International Journal of Science and Research (IJSR)
ISSN: 2319-7064
SJIF (2019): 7.583

Research on Capital Structure and Financial Risk of Real Estate Companies in China - Based on the Case Analysis of Poly Real Estate

Qian Zhang

Xidian University, College of Economic and Management
No.266, Xinglong Section, Xifeng Road, Chang 'an District, Xi 'an, China
18829513195[at]163.com

Abstract: ***With the acceleration of urbanization, real estate is an industry that affects the national economy and people's livelihood. However, the real estate industry faces a common problem: "how to optimize the capital structure to improve corporate benefits and reduce financial risks". In this paper, the characteristics of the capital structure of China's real estate industry and the risk caused by the relevant indicators are analyzed. Then, taking Poly Real Estate as an example, this paper analyzes the relevant data of the company in 2016, 2017 and 2018, and concludes that the equity capital ratio of the company keeps rising, which can reduce its risk but cannot eradicate it. In addition, the increase of asset-liability ratio and net liability ratio will reduce the return on investment of investors, and thus increase the risk of listed real estate enterprises. Finally, in view of the development status of Poly Real Estate listed companies put forward several suggestions for optimization.***

Keywords: real estate, Poly Real Estate, Capital structure, Financial risk

1. The Introduction

1.1 Research Background

The real estate industry has gradually become the backbone of the national economy. With the reform of the housing system of the real estate industry in China, local governments also hope that the real estate industry can drive the economic development of their own regions, so they gradually begin to pay attention to its development. The development of China's real estate industry has mainly experienced five stages: expansionary policy stage, tightening policy stage, accelerating development stage, returning to containment stage, adjustment stage and falling back stage. The real estate industry is capital intensive and its periodicity is long, so it needs a huge capital supply at the beginning of the industry. With the support of huge capital, its risks are also multiplied.

1.2 Significance and purpose of the study

In the rapidly developing economic operation market, the industry is still facing many difficulties, such as: the banking system is not perfect, so the sustainable and healthy development of real estate enterprises is directly related to the risk in the operation process of the banking system. At the same time, China's capital market is still not mature, and capital structure research as an indispensable part of the development of enterprises, hope to put forward suggestions for the risk of enterprises through the research of capital structure.

2. Concepts related to capital structure and financial risk

2.1 Capital structure

Capital structure refers to the capital and its proportional relationship involved in the normal operation of an enterprise. It can be divided into broad sense and narrow sense. The difference mainly lies in whether the scope includes all the capital and its proportional relationship. The precondition for an enterprise to achieve the optimal capital structure is to promote the balance between leverage benefits and financial risks. Secondly, it depends on whether the enterprise can achieve the maximum economic benefits and the highest comprehensive capital cost. Finally, it depends on whether the enterprise can achieve the maximum social benefits. Only when these are met at the same time can it be said that the enterprise has realized the optimal capital structure in the true sense. However, in reality, the so-called optimal capital structure of many enterprises obviously fails to meet such requirements and only realizes one or several conditions.

2.2 Financial risk

Similar to capital structure, risk also has the so-called broad and narrow boundaries. Some scholars simply define risk as the uncertainty of loss, that is, risk in the narrow sense. Some foreign scholars believe that risk contains two parts: the uncertainty of loss and the uncertainty of profit, which constitute a whole, is the real sense of risk, that is, the so-called generalized risk; The risks used in this paper generally refer to generalized risks.

2.3 Relationship between capital structure and financial risk

Once the proportion of debt in the capital structure exceeds a certain limit, the degree of protection of creditors will be greatly reduced, which will increase the difficulty of debt financing of enterprises and increase the possibility of capital chain breaking of enterprises. At the same time, debt management will also form financial leverage effect, which will further accelerate the formation of financial risk. Annual interest rates on debt are known to change with capital structure. The formula for the financial leverage factor is as follows: DFL= EBITDA /(EBITDA - annual interest on debt). does the financial leverage coefficient change, the resulting leverage benefits and financial risks change in the same direction with the help of its effect; And vice versa. That is to say, leverage returns and risks change in the same direction, increase or decrease with each other; And both of these and the leverage coefficient change in the opposite direction, the first increase and then decrease or decrease.

3. The present situation of capital structure of real estate enterprises in China

3.1 The asset-liability ratio of listed real estate companies is high

Generally speaking, once the ratio of debt capital in the capital structure exceeds the reasonable range, it will aggravate the operation risk of the enterprise and further affect

3.2 The debt structure of listed real estate companies has been continuously optimized

During the four years from 2015 to 2018, Poly Real Estate's current liability ratio was 72.33%, 71.86%, 67.44% and 67.41% respectively, both lower than the safety standard 75% and tending to decrease year by year. Poly Real Estate has become the leader of China's real estate industry, with a typical representative. It shows that the overall debt structure of the real estate industry in China is gradually rationalizing in recent years.

