Financing Risks and Preventive Measures for E-Commerce Corporates

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Abstract. The e-commerce industry has achieved tremendous development in the past decade. However, in this rapid development process, there are some problems that have caused huge hidden dangers, and financing is the most important one among them. Therefore, the topic of this article is the dangers and prevention methods of e-commerce corporations under different financing methods. The method of this paper is as follows: first, segment the financing models of e-commerce corporates, then combine the financing situation of several well-known e-commerce corporates in China, analyze relevant data, and discuss the possible problems under these financing models separately. The research shows that the short-term debt payment risk, financial leverage risk and investment decision risk are the major risks that have influences on the firms' financing, and the first two have a greater impact. To resolve these dangers, e-commerce firms can adjust debt structure, diversify financing channels and establish a sound risk prevention mechanism.

Keywords: E-Commerce Financing, Risk Prevention, Debt Structure.

1. Introduction

With the continuous development of economic globalization, the new business model of e-commerce is gradually becoming popular in today's society. Although China has taken many powerful measures, there are still many objective factors hindering the development of e-commerce enterprises. The development of e-commerce faces problems of non-standardization, inadequacy, and imbalance, with prominent issues of monopoly and unfair competition among platform enterprises. The core competitiveness of enterprises is not strong, the financing is not stable, and the external macro environment undergoes complex and profound changes [1]. Among them, the most prominent is a series of problems that e-commerce enterprises face in financing activities. The total financing amount of e-commerce is 22.62 billion yuan, with a sharp drop of over 80% [2]. It reflects that E-commerce firms in China have met big problems that they can't afford the risks of great financing. What's more, it reflects that some capitalists have been not optimistic about the development of E-commerce.

In addition, some e-commerce firms' overreliance on debt financing has led to a continuous increase in asset liability ratio, a decrease in resource integration, and low utilization of funds. Taking Suning.com as an example, Table 1 is about its liability information, as follows.

Table 1. Liability information of Suning.com

Year	Accounts payable	Notes payable	current liabilities	ratio of accounts payable and notes payable to current liabilities(%)	asset-liability ratio(%)
2016	12,038,435	17,477,129	68,464,936	43.11	49.02
2017	13,095,182	27,356,717	64,263,657	62.95	46.83
2018	47,071,017		93,696,656	50.24	55.78
2019	44,380,475	26,158,849	121,256,981	58.17	63.21
2020	31,051,472	21,021,224	124,601,727	41.79	63.77

From Table 1, it can be seen that the total accounts payable and notes payable of Suning.com account for over 40% of its current liabilities. Apart from the systemic reasons for the overall industry downturn during the 2020 pandemic, this proportion is generally on the rise. The financing effect of Suning.com is significant, and the financing scale also develops in the same direction as the enterprise scale. However, in the past five years, Suning.com's asset-liability ratio has been increasing year by year. In 2020, Suning.com's asset liability ratio reached as high as 63.77%, posing a huge hidden danger [3].

The purpose of this study is to analyze the significant risks and harms in financing for e-commerce enterprises by combining specific examples, and provide effective solutions.

2. Financing Types

This section will first introduce the types of financing, which are mainly divided into equity financing and debt financing. Equity financing is the process of raising capital through the sale of shares. Debt financing refers to the financing of enterprises through borrowing. The funds obtained from debt financing must first bear the interest of the funds, and in addition, the enterprise must repay the principal of the funds to the creditors after the loan expires.

2.1. Financial Leverage Risk

According to “Pecking Order Theory”, when a company finances a new project, its first choice is internal financing with the lowest financing risk and no financing cost, with the most typical being retained earnings. The second option is debt financing with low financing costs. If the debt ratio is at a high level and the company is in a financial crisis, then the stock financing method will be chosen [4]. Businesses frequently lack sufficient internal funding resources. Additionally, debt financing is typically less expensive than equity financing, and it can cut a company's cost of capital because the interest rate on debt is frequently lower than the return on equity. By boosting a company's profitability, the financial leverage effect can raise the return on shareholder stock. Debt financing can provide extra funding to expand an asset's size and yield. Consequently, e-commerce businesses frequently favor debt financing, which raises their level of financial leverage.

