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Research on the Innovative Mode of Financial Leasing for SMEs

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Abstract

Small and medium-sized enterprises (SMEs) play a crucial role in modern economies. However, due to various internal and external factors, they have long faced significant challenges in accessing financing. To address this issue, this paper delves into the research of "Innovative Models of Financing Leasing for SMEs," aiming to provide SMEs with a more flexible and sustainable financing approach. Key factors for the successful adoption of these new models include policy support, the economic environment, and the size and management capabilities of the company itself.

Keywords

Mall and Medium-sized Enterprises (SMEs); Financing Leasing; Innovative Models; Case Analysis; Influencing Factors; Development Trends.

1. Introduction

Small and medium-sized enterprises (SMEs) are an indispensable driving force for China's economic development and an important source of job creation. However, while its importance should not be underestimated, its financing has persisted in serious difficulties. The reason for this is that small and medium-sized enterprises are small, have limited financial resources, and have limited financing channels. Traditional financing models require high liquidity for SMEs, for example, bank loans often require high collateral or credit guarantees, while equity financing can cause companies to lose control. At the same time, although financial leasing is a flexible financing tool, its scope of application and role are limited in the actual operation process. Therefore, in order to solve the financing problems of small and medium-sized enterprises, it is imperative to explore an innovative financing model that is more suitable for the characteristics of small and medium-sized enterprises. Through the introduction of innovative financial leasing models, it can provide SMEs with more flexible and convenient financing channels, which will help enhance their competitiveness and sustainable development capabilities. The purpose of this study is to explore the innovative model of financial leasing for small and medium-sized enterprises, in order to provide a new solution to the financing problems of small and medium-sized enterprises and promote their healthy and stable development.

Looking back on the development of China's financial leasing industry, we note that the rise of this field is relatively late, and the progress in theoretical research is slow, and the system is not perfect. However, in recent years, with more and more attention from the government and academia, a series of new research perspectives and ideas have emerged in the field of financial leasing. Although the research on financial leasing for small and medium-sized enterprises is still relatively scarce, a number of research results worthy of attention have emerged in this regard. Wu Shenzhi (2003) found that financial leasing is an inevitable choice for small and medium-sized enterprises to finance. Based on the analysis of the financing difficulties of small and medium-sized enterprises, his paper proposes that solving the financing difficulties of small and medium-sized enterprises is an inevitable choice and an effective way to strengthen

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the function of financial leasing, and puts forward corresponding countermeasures [1]. Zeng (2019) believes that after the introduction of the financial leasing industry into China, the process of its phased development is essentially the process of institutional entrepreneurship carried out by institutional entrepreneurs such as financial leasing companies, and the professionalization, legalization, and institutionalization of the industry are gradually realized through the coordinated promotion of leasing enterprises, industry organizations, governments, user enterprises and other field entities [2]. Zhao Na et al. (2021) believe that both financial leasing and bank credit will significantly improve the company's investment efficiency, and there is a significant substitution effect between financial leasing and bank credit. For private companies with high asset-liability ratios, low tangible net asset ratios, or private companies, the substitution effect of financial leasing on bank credit is more obvious due to the high degree of financing constraints of the companies [3]. Lan Jianping (2016) believes that the so-called innovation of financial leasing business model is based on the direct leasing, sale-leaseback and other models in traditional leasing methods, starting from the actual market situation, and on the premise of not violating relevant laws and regulations [4]. Shi Yanping (2021) found that after enterprises adopt lease financing, their market value is often higher because their leased objects are often equipment or equipment of great significance to the company's operation. The lessor, out of its own profit acquisition, supervises and even manages the lessee to a certain extent, thus forming a huge short-term profit pressure; In order to meet the demands of lessors, corporate executives pay more attention to improving short-term and predictable profits, increase short-term investments with more profitable levels, and ignore long-term R&D investment, resulting in a significant decline in corporate innovation [5].

