ISSN: 2688-9323

Comprehensive Analysis of Enterprise Financial Risk

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Abstract

Enterprise financial risk runs through the entire business process of an enterprise, and evaluating the risk is the basis for risk prevention. From the perspective of enterprise management, the paper analyzes the current financial management from the concept, causes, and management of financial risk, and puts forward corresponding suggestions. Provide theoretical support and thinking perspective for enterprises to formulate corresponding development strategies and make strategic adjustments.

Keywords

Financial Risk; Reason; Risk Management.

1. Introduction

Under the conditions of the market economy, enterprises face various risks, among which financial risks are everywhere. One of the real estate giants, Evergrande Group, failed to pay attention to and manage the financial risks of the company and failed to operate prudently to changes in the market situation, resulting in serious deterioration of operating and financial indicators, and finally, a huge financial crisis broke out in 2021. Therefore, enterprises should pay attention to the management of financial risks, and regard financial management as the core issue.

There is a lot of research on financial risk today. Liu and Gu expounded on the basic principles of building a group enterprise financial risk management system and constructed an innovative financial risk management system [1]. Based on the background of service-oriented government construction, Xue and Wang discussed the manifestations and causes of local government financial risk around the core concept of local government financial risk. It also points out the matter existing in the financial risk management of local governments in my country and puts forward suggestions and countermeasures for local government financial risk control based on performance evaluation [2]. Wang and Xing analyzed the financial risks in the process of coal resource integration based on the practical problems encountered by YongMei Coal Company in the integration of regional resources and proposed measures to deal with the risks [3]. Huang Wanting pointed out that the frequent bankruptcy of enterprises due to financial risks and the eruption of crises used the financial statement analysis method to analyze the typical domestic listed company-Dongfeng Motor Company, and pointed out the main financial risks faced by Dongfeng Motor Company [4].

The above studies all prove the significance of financial risk and a financial risk management system. Suggestions are put forward to reduce financial risk losses, such as improving information asymmetry, standardizing capital payment flow, and improving the performance appraisal system. This article makes a comprehensive analysis of financial management from the concept, causes, and management suggestions of financial risk, which is conducive to promoting the sustainable, healthy, and stable development of enterprises.

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2. The Concept of Financial Risk

2.1. Definition

Financial risk is an inevitable product of the capital movement of enterprises under the market economy. It is the opportunity and possibility of loss due to the influence of many uncertainties in the financial activities of the enterprise, which makes the income of the enterprise deviate from the expected. Problems in almost every link in the organization and management of financial activities may lead to the transformation of such risks into losses, resulting in the reduction of profitability and solvency [5]. The most common include market risk, financing risk, investment risk, credit risk, tax risk, and legal risk. As an economic signal, it reflects the operating conditions of the enterprise.

2.2. Type

1. Market risk

Market risk refers to the impact of unpredictability in market interest rates, exchange rates, stock prices, and commodity prices on an enterprise. Chief among these are changes in stock prices and exchange rates. In the stock market, stock prices change rapidly. If the prices fall sharply, the company may face the risk of being acquired or forced to delist. The third-party stocks held by the company will make the value of the financial assets held by the company full of uncertainty. Once the stock price falls sharply, the financial assets will depreciate, and the company may face a financial crisis.

In addition, with the advancement of economic globalization, the foreign-related business of enterprises is increasing, and the risk of exchange rate fluctuations is also increasing, which brings new challenges to enterprises. During the inflation period, the currency depreciates sharply, which will cause foreign exchange losses in the accounts receivable of the foreign-related business, and the assets will face shrinkage. At the same time, the value of foreign exchange items will also decline. This requires enterprises to establish the awareness of medium-sized financial management of exchange rate risk to avoid losses caused by exchange rate risk.

2. Financing risk

The main financing ways of enterprises are internal financing and external financing, and external financing includes debt financing and equity financing. Due to the diversification of financing objects and financing methods and the uncertain factors in the financing process, enterprises are faced with financing risks. The causes of current corporate financing risks include excessive debt, lack of capital structure, and high financing costs. In the financing process, enterprises should fully consider these factors. Enterprises need to always pay attention to some key financial indicators to control financial leverage, such as the current ratio and asset-liability ratio, which are closely related to the generation of financial risks. To prevent financial risks in the course of operation, enterprises need to control them, reasonably determine the scale and method of financing and strengthen the operation and management of debt funds.

3. Investment Risk

Investment risk refers to the risk that an enterprise undertakes by making unreasonable use of idle funds and investing too much in high-risk areas. With the development of society, many non-financial enterprises have embarked on the road of production and financing [6], investing in financial institutions in various ways, blindly and excessively involved in the financial field, over-investing in financial products, and moving towards the "departure from the real to the virtual" "path of. However, the development of the financial market brings great uncertainty, which increases the investment risk of enterprises. If the value of the financial assets held by them falls sharply, it will even bring difficulties to the financing of enterprises. Therefore,

ISSN: 2688-9323

enterprises should avoid excessive financialization, moderately invest in the field of virtual economy, and rationally use spare funds.