However, firstly, the financial leverage effect increases the financial risk of the enterprise. Debt financing places companies under higher financial leverage, meaning they bear a higher proportion of debt. When a company faces economic recession, intensified industry competition, or unfavorable market factors, the financial leverage effect may amplify the company's losses, leading to financial difficulties or even bankruptcy. Secondly, highly leveraged enterprises may find it difficult to bear the pressure of debt repayment when facing rising interest rates, economic recession, or adverse market conditions. Thirdly, market response and investor confidence. Highly leveraged enterprises will receive market attention and evaluation, and investors are more sensitive to their financial condition and debt tolerance [5].

Now we need to introduce a concept: financial leverage coefficient (DFL)=Change rate of earnings per share/change rate of pre interest and tax profit. The return on debt investment exceeds the debt interest rate, shareholders can gain a certain profit in the leverage effect, otherwise, it will reduce returns. This uncertain financial risk is mainly determined by the financial leverage coefficient. If the value of this coefficient is larger, the earnings per share will quickly change in the pretax profit margin, which will bring greater financial risk.

Table 2. Financial leverage coefficients of well-known E-Commerce companies from 2015 to 2017

	2015	2016	2017
Suning	1.48	1.06	1.67
JD	1.49	1.92	1.88
Gome	1.32	1.47	1.41
Vipshop	1.56	1.75	1.62

Table 2 shows the financial leverage coefficients of several well-known e-commerce companies from 2015 to 2017. We can find that e-commerce companies generally maintain high financial leverage. It means that e-commerce firms always meet high financial risks [6].

2.2. Short-Term Debt Repayment Risk

In interest bearing debt, long-term debt is much smaller than short-term debt, indicating that short-term debt financing is currently the main way for e-commerce enterprises to raise debt. Short term debt financing is flexible and can bring a large amount of financing funds to enterprises, but it has to bear the pressure of a large amount of due repayment. This means that once e-commerce companies encounter unexpected situations that may lead to a decrease in business volume, they may not be able to repay all their debts on time, so that they have to borrow from banks or other companies that provide loans. This will make it more difficult for the company to repay its debts in the future, and even lead to a vicious cycle.

Taking Suning.com as an example, since 2017, Suning.com has had negative operating cash flow, which has put significant pressure on the repayment of short-term loans. From the 2020 financial statements, although current assets are sufficient to repay short-term loans, most of them are restricted assets due to equity pledge reasons. Although Suning's borrowing is not much compared to its total assets, the repayment of short-term debts is still a pressure that Suning must face due to its current business and other issues. At the same time, Suning.com does not provide loans to banks that correspond to the size of the enterprise itself. The main reason for this is that Suning.com has suffered losses in its main business operations in recent years, which has made banks hesitant to open up credit limits for Suning.com [3].

In addition, for the current Chinese market, e-commerce business is dominated by companies such as Taobao, JD.com, and Pinduoduo, during Double Eleven or other times, these giant companies often lower prices to gain more sales volume. According to data, during the Double Eleven period in 2022, the sales volume of various e-commerce platforms accounted for 60.02% on Tmall, 27.86% on JD.com, 7.34% on Pinduoduo, and 4.77% on other platforms (as Taobao did not disclose the transaction volume, Taobao was not included in the calculation) [7]. The proportion of sales on other platforms is surprisingly less than 5%, indicating that non leading companies are very disadvantaged in this type of promotional activity. They have to lower prices like leading companies in order to reap the benefits of promotional activities, but market share is still inevitably encroached upon by large enterprises. This situation is highly likely to result in small and medium-sized e-commerce enterprises not being able to obtain sufficient cash flow to repay short-term debts in the short term, leading to the vicious cycle mentioned above, which will bring greater pressure to their later operations.