4. Poly real estate case analysis

4.1 Asset structure analysis

Table 4.1: Indicators of Poly Real Estate's capital structure

The annual / *Indicators*	*2018*	*2017*	*2016*	*2015*
Liquidity ratio (%)	1.72	1.78	1.74	1.73
Asset-liability ratio (%)	77.97	77.28	74.76	75.95
Long-term debt to working capital ratio (%)	0.57	0.52	0.37	0.41
Shareholders' Equity Ratio (%)	22.03	22.72	25.24	24.05
Long-term Debt Ratio (%)	21.49	21.2	14.72	16.45

Source: Netease Finance

In the previous article, we have had a certain understanding of the asset-liability ratio. As an indispensable index to measure the asset-liability items of an enterprise, the assetliability ratio plays a huge role in the creditor's evaluation of the solvency of an enterprise. As can be seen from the above table, the asset-liability ratio of Poly Real Estate in the four years from 2015 to 2018 is 75.95%, 74.76%, 77.28% and 77.97% respectively. In addition to a slight decline compared with 2015 in 2016, the overall trend kept rising and reached a four-year peak in 2018. The continuous rise of this index is obviously not a good signal for the real estate industry, which means that the proportion of liabilities in total assets is rising, which is bound to affect the repayment ability of debt.
Meanwhile, the ratio of long-term debt to working capitalis 0.37%, 0.52% and 0.57% respectively from 2016 to 2018, rising year by year in the recent three years, indicating theincrease of the company's debt, which means that

5. Suggestions on the optimization of China's real estate capital structure and risk control

5.1 Take appropriate sales strategies and accelerate the recovery of house money

The housing recovery rate of typical real estate enterprises in 2018. In recent years, the representative listed real estate companies in China are constantly improving the housing recovery rate, in order to provide enough funds for the operation of the following real estate projects. Looking forward to 2019, enterprises should strictly control the recovery rate of housing funds, and accelerate the destocking, and reserve sufficient development funds for enterprises.

5.2 Give full play to the financial leverage effect of enterprises and avoid blind debt management

Poly Real Estate's financial leverage coefficient has become larger in recent years, and the fluctuation range of earnings per share brought by the corresponding common stock will expand accordingly. This indicates that even if the capital structure of the company remains unchanged, if the financial risk gradually expands, then the probability of financial crisis will also gradually increase, which needs our attention. The solution lies in reducing the huge debt pressure of enterprises, increasing the profit before interest and tax of enterprises, and gradually shifting the focus of enterprise financing to the way of equity.

5.3 Control the level of current liabilities to optimize capital structure

The debt structure of the real estate industry is obviously unreasonable, and the long-term and short-term solvency is weakening, which deserves close attention of enterprises. From the asset-liability ratio and current ratio of Poly Real Estate in recent years, it is clear that its current liabilities are growing too fast. Therefore, we should consider moderating the growth rate of current liabilities and increasing long-term non-current liabilities in order to relieve the debt repayment pressure of the enterprise

Reference

[1] ChaohuiLi, “Capital structure analysis and optimization of real estate enterprises,”. Modern Economy, XII (6), pp. 971-976, 2015.

[2] ShaochengNiu, BingLi. “Research on Financial Risk Control and Countermeasures of Listed Companies,” China Market, III (3), pp.65-67, 2014.

[3] ZuopingXiao, “Analysis of the capital structure characteristics of China's listed companies,” Operations Research and Management, XXIII(1), pp.14-19,2006.

[4] BingLi,”Risk and capital structure analysis,” Journal of Quantitative and Technical Economics, XXI(3), pp.23-25, 2003.

[5] ZhenfengYang, “Research on Capital Structure and Financial Risks of Listed Companies in China ,Shanxi Normal University, Shanxi,2012

[6] Sang YeHuang, “Financial development level, capital structure and enterprise risk taking,” Finance and Accounting Bulletin,VII(18), pp. 26-29,2017.

[7] QianLiu, Research on the Capital Structure Optimization of Real Estate Listed Companies., Shanxi University, Shanxi, 2012

[8] Guang Li., Venture Capital, First-mover Advantage and Capital Structure, Graduate School of Nankai University, Tianjin, 2013

[9] GuohuaShao, ”Real Estate Finance Analysis and Countermeasures,”Special Zone Economy, VIII(12),pp.34-44,2008

[10] Hong Qiao, “Optimal design of Poly real estate capital structure,” Finance and Accounting Bulletin, XI (17): 19-23, 2017.

[11] ShaoxinLiu, Research on Capital Structure Optimization of Sunshine Real Estate Company, Hunan University, Hunan,2013.

[12] Miaomiao Chen. An empirical study on capital structure and financial risk of real estate listed companies, Shandong building University, Shandong, 2015.

[13] Yanying Li. “Research on the capital structure of listed real estate companies in China: A case study of Vanke,” Times Economics and Trade,VIII (25), pp.26-36, 2017.

[14] ZhenfengYang, “Research on capital structure and financial risk of listed companies in China,” Journal of Shanxi University (Social Science Edition) Postgraduate Theses, XXXIII(39),pp. 56-63,2012.