

The Causes and Countermeasures of High Debt Ratio in Real Estate Enterprises

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Abstract. Real estate companies generally have a high debt to asset ratio, which not only brings more profits but also brings more risks. Therefore, maintaining a reasonable debt to asset ratio is of great significance to enterprises. This article first lists the significance of reducing the excessively high asset liability ratio of enterprises, and then analyzes the reasons for the high asset liability ratio of real estate enterprises. Targeted suggestions are given to address this phenomenon, hoping to provide some help for the optimization of the asset structure of real estate enterprises.

Keywords: Asset liability ratio, Real estate, Optimization of capital structure.

1. Introduction

With the rapid development of the economy, people's demands for housing continue to increase, and the real estate industry has also achieved good development. The real estate industry is a capital-intensive industry with its own characteristics, such as high demand for funds, long investment payback period, and high dependence. Under the current market economy conditions, to achieve the goal of maximizing operating profits, enterprises usually adopt a debt-based approach, but this strategy must control the asset liability ratio well. Only when the debt to asset ratio is within a reasonable range can sufficient material conditions be provided for the development and operation of enterprises, thereby promoting better development. Therefore, for real estate listed companies, having a good capital structure and doing a good job in optimizing and managing their capital structure is crucial to ensure smooth capital operation.

This article systematically elaborates on the capital structure of listed real estate enterprises, deeply analyzes the problems and reasons of the capital structure of listed real estate enterprises, and proposes countermeasures and suggestions to improve the capital structure of listed real estate enterprises.

2. The significance of optimizing capital structure

2.1. Measuring the financial risk level of real estate enterprises

A reasonable debt to asset ratio refers to the adjustment of a company's debt structure through certain methods and means, enabling the full play of the role of debt and promoting the increase of enterprise value through this approach. The real estate industry is relatively capital intensive, and the reasonable use of financial leverage can effectively enhance the scientific and rational investment decisions of enterprises, which is conducive to the improvement of the economic efficiency level of enterprises, and can help enterprises better avoid and prevent possible financial risks.

When real estate companies borrow from banks or other financial institutions, the other party needs to evaluate the company's debt paying ability, considering the company's history and current debt situation. The cost of asset liability ratio is a potential important factor for creditors to consider, and an excessively high asset liability ratio will make them more cautious.

2.2. Evaluating the management and profitability of the enterprises

How to control a reasonable amount of debt and how to make reasonable use of internal resources, including debt, to maximize profits, can be used to evaluate the profitability and management ability of a company. If a company can leverage its debt effectively and generate higher returns than its costs, it reflects strong management capabilities. If the benefits obtained through debt are less than the costs paid, it indicates that the company has not fully utilized its debt function and that its management capabilities are relatively poor. However, this needs to be analyzed in conjunction with the specific situation of the enterprise.

If using debt can create profits greater than the cost of debt, it can increase shareholder income, amplify the return on equity, and accelerate the company's development speed. Conversely, if the company does not control the debt ratio reasonably and the profits obtained cannot compensate for the cost of debt, then shareholder equity will be lost.

3. The reasons for the formation of high asset liability ratio

3.1. Characteristics of the industry

Compared to other industries, the real estate industry itself has significant regional and cyclical characteristics, and is also highly sensitive to policies. Compared with other industries, the real estate industry has a large initial investment in project development, a longer construction period, and a relatively long investment payback period. After obtaining the right to use the land through purchase, and carrying out preliminary design and planning, construction officially begins.

After construction is completed, promotion and sales are required, and all aspects and activities require capital investment. The demand for funds is very high, and the company's own funds are difficult to support the entire project development process. Therefore, many projects rely on external financing to solve the problem of tight funds.

3.2. The needs of enterprise scale and development

Most real estate enterprises have a certain scale and high credibility, making it easier for them to borrow from banks for financing. Compared to equity financing, the cost of debt financing is lower, and the interest generated by debt can be offset against taxes. Therefore, real estate companies generally tend to use debt financing, resulting in a higher debt to equity ratio.

In recent years, whether it is speculative demand or hard demand, it has reflected a signal that the domestic sales market demand is greater than supply, which has led to accelerated development of China's real estate industry and a continuous increase in development projects. Therefore, real estate enterprises have their own funds far from sufficient to meet the demand for project development investment funds, and they need to increase liabilities for project investment and development. As a result, the overall asset liability ratio of real estate enterprises continues to rise, which also leads to a continuous increase in their financial and economic risk levels, thereby affecting and impacting the healthy and sustainable development of enterprises and the industry.

3.3. Limitations of financing channels

The main source of external financing for real estate enterprise development projects is through bank loans. Many banks in China often bear high risks and pressures when providing loans to real estate enterprises. The Chinese government helps banks alleviate this pressure through macroeconomic policies, such as tightening monetary policy and increasing bank reserves. Therefore, the difficulty of real estate enterprises raising funds through banks is constantly increasing, making real estate enterprises bear more severe pressure in their business activities.

In recent years, China has basically established a relatively complete market economy system. However, the development of the real estate industry in our country has shown a distorted situation. Many real estate enterprises find it difficult to obtain sufficient financing, and the cost of obtaining

funds through bank channels is often relatively high. Generally, the company's own funds can only pay for part of the development project expenses. To ensure that the company's capital chain does not break and maintain the necessary funds for development, the company can only choose to borrow from banks.