2. Status Quo

2.1. Definition of Financial Lease

Financial leasing, as a special means of financing, also known as lease financing or financial leasing, provides a non-traditional funding path for enterprises using assets. In this model, the leasing company buys assets specified by the customer, such as industrial equipment, machinery, or vehicles, and then leases these assets to the customer, who pays rent during the lease period. Unlike conventional leasing, financial leasing focuses on the financing function of an asset rather than just its use value. The characteristics of financial leasing include that the ownership of the assets is owned by the leasing company during the lease period, and the customer only has the right to use it; At the end of the lease, the customer generally has the option to purchase the asset, renew the lease or return the asset to the lessor; The payment structure of rent includes the principal and interest in the base rent; For leasing companies, the rent received is often considered income and can be used for tax deductions, giving the business a tax advantage. Financial leasing is seen as a convenient means of raising capital due to the significant benefits of providing capital flexibility, capital savings, and risk diversification. Applicable to many industries, financial leasing has become one of the important channels for small and medium-sized enterprises to obtain financing.

2.2. Regular Forms of Financial Lease

2.2.1. Finance Lease

In this model, the leasing company acquires the assets required by the customer and leases them to the customer. During the lease period, the rent paid by the customer consists of the principal and interest components. At the end of the lease term, the customer generally has the option to purchase the asset, renew the lease or return it. This is suitable for customers who want to stay on top of the asset for the long term and may eventually buy it.

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2.2.2. Operating Lease

In an operating lease, the leasing company offers a lease agreement for a shorter period, which is usually accompanied by a lower rent. In this type of lease, the ownership of the assets is mostly still owned by the leasing company, and the customer only has the right to use the assets. This approach is suitable for clients who want to maintain flexibility in the use of assets and want to avoid the risk of asset depreciation.

2.2.3. Installment Lease

The customer pays the rental company the rent including the principal and interest according to the established instalment plan. After the full payment is made, the leasing company will transfer ownership of the asset to the customer. This leasing method is suitable for customers who are willing to gradually solve their financing problems and want to ease the pressure of payment.

3. Empirical Analysis

3.1. Sichuan CZ Machine Tool Group Co., Ltd.

Sichuan CZ Machine Tool Group Co., Ltd. (hereinafter referred to as the "lessee") is a high-tech enterprise (2023), a small and micro enterprise, and a subsidiary of Yingxiang Industrial Group. It is a CNC manufacturing company focusing on the development, production and sales of machining centers, CNC machine tools, large-scale CNC special processing equipment and ordinary milling machines. The lessee currently has a domestic market share of 8% for CNC machine tools and 35% for general products, making it the largest vertical machining center in Southwest China. Not only that, it is also a second-level enterprise, a key backbone enterprise of the national mechanical and electrical industry, and a provincial manufacturing informatization demonstration enterprise, which has emerged in the mechanical and electrical industry of Zigong City, and has become one of the main manufacturers of CNC equipment in China.

In order to further expand the scale of production and sales and enhance sustainable profitability, the company decided to introduce a number of advanced processing center equipment, but limited by financial strength, it was unable to purchase in large quantities. After various investigations, the company finally chose to cooperate with Zhongfeng Financial Leasing Co., Ltd. (hereinafter referred to as the "lessor") to adopt the sale-leaseback model to revitalize the stock assets and replenish the working capital. In this transaction, the lessee transferred a batch of equipment owned by it to the lessor at a price of 26 million yuan, and at the same time signed a financial lease contract with the lessor, agreeing to pay rent to the lessor as agreed during the lease period. At the expiration of the lease term, the lessee retains the leased property at the nominal price. Through this series of arrangements, the lessee can obtain a stable, long-term, low-cost capital to meet the capital needs of the manufacturing. At the same time, compared with the traditional mortgage loan model, the sale and leaseback has more advantages in terms of procedures, time, financial statements, cash flow, etc.

