Research on Enterprise Financial Risk Management Based on Cash Flow-A Company as an Example

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Abstract. With the growth of domestic economy, minor enterprises are growing steadily, the financial risk is also increasing. Analysis of the characteristics of minor enterprise’s financial risk, identification of financial risk and effective control is an important guarantee for their healthy development. In this context, taking a company as the object, we analyze the management problems of the company’s financial risks on three aspects of financing, investment and management on the basis of cash flow. By analyzing we find that the company has problems of unreasonable financing structure and low matching degree of capital investment, and put forward some concrete measures to broaden the financing channels and improve the structure of investment.

Introduction

With the rapid development of modern economy, the financial risk is the key factor that threatens the healthy and sustained development of enterprises under the environment where the business environment is complex and changeable, and the uncertain factors are greatly increased as well. It is worth to note that a series of enterprises especially small businesses have not put high emphasis on financial risk management. Even if some enterprises have a certain of risk consciousness, as lacking of effective control measures, the operation and development of the enterprise is in jeopardy. Therefore, the prevention and research of financial risk ought to be paid more and more attention.

Analysis of the Current Situation of Enterprise Financial Risk Management Based on Cash Flow

A company was founded in 2010, with the registered capital of 500 thousand yuan, which belongs to the industrial manufacturing enterprises, specializes in general machinery and equipment, machinery parts, hardware production and processing. The operation of the company is small and the operation period is short. The enterprise owner and the operator combine together and the internal structure is simple.

Analysis of Current Situation of Financial Risk Management in Financing

According to the cash flow statement in recent years, we draw the bar charts of net cash flow generated by financing activities in 2011-2016 years. The Figure 1 shows the size and positive and negative value of the net financing flows of each year, the inflow and outflow of funds in an enterprise's financing activities may be judged by that.

Figure 1. A column of net flow for corporate financing activities (2011-2016).

As is shown in Figure 1 that A Company’s net capital flow was positive and the amount was large in 2011, indicating that the amount of funds raised was larger, and the inflow of funds was far
larger than the outflow. The gap between the inflow and outflow of the company is narrowed and the amount of financing decreased in 2012. Between 2013 and 2016, net cash flows from financing activities were negative, and negative values gradually increased. Therefore, the amount of capital outflow and inflow are gradually widened, and the amount of funds became less and less, the outflow of funds became more and more.

A company has different financing methods and financing proportions in different periods. The amount of money borrowed from relatives is the largest, and the rest is obtained certain loans from banks and other financial institutions by the use of credit. Otherwise, the owner’s own contribution combined into all year’s financing. The four methods of financing flattened in 2011, but still mainly borrowed from relatives and friends. From 2012 to 2015, most of the sources of financing for enterprises mainly depend on internal accumulation, however, the accumulation of funds reduced year by year, and the loans borrowed from banks are also small, and the enterprise owners’ contribution changes every year.

Analysis of the Current Situation of Financial Risk Management in Investment Links

A company also makes some financial and managerial mistakes in the investment process. Unreasonable capital investment, by calculating the matching degree of funds, we draw the source of A company's investment in fixed assets to analyze the investment situation. The matching degree of capital refers to the matching degree between the source of the investment fund and the project invested, its reference table is shown in Table 1.

Table 1. Reference table of matching degree of fund input.

<table>
<thead>
<tr>
<th>Matching extent of funds (x)</th>
<th>x ≥ 70%</th>
<th>70% &lt; x ≤ 50%</th>
<th>50% &lt; x ≤ 30%</th>
<th>x &lt; 30%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fund matching degree</td>
<td>high</td>
<td>higher</td>
<td>little low</td>
<td>very low</td>
</tr>
</tbody>
</table>

A company accounts for 32% of fixed asset investment from long-term investments and 68% of short-term borrowing with low matching degree in capital investment. The study finds that, in the specific way of the source of investment funds, the sources of funds mainly depend on loans from relatives and friends, while most of the loans from relatives and friends belong to short-term loans, reflecting the low matching degree of the funds of the company.