4. Fund recovery risk

Capital recovery risk refers to the risk that the debt is due and the counterparty does not perform, resulting in the possibility of loss. This requires financial personnel to always pay attention to the turnover effect of corporate funds. On the one hand, take notice of accounts receivable, you can use indicators such as accounts receivable turnover rate to judge. If the company's more credit sales will cause uncertainty of funds, then cash discounts can be used to speed up the recovery of the company's money. Excessive accounts receivable cannot be recovered, which may affect the company's daily liquidity needs. This requires enterprises to do a good job of investigating the counterparty to prevent the occurrence of bad debts from the source. On the other hand, pay attention to the sales status of products. Products can only be realized when they are sold. You can use indicators such as inventory turnover rate to judge. If there is a backlog of inventory, you can increase sales expenses, improve product quality, reduce costs to gain price advantages, or become a counterparty. offer commercial discounts.

5. Tax risk

Tax risk is the unreasonable tax planning of the enterprise, which leads to the payment of unnecessary taxes or involvement in tax disputes. The country's tax policy is constantly being reformed, the taxation department's ability to collect and manage is also continuously enhanced, the tax-related business of enterprises has become transparent, and the impact of tax risks is also increasing. This requires the tax-related personnel of enterprises to strengthen their awareness of paying taxes, understand the latest tax policies, and prevent tax risks. On the one hand, we should pay attention to preferential tax policies and make good tax planning. On the other hand, we should pay attention to whether the current applicable policies and regulations are changed, and whether relevant qualifications such as high-tech enterprise certification meet the conditions and other factors that may affect the tax payment of enterprises. Qualified enterprises can also set up tax risk management departments internally to supervise and manage the production and operation of enterprises.

6. Legal risks

The concept of "enterprise legal risk" first appeared in the "Administrative Measures for Legal Advisors of State-owned Enterprises" promulgated by the State-owned Assets Supervision and Administration Commission in 2004. "Enterprise legal risk" refers to the lack of knowledge of relevant laws and regulations, the wrongful actions of actors, or changes in objective circumstances such as national policies during the implementation of the law, which lead to differences with the expected interests of the enterprise itself, thus bringing unfavorable benefits to the enterprise. The possibility of legal liability [7]. If you violate the "Anti-Monopoly Law" and be sanctioned or violate the contract, you will be liable for huge compensation. At present, many companies do not pay much attention to the prevention of legal risks, and only take measures to remedy them when they occur. However, as a corporate legal person, legal risks are everywhere, and you should take precautions. Chief among them is contract management. Once a contract is signed, it is not only a document but also involves the rights and obligations of the company. A good contract should not only urge both parties to perform their obligations but more importantly, avoid losses.

3. Features

1. Objectivity. Financial risks permeate every aspect of an enterprise's daily operations and are not transferred due to people's subjective will. Financial risks cannot be eliminated. Enterprises can only prevent risks according to their conditions and minimize the losses caused by the occurrence of risks.

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2. Bidirectionality. Risks and benefits coexist. The existence of financial risks may cause losses to enterprises but also bring opportunities. High risk is accompanied by high returns. For example, the stock investment of a company is full of uncertainty, but the benefits brought to the company are also immeasurable.

3. Comprehensiveness. Financial risk exists in the whole process of production and operation of an enterprise, and it will have a large or small impact on multiple links. In the process of enterprises operating with external funds, financial risks also follow, but it is difficult to be noticed. This requires enterprises to do a good job in risk prevention and monitoring, and pay enough attention to them.

4. The Reasons for the Formation of Financial Risks

4.1. The Macro-environment is Complex and Changeable

All operating activities of enterprises are based on the environment, and the macro environment is complex and unpredictable for enterprises. The variability of the external environment may bring opportunities and benefits to enterprises, but it is more of a threat. Take the new crown epidemic in the past two years as an example. During this period, many small and medium-sized enterprises failed to withstand the pressure and faced bankruptcy or went bankrupt and liquidated, including many large enterprises, especially the manufacturing industry, although they were able to survive, their operating performance was facing losses, and this is the epidemic. uncontrollable and sudden.

In addition, the international situation will also affect the operation of enterprises. For example, the Russian-Ukrainian conflict appears to be thousands of miles away from my country, but in the era of economic globalization, Chinese companies cannot stay out of it. The Russian-Ukrainian conflict has caused a sharp rise in crude oil prices, which inevitably brings economic burdens to some companies that use crude oil as raw materials. In terms of different industries, Chinese companies have been actively investing in Ukraine in recent years, such as Longyuan Power, Arowana, and other companies. The conflict between Russia and Ukraine has inevitably affected the business of these companies in Ukraine.