3.1.1. The Profits are Increasing

It can be seen that from 2018 to 2022, the company's various profitability indicators have shown an upward trend year by year, indicating that financial leasing has enhanced the profitability of the company and promoted the continuous improvement of performance.

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Table 1. Profitability indicators of Sichuan CZ Machine Tool Group from 2018 to 2022

Time	Gross Margin	Net Profic Margin	ROE
2018	29.36%	6.85%	7.12%
2019	30.12%	7.24%	8.05%
2020	31.57%	7.96%	9.33%
2021	32.61%	8.73%	11.26%
2022	33.42%	9.19%	12.74%

Data source: "CZ Machine Tool (Group) Co., Ltd. Corporate Bond 2023 Tracking Rating Report", United Credit, 2023.06.27.

3.1.2. The Short-term Debt Risk is Declining

Table 2. Current ratio and quick ratio of the company from 2018 to 2022

Time	Current ratio	Quick ratio
2018	1.32	0.95
2019	1.45	1.08
2020	1.67	1.26
2021	1.89	1.45
2022	2.15	1.64

Data source: "CZ Machine Tool (Group) Co., Ltd. Corporate Bond 2023 Tracking Rating Report", United Credit, 2023.06.27.

The current ratio and quick ratio are important indicators to measure the short-term solvency of a company. Where current ratio = current assets / current liabilities, quick ratio = (current assets - inventories) / current liabilities. From 2018 to 2022, current ratio of the company increased from 1.32 to 2.15 and its quick ratio increased from 0.95 to 1.64, both of which have achieved significant improvements, and in 2018 they were much higher than the average manufacturing industry (the average current ratio and quick ratio were 1.48 and 1.06, respectively. This shows that the company's liquidity has continued to improve through financial leasing to revitalize existing assets and replenish working capital, and the short-term debt repayment risk has been declining, and its financial position has become increasingly stable.

3.1.3. The Efficiency in the Use of Funds is Improving

Table 3. Total asset turnover and Inventory turnover of the company from 2018 to 2022

Time	Total asset turnover	Inventory turnover
2018	0.65	2.42
2019	0.72	2.85
2020	0.84	3.36
2021	0.97	3.92
2022	1.12	4.57

Data source: "CZ Machine Tool (Group) Co., Ltd. Corporate Bond 2023 Tracking Rating Report", United Credit, 2023.06.27.

As shown in the table above, the company's total asset turnover ratio increased from 0.65 to 1.12 from 2018 to 2022,, and the inventory turnover ratio also increased from 2.42 to 4.57, reflecting that financial leasing has effectively improved the efficiency of capital use and allowed enterprises to create more value with fewer assets.

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3.1.4. The Evaluation of Implement Effectiveness

In the traditional financial leasing model, the lessee's capital demand is usually due to a shortage of funds and needs to take the form of financial leasing to purchase equipment, property and other assets. However, the innovation of Sichuan CZ Machine Tool Group is that it sells its existing assets, such as machinery and equipment, warehouses, etc., to Zhongfeng Financial Leasing Co., Ltd., and then "leases" these assets back in the form of leasing. This method is known in the industry as the Sale and Leaseback model. The advantages of the Sale and Leaseback model are reflected by many aspets. Firstly, by converting the fixed assets in the enterprise into working capital, the cash flow of the enterprise will be further enhanced to meet the short-term capital needs of the enterprise. Secondly, change the situation of a large number of fixed assets and relatively few current assets of the enterprise, improve the rationality of the asset structure of the enterprise, and make the assets more flexible. Thirdly, after the company sells its fixed assets, it can reduce the amount of total assets, which improves the company's return on assets. At the same time, there are no new liabilities of the enterprise, which reduces the pressure of the debt on the enterprise. Rental expenses can be used as the operating cost of enterprises, and some tax incentives can be obtained in many countries and regions. Finally, businesses lease assets back out immediately after they are sold, with no impact on the normal operation of the business. Through innovation in the mode of financial leasing, Sichuan CZ Machine Tool Group has realized the rapid return of funds in a relatively short period of time, improved the efficiency of capital use, and improved the overall operational efficiency of the enterprise to a certain extent by optimizing the asset structure and reducing financial risks.