Analysis of the Current Situation of the Financial Risk When In Managing

Short Term Debt Paying Ability Index and Analysis. Since its inception, a company has usually raised some of its funds in the form of loans to meet the needs of operations, investments, and so on, in order to achieve better development of enterprises. Since the amount of money is different at each stage and most of them are short-term borrowings, they need strong solvency. By compiling the form of cash flow liabilities ratio of a company in recent three years, the debt paying situation of a company in different periods is analyzed concretely, as shown in table 2.

Table 2. The cash flow debt ratio of the A company between 2014- 2016 (Unit: yuan).

<table>
<thead>
<tr>
<th>Years</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>① net cash flow generated by operation</td>
<td>1038573.24</td>
<td>983425.24</td>
<td>903895.79</td>
</tr>
<tr>
<td>② current liabilities</td>
<td>1703212.54</td>
<td>1764524.58</td>
<td>1800604.36</td>
</tr>
<tr>
<td>①② cash flow liabilities ratio</td>
<td>61%</td>
<td>56%</td>
<td>51%</td>
</tr>
</tbody>
</table>

As shown in table 2 that the net cash flow was 61% of the current debt in 2014. The cash flow liability ratio was 56% in 2015 and 51% in 2016 respectively, and the ratio is going down. It shows that a company has low ability to pay short-term debt, and there is a risk of the short-term debt payment.

Accounts Receivable Index Analysis. Accounts receivable turnover rate means the ratio of the sales revenue of products and the average balance of accounts receivable during the period\[2\]. It is also an important ratio to show the situation of the turnover of accounts receivable. A company often provides products for customers on credit and then produced a number of accounts receivable.
Table 3. The calculation sheet about the accounts receivable turnover rate and days of turnover of a company (2012-2016).

<table>
<thead>
<tr>
<th>Years</th>
<th>2012</th>
<th>2013</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales revenue (yuan)</td>
<td>1795645</td>
<td>1865924</td>
<td>1986046</td>
<td>2026345</td>
<td>19472811</td>
</tr>
<tr>
<td>An average balance of accounts receivable (yuan)</td>
<td>409031</td>
<td>447463</td>
<td>781908</td>
<td>891534</td>
<td>917233</td>
</tr>
<tr>
<td>Turnover of accounts receivable (the number of)</td>
<td>4.39</td>
<td>4.17</td>
<td>2.54</td>
<td>2.27</td>
<td>2.12</td>
</tr>
<tr>
<td>Accounts receivable turnover in days (days)</td>
<td>82</td>
<td>86</td>
<td>142</td>
<td>159</td>
<td>170</td>
</tr>
</tbody>
</table>

The table3 indicates the accounts receivable turnover rate is going down constantly from 2012 to 2016, however, the accounts receivable turnover in days is increasing constantly. The accounts receivable average turnover rate is about four times, and relatively normal in the management of accounts receivable. Since 2013, the number of accounts receivable turnover in days are gradually elongated, with larger variation, indicating that the company accounts receivable management problems are becoming more and more serious.

Problems and Analysis

Problems and Causes during Financing Activities

Difficulty in Financing. A company mainly relies on internal financing. The internal financing means they accumulate finance constantly and change retained earnings into capital to raise finance during the development of business\(^3\). It can also include family property, money from friends and relatives, loans and enterprise retention. Because of the difficulty and low cost of internal financing, it is welcomed by small enterprises. Survey showed that in 2011-2016 years, the amount of funds received by banks loans, loans from relatives and friends and their own deposits has gradually decreased, and the difficulty of obtaining funds has become more and more increased. With the development of the company, the business mainly depends on internal accumulation of the finance to sustain normal development, but it also exists some limitations. Only when the business is in good condition can the internal accumulation be made, and the amount of funds obtained is limited.

There are mainly two reasons about the difficulty in raising finance of A company. Firstly, due to the lack of awareness of corporate financing management, it does not show much attention to the cost of capital and manage effectively in fund-raising, which was greatly harmful to the fulfillment of business objectives. Secondly, the company does not predict correctly in advance about the number of funds, which leads to the randomness and subjectivity of the actual fund-raising and the mismatch between the amount of capital raised and the actual demand of the enterprise\(^4\). The waste of enterprise funds is bound to reduce the efficiency of enterprise funds.