3.4. Uncertainty of the policy

At present, financing for real estate enterprises is very difficult, and they are also in a critical period of transformation and upgrading. Therefore, in the long future, the operation of real estate enterprises will face huge challenges and high risks. This requires real estate enterprises to actively communicate and exchange with other industries, leverage the joint efforts of different industries and enterprises within the real estate industry, and promote the healthy and stable development of the real estate industry.

3.5. Real estate listed companies do not pay attention to the expansion of internal financing

In the theory of orderly financing, it is pointed out that enterprises should prioritize internal financing when financing, because the cost of using their own funds is the lowest. However, from the current financing structure of listed real estate companies, the proportion of the total amount of external financing as the source of funds is greater than that of internal financing.

Real estate listed companies have shifted from a "high debt, high development" business strategy to a "cash is king" stable business strategy, and have begun to attach importance to their profitability. If the profitability of a company increases, the proportion of its surplus reserve will increase, and there will be sufficient self-owned funds for project development.

4. Strategies for optimizing capital structure

4.1. Developing diversified financing channels

The mature real estate market abroad has relatively rich financing channels. Taking the United States as an example, its debt ratio is generally around 30%, while the debt ratio of Chinese real estate enterprises is around 70%, which is twice that of the United States. Of course, the economy of the United States is far from that of China, but we need to learn from its rich financing channels. China's economy is in a stage of rapid development, and the financing channels for listed real estate companies are also in the development stage. For a long time, China's financing channels have only focused on listing financing, bank loans, and a few corporate bonds, resulting in the current narrow financing channels for listed real estate companies.

Therefore, when expanding real estate financing channels, the country's financial policies can have a significant impact on its development. China's real estate market is a semi market-oriented industry under government regulation. While encouraging listed real estate enterprises to expand financing channels, the government must also improve the laws and regulations of the financial market and regulate operational behavior.

4.2. Enhancing the long-term and short-term solvency of enterprises

Debt paying ability refers to the ability of a company to repay its debts, which includes short-term debt paying ability and long-term debt paying ability. At present, the overall asset liability ratio of listed real estate companies is relatively high, but the proportion of short-term liabilities in these liabilities is relatively high, while the proportion of long-term liabilities is very small. This debt structure not only fails to fully utilize the leverage of liabilities, but also brings many unstable factors to the enterprise.

This phenomenon not only makes the capital structure of the enterprise extremely unreasonable, but also puts the enterprise at a relatively high financial risk. Once the enterprise's funding chain encounters problems, it may face a debt crisis. In response to this situation, real estate listed

companies should be fully prepared, on the one hand, actively expand financing channels, and on the other hand, improve the short-term debt repayment ability of the enterprise in the current situation, so as not to cause financial crisis for the enterprise. However, currently, it is quite difficult for listed real estate companies in China to obtain long-term debt. The requirements for issuing corporate bonds by enterprises in China are very strict, including the net assets, use of funds, and profitability of enterprises. Therefore, except for a few companies that can issue corporate bonds and can refinance, most real estate companies in China do not have enough ability to issue corporate bonds.

In such a severe financing environment, real estate listed companies not only need to actively seek new debt financing channels, but also strengthen their short-term debt repayment ability.

4.3. Enhancing the profitability of enterprises and the proportion of internal financing

Utilizing the company's own funds to invest in its production and operation has the intuitive benefits of being unaffected by external factors and having low costs. Increasing the proportion of internal financing is beneficial for optimizing the capital structure of enterprises. However, listed real estate companies in our country are small real estate companies that do not pay attention to the accumulation of their own funds and blindly expand. Therefore, although listed real estate companies have certain profitability, their capital structure is still unreasonable.

Therefore, real estate listed companies should choose projects with good development prospects instead of blindly following the trend. In the process of operation, enterprises should adopt diversified business models, avoid risks, adopt strategies to accelerate supply and sales, improve inventory turnover, accelerate capital flow, optimize capital structure, and achieve sustainable development of real estate listed companies.

4.4. Actively developing the financial market

The funds of listed real estate enterprises in China mainly come from seven aspects: domestic loans, utilization of foreign investment, foreign direct investment, self-raised funds, self-owned funds, deposits and prepayments from homebuyers, and other funds. There are many financing channels for enterprises, but the financing channels for real estate listed companies are relatively narrow, which is not conducive to optimizing the capital structure of real estate listed companies. Realizing diversified financing channels not only requires active exploration by enterprises, but also requires support from China's economic policies.

Firstly, it is necessary for the country to establish sound laws and regulations to provide a favorable economic environment for real estate listed companies; Secondly, it is necessary for the government to introduce corresponding incentive policies to encourage real estate listed companies to explore diversified financing channels because of sound laws and regulations.

Only in this way can real estate listings have more motivation to expand financing channels, which is conducive to optimizing the capital structure of real estate listed companies.

4.5. Establishing sound financial market regulations and systems for the real estate market

Due to the late start of marketization in China's real estate industry and the emergence of many non-standard and uncorrected issues in the development process, as well as the immature management of government policies related to real estate, the current laws and regulations on real estate financing in China are still very imperfect. To ensure the healthy and sustainable development of the real estate industry, it is necessary to rely on a sound financial legal system.

5. Summary

This article proposes five suggestions for optimizing the capital structure of real estate companies, focusing on the reasons for their high debt, including developing diversified financing channels, enhancing their long-term and short-term debt repayment capabilities, enhancing their profitability, and increasing their internal financing ratio.

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