3.2. Credit Ease Co., Ltd.

3.2.1. Company Profile

Founded in 2006 and headquartered in Beijing, Credit Ease Co., Ltd (CE) is one of China's leading integrated financial services groups. CE focuses on providing diversified financial services including credit, wealth management, financial leasing, etc., and is committed to helping individuals and small and micro enterprises solve financing problems through innovative financial solutions. CE is a company that provides comprehensive financial services, and its innovation in financial leasing is particularly prominent, especially in the field of financing for small and micro enterprises.

3.2.2. Innovation Model

One of CE's innovations lies in the application of its financial leasing business model, especially the "credit leasing" model for small and micro enterprises. The core of this model is to use big data and cloud computing technology to evaluate the credit of enterprises, and provide financial leasing services without collateral on this basis. Compared with traditional asset-based financial leasing, credit leasing pays more attention to the operating conditions and credit history of enterprises, thereby greatly reducing the financing threshold for small and micro enterprises. First of all, by collecting the financial data, operating data and market data of the enterprise, the big data analysis technology is used to conduct a comprehensive credit evaluation. The second step is to customize a personalized financial leasing plan for the enterprise according to the evaluation results, including financing amount, lease term, repayment method, etc. Finally, after the credit evaluation and financing plan is formulated, the signing and execution of the financial lease contract will be completed quickly to provide the required funds or equipment for the enterprise.

3.2.3. The Evaluation of Implement Effectiveness

The "credit leasing" model adopted by CreditEase has significantly improved customer satisfaction, from 85% in 2018 to 95% in 2022. This increase in satisfaction shows that CreditEase's services have received positive reviews among the customer base. Reasons for the

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improvement may include faster financing approvals, more flexible financing options, and better customer service. The increase in customer satisfaction not only strengthens customer loyalty, but also attracts more potential customers through word-of-mouth, thereby further expanding CreditEase's market share.

4. Suggestions

In 2023, we do see momentum in the economic recovery, but this weak recovery has not been completely reversed. It is expected that in 2024, the financial leasing industry will maintain a slow development trend. Although the market as a whole has stabilized, we can also observe the fragmentation within the industry. The leading financial leasing company has accumulated rich business resources and professional capabilities through years of operation, and has strong capital strength and risk management capabilities, so it has shown obvious advantages in the competition. Looking ahead to 2024, financial leasing companies will still need to face asset quality pressures and liquidity challenges, despite the limited overall market development speed. In other words, the pressure to transform your business is increasing. In order to adapt to this challenge, financial leasing companies need to strengthen professional operations, improve risk identification and management, and enhance the sustainability of their business, so as to maintain their leading position in the fierce market competition.

5. Conclusion

At present, SMEs are still facing significant difficulties and high costs in the financing process, which requires an urgent expansion of financing channels. Thanks to its flexibility and convenience, financial leasing has evolved into a key tool to alleviate these dilemmas. With the increasing demand for capital from small and medium-sized enterprises, traditional direct leasing methods cannot fully meet these needs, which has promoted the emergence of innovative financing models such as sale-leaseback, credit leasing and entrusted leasing. These models provide a wealth of financing options and improve the efficiency of the use of funds by activating the fixed assets of the enterprise, thereby improving the financial position of the enterprise and enhancing its long-term business stability. Key factors for the successful adoption of these new models include policy support, the economic environment, and the size and management capabilities of the company itself. Looking ahead, with the promotion of "Internet +" and other emerging technology models, financial leasing is expected to achieve deep integration with information technology, supply chain finance and other fields, and further create new models, so as to provide a broader financing space for small and medium-sized enterprises.

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