2.3. Investment Decision Risk: Market Risk

In the process of making investment decisions for enterprises, they are greatly affected by market risks, leading to unsuitable investment decisions. Market risk mainly refers to the impact of the external market economy environment on the development of enterprises, which leads to the inconsistency between the actual investment decision-making effect and the expected effect, resulting in a decrease in the operating level of enterprises and the inability to provide high-quality services [8].

Commerce enterprises face the problem of imbalanced supply and demand in the early stages of development, as well as the mismatch between product prices and actual demand. E-commerce companies often deliberately lower product prices in order to seize market share, spending a lot of time and effort to attract users and merchants to settle in. In this situation, the investment and production of the enterprise, as well as the actual and expected outcomes, will go against each other, posing a risk of bankruptcy. In addition, e-commerce companies often sell more popular products, but the market is time sensitive. These products may become unpopular immediately after a period of time, which can lead to overcapacity, product backlog, and losses.

3. Suggestions

3.1. Adjusting Debt Structure

E-commerce businesses should make the necessary adjustments to maintain a reasonable ratio of long-term to short-term debt, such as raising the percentage of long-term financing options like bonds receivable, in order to assure a more reasonable debt structure. In order to grow its bond market, China is taking a cue from capital-rich nations with their sophisticated management practices. E-commerce companies can take advantage of the policy's benefits by issuing long-term bonds to relieve the pressure on their short-term cash flow. Suning should continue to work closely with banks, keep credit leasing within an acceptable range, use long-term loans and bond issuance techniques, and increase the amount of non-current liabilities held by the company [3].

3.2. Diversified Financing Channels

The Chinese e-commerce retail sector ought to progressively give up its debt-based profit model, increase the percentage of self-operating retail businesses that operate independently, and go back to its original profit model, which is primarily based on sales profit rate and commodity turnover. Based on these principles, the sector should also continue to innovate its financing model. Create a strong and comprehensive social credit system, actively develop new commercial financing channels, and diversify financing risks and channels. E-commerce businesses must prioritize not just their own strategic development but also increasing their profitability by using retained earnings to increase the amount of capital they may raise internally. In order to obtain funds from the capital market during an extended period of sustained enterprise growth, it is imperative to actively expand external financing channels, including but not limited to credit-based bond financing and venture capital financing. In addition, the financing structure must be continuously optimized with an eye toward cost-effectiveness [9].

3.3. Establishing a Sound Risk Prevention Mechanism

The effective implementation of any work requires strict mechanisms as the foundation, standardized management of the thoughts and behaviors of staff, so that risks can be effectively controlled. In terms of financing risk prevention for enterprises, they should establish a sound risk prevention mechanism in combination with their own construction and development needs and market development conditions during development, and clarify that the return on financing work will not be obtained in the short term, but requires internal personnel to persist in the long term and obtain corresponding economic benefits. Therefore, enterprises need to increase their risk prevention efforts, transform the situation of "heavy financing and light management" when improving risk prevention mechanisms, put the financing and management of enterprises in the same position, and comprehensively supervise and manage financing decisions. Once problems are found, reliable measures need to be taken in a timely manner to solve them. Enterprises should implement risk prevention mechanisms in place to provide the correct direction and professional guidance for financing work, so that financing risks can be effectively controlled and other work of the enterprise can be safely and steadily carried out. At the same time, enterprises also need to improve their financing risk prevention mechanisms while organizing legal and regulatory training activities for internal management personnel, strengthening their understanding of laws and regulations, and providing favorable conditions for financing work [10].

4. Conclusion

By research, this paper finds that short-term debt payment risk, financial leverage risk and investment decision risk are the major risks e-commerce enterprises may meet during their financing process. This article analyzes the financing data of e-commerce enterprises such as Suning and Taobao, and points out that the existing common financing models may bring problems such as cash flow shortages and increased losses. Finally, based on literature, reasonable solutions are proposed: adjusting debt structure, diversifying financing channels, and improving risk prevention mechanisms. Due to significant differences in enterprise scale, development stage, and business scope among different e-commerce enterprises, the research significance of this article has certain limitations. However, the conclusion can provide certain reference value for other retail enterprises in the same industry to transform into e-commerce.

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