Finance, 2023, (02): 58-62

[3] Jia Ziting. Research on the Current Situation and Countermeasures of Real Estate Financial Management under the New Situation [J]. Finance and Accounting Learning, 2023, (06): 28-30

[4] Huang Zhijin. Reflections on Reducing Financial Risks in Newly Established State owned Real Estate Groups [J]. Wealth Life, 2023, (04): 157-159

[5] Liu Fang. Analysis of the Causes and Control Strategies of Tax Risks in Real Estate Enterprises [J]. Business News, 2023, (04): 97-100