4.2. Inadequate Internal Control

On the one hand, the financial risk of an enterprise is affected by the external environment and policies, and on the other hand, it is also due to the imperfect internal control of the enterprise. Internal control is the foundation of an enterprise's financial management system and an important factor in enterprise development and management. The governance structure of some companies is not perfect, the board of directors fails to perform its duties, and the board of supervisors is a fake. In the process of operation, such as fund management, procurement business, asset management, sales business, etc., it fails to assess various risks and does not have clear strategies to deal with financial risks, resulting in regulatory loopholes in enterprises. Based on different life cycles of enterprises, there are differences in the impact of internal control quality on enterprise financial risks. According to the life cycle theory, enterprises can find their period and formulate internal control systems to control the financial risks enterprises. If the responsibility center is refined, the responsibility investigation is strengthened, and the improvement of the internal control quality will restrain the financial risk of the enterprise.

4.3. The Quality of Financial Personnel is too Low

The quality of enterprise employees varies. Older employees may not be able to adapt to new policies and environments and keep pace with the times. The new employees are inexperienced, which requires the human resources management department of the enterprise to achieve the distribution and balance of the new and old employees and to do a good job in training the new

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and old employees. Financial personnel should strengthen their awareness of financial risks, strengthen their sensitivity to financial risks, correctly recognize financial risks, and improve countermeasures.

4.4. Unreasonable Capital Structure

One of the most important points of business continuity is the need to balance the relationship between business risk and financial risk. Enterprises should correctly use leverage to manage the company's funds and achieve governance efficiency. Financial leverage not only reflects the solvency of a company's debt but also serves as an indicator for banks and other institutions to identify corporate risk signals. Therefore, companies need to control their financial leverage. For example, companies can increase unemployment insurance premiums, reduce employee unemployment risk premiums, and reduce company labor costs. The company has more free cash flow and profits for endogenous financing and debt repayment, thus making the company financial leverage. drop [8]. A reasonable capital structure, on the one hand, minimizes the risk cost of the capital structure, and on the other hand, maximizes the relative benefits.

5. Advice on Financial Risk Management

As the premise of realizing the development strategy of the enterprise, enterprise financial risk management is the basis for the enterprise to enhance its self-value.

5.1. Avoidance of Financial Risks

Risk aversion is taking the initiative to give up or change measures when the possibility of risk loss is high. There are many measures to avoid financial risks, such as refusing to trade with counterparties with bad credit to reduce the risk of bad debts; setting a leverage red line, establishing a debt early warning system, and achieving the best capital structure; on the premise of ensuring the realization of financial management goals, choose a less risky investment plan, and prudently engage in equity investment.

5.2. Transfer of Financial Risk

Risk transfer means that the enterprise transfers all or part of the risk to a third party by some means. There are many ways to transfer risks. The most commonly used ones are the purchase of property insurance by the enterprise to transfer the risk of property loss to the insurance company; when investing abroad, the enterprise can use the joint investment to transfer the risk to other parties involved in the investment; issue stocks to raise funds. When raising funds, the stock can be underwritten to the underwriter, and the risk of financing failure is transferred to the underwriter [9]; a service guarantee letter can be signed with the counterparty to avoid default by the counterparty; high-risk projects can be securitized to transfer risks, etc. Transferring risk to other parties can greatly reduce the loss of business financial risk.

5.3. Hedging Financial Risks

Financial risk hedging refers to the introduction of certain assets or derivatives that are in the opposite direction to the underlying asset and offset profits and losses to reduce financial risk losses. Risk hedging is a very effective way to manage various types of risk. The biggest role of hedging trading is to lock in losses and keep profits. The key to doing a good hedging transaction is to reduce transaction costs, do a good job of risk monitoring and forecast risks, flexibly combine investment products, and use call or put options to hedge.

5.4. Compensation for Financial Risks

Financial risk compensation refers to measures taken by an enterprise to compensate for possible losses caused by financial risks. Compensate for risks that cannot be managed or avoided through risk aversion, risk transfer, or risk hedging. For example, you can sell goods at

ISSN: 2688-9323

a premium, increase risk returns, or increase your reserves and emergency capital to deal with risk losses. Risk compensation is proactive and ex-ante, which is to predict possible losses and take measures in advance. The research and analysis of this paper show that the financial risk of an enterprise is caused by the macro environment, internal control, the quality of financial personnel, and the capital structure. Risk management suggestions are put forward from the four aspects of risk avoidance, transfer, hedging, and compensation. Enterprises should invest cautiously and can reduce financial risks by setting leverage red lines, properly purchasing property insurance and financial derivatives, and increasing their reserves and emergency capital. resulting losses.

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