The Unreasonable Financing Structure. A company has unreasonable financing structure, and the proportion of internal aid financing is relatively large. Since 2010, the wayt has been used to raise funds both inside and outside, the quantitative structure of financing tends to be irrational. On the whole, the company has acquired capital from the operations mainly through internal financing. At the initial stage of the establishment of the enterprise, the business was in good condition and the credit was high. Some short-term loans were made from the bank. Because the commercial bank is very strict with the loan of the small business and loans are limited, so it cannot fully meet the funds demand of the normal business development. So the enterprise has to acquire more funds through various means of internal assistance.

Questions and Reasons in Business Activities

Matching Degree of Capital Input Is Low. From the above analysis, the paper calculates the matching index of capital input in the investment activities of a company. Calculated for nearly three years of fixed asset investment funds from long-term loans accounted for the proportion of total investment funds is 32%. Table 1 shows that the matching degree of capital input is on the low side because of lack the long-term assets of enterprises, and the funds raised from the outside are mostly short-term loans. So we have to invest in long-term assets with short-term funds.
The Investment Decision-Making Mechanism Is Irrational. A company’s managers adopt individual decision-making without forming a reasonable investment decision mechanism. Since the beginning of 2013 year, a company has been experienced fierce competition from competitors, resulting in declining profits. Company managers trying to expand the production scale to reduce fixed costs, to obtain low-cost advantage to promote the sale of goods, but this is not a permanent policy. A company relies on short-term borrowing to expand the scale of operation, once the sales of goods accounts receivable fails to recover so as unable to repay the loan in time, the company will have a credit crisis. Therefore, the individual decision has great limitations, it increases the potential investment risk of the enterprise.

Measures to Reduce the Financial Risk

The Prevention Measures of Financing Risk Management

Raise the Awareness of Financing Management. Facing the impact of capital cost on enterprise development, a company should raise the awareness of financing management. In enterprise activities, corresponding financing plans and strategies must be developed to decide the financing scale. A company should anticipate the demand for enterprise funds from the financial management objectives, the business objectives and operation.

Expand Corporate Financing Channels

In view of the unreasonable financing structure, a company should broaden the financing mode, optimize the capital structure of the enterprise and diversify the financing risk. As manufacturing enterprises, capital demand is more and more mixed, operating activities and funds use relatively wide scope, so the risks are relatively large. The company can not only borrow money from the bank, but also finance lease, account financing, commercial paper financing and the financing of advance receivable.

Investment Risk Management Preventive Measures

Improve the Investment Structure. A company should avoid using short-term financing to invest in long-term assets. So it may provide perfect financial statement data to banks and other financial institutions to achieve long-term capital, and improve the matching degree of capital investment. A company's investment in internal fixed assets is not only a choice of purchase method, but also a choice of financing lease mode. That will reduce the pressure of capital flow and reduce the investment risks.

Establish a Sound Investment Decision-Making Mechanism. A company can set up investment decision department and perfect investment decision mechanism. Small enterprises, whether private enterprise or partnership and private limited liability company, the operators and owners of enterprises are basically merged into one. Due to the relatively simple organizational structure of a company, the management of small enterprises is very prominent. The personal appeal of entrepreneurs, especially entrepreneurs, is often a key factor in maintaining the stability of business management. In terms of enterprise financial risk management, the leadership of the enterprise is the ultimate interpreter and leaders who cannot be arbitrary. It is necessary to put our heads together, listen to the opinions of the personnel at the grass-roots level, it will be helpful to the enterprise to make scientific and rational decision-making.

Conclusion

In the condition of the current market economy, enterprises should raise the attention to cash flow management, enhance the awareness of financial risk management, comprehensively investigate the relevant cash flow management methods suitable for their own, as well as effectively control the financial risks of enterprises and actively promote the sustainable development of enterprises.
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References


