

Capital Supply and Financial Risk of Enterprises

—Research on the Relationship Between Shareholders and Banks and Enterprises

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ABSTRACT

Based on the clear definition of financial risk, this paper discusses the relationship between shareholders, banks and financial risk. The results show that: to a certain extent, shareholders' behavior affects the financial risk of enterprises. When the amount of capital contribution of shareholders is reduced or the related party transactions under the control of large shareholders occur frequently, the probability of financial risk of enterprises is higher; In the following four cases, bank enterprise relationship reduces the probability of financial risk: the enterprise is state-owned, the bank and the enterprise have established a long-term trading relationship; the enterprise appoints people who was worked in bank background as directors or senior managers; the financial institutions send directors to the enterprise, forming an effective third-party supervision.

Keywords: *financial risk, shareholder relationship, bank enterprise relationship*

1. INTRODUCTION

Based on Wang Zhu quan's view that enterprise is the collective choice of stakeholders and Financial risk is the uncertainty of the ability of financing activities to guarantee the demand for working capital of business activities, financial risk originates from the uncertainty of the ability of stakeholders to guarantee the demand for working capital caused by their influence on the supply or demand for working capital of enterprises [1]. According to the influence of stakeholders on the capital supply and working capital demand of enterprises, financial risk of enterprises can be divided into financial risk under the influence of investors and financial risk under the influence of non-investors.

The economic activities of enterprises are divided into business activities, investment activities and financing activities, which are collectively referred to as business activities. The development of enterprise's business activities needs funds and produces the total demand for funds; the financing activities provide funds for the development of business activities and form the total supply of funds. Since capital is the monetary expression of enterprise's economic activities, and the core of enterprise's economic activities is capital turnover, then the total capital supply of enterprise's financing activities

and the total capital demand of business activities constitute the whole of enterprise's economic activities. The working capital demand of enterprise's business activity is a part of the total demand of enterprise's business activity capital. What meets the demand of enterprise's working capital is not only the supply of working capital, but also the total supply of enterprise's capital.

When the total fund supply of enterprise financing activities can meet the total demand for funds of business activities, the enterprise will have sufficient funds and the business activities can be carried out smoothly. At this time, the enterprise is in a state of financial security. When the total fund supply of financing activities can not meet the total capital demand of business activities, but can still meet the working capital needs of business activities, the enterprise's daily business activities can be carried out smoothly, and the total capital supply can be increased by means of asset disposal and asset restructuring. At this time, the financial security status of the enterprise can still be maintained. However, if the total fund supply of enterprise financing activities can not meet the working capital demand of business activities, it will naturally be unable to meet the total capital demand of business activities of enterprises. The daily business activities of enterprises will be stopped and the capital

chain will be broken, and the enterprises will fall into financial risks. Therefore, the financial risk of an enterprise is more affected by the total supply of funds and the demand for working capital of business activities than by the total supply of funds and the demand for working capital of business activities. That is to say, it is more accurate to measure the financial risk of an enterprise by using the total supply of funds and the demand for working capital of business activities. Of course, the gap between the total supply of funds and the total demand of funds can also be regarded as the possible financial risk of an enterprise Signs of signs.

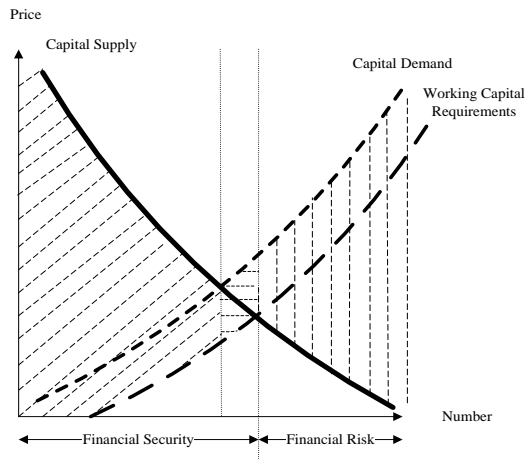


Figure 1 Financial Security and Financial Risk

2. THE MAIN CHANNELS OF ENTERPRISE CAPITAL SUPPLY

2.1. The main channels of enterprise's own capital supply

When an enterprise is formed through two levels of collective selection, the self-owned capital supply of the enterprise is the initial capital contribution of the shareholders, which is equal to the total amount of the paid in capital of the registered capital and the amount of the excess registered capital recorded in the capital reserve. After the establishment and operation of the company for a period of time, the company's own capital will increase the company's own accumulation, including other capital reserves and retained earnings due to the valuation changes of specific assets, on the basis of the previous shareholders' contributions. At this time, the enterprise 's own capital supply equals to the sum of shareholders' capital contribution and the enterprise' s own accumulation. Therefore, the supply of the enterprise's own capital is determined by the amount of the shareholder's contribution and the enterprise's own accumulation. However, at the time of the initial establishment of the enterprise, because the enterprise has not yet carried out business activities, the enterprise's own accumulation is 0. Of course, in the case of shareholders' collective choice of additional investment and recovery

of investment again, the amount of capital contribution of shareholders will also change accordingly, that is, the amount of capital contribution of shareholders = initial amount of capital contribution + additional amount of capital contribution - recovery of capital contribution.

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2.2. The main channels for enterprises to borrow funds

When the supply of the enterprise's own funds can't fully meet its working capital demand, the enterprise needs to borrow funds from the bank in the form of financing current liabilities and long-term liabilities. Among them, financing current liabilities are mainly short-term borrowings, and long-term liabilities mainly include long-term borrowings and enterprise bonds. Therefore, the main forms of the supply of borrowed funds are borrowing and issuing bonds. The borrowed funds are different from the self-owned funds. They are used for a certain period and need to repay the principal and interest when they are due. After the maturity of the borrowed capital, if the capital supply of the enterprise is enough to support the demand of working capital, the business activities of the enterprise will continue to be carried out smoothly. Otherwise, the enterprise needs to raise funds from the bank again to prevent the damage caused by the break of capital chain to the business activities of the enterprise [2].

The amount of enterprise loan is determined by the loan contract signed between the enterprise and the bank.

The bank determines the amount of the final loan obtained by the enterprise. It controls the initiative to approve the loan, recover the loan in advance and so on, which is not conducive to the enterprise's financing activities. It is one of the influencing parties of the enterprise's loan fund supply. Corporate bonds are issued by enterprises in accordance with legal procedures and agreed to repay the principal and interest within a certain period of time. The person or organization who purchases corporate bonds becomes the creditors of the enterprise. Their decision not to purchase or require repayment in advance affects the funds raised by the enterprise and the length of their use time, and is also the influencing Party of the supply of borrowed funds. Enterprises prefer to borrow money, which shows that the policies and preferences adopted by banks are more attractive to enterprises than those issued by enterprises themselves. The relationship between banks and enterprises has played a very positive role, leading enterprises to borrow money as much as possible.

3. THE SUPPLY OF SHAREHOLDERS' OWN FUNDS AND THE FINANCIAL RISK OF ENTERPRISES

3.1. The influence of the change of shareholder's contribution on the supply of enterprise's own capital and financial risk

After the establishment of an enterprise, both the additional investment and the recovery of the investment of the shareholders have affected the supply of the enterprise's own capital. Especially when the guarantee ability of the enterprise's financing activities to the demand for working capital of the business activities is at the critical point of financial risk, the recovery of the investment of the shareholders will reduce the supply of the enterprise's own capital, resulting in the insufficient supply of the enterprise's capital to meet the demand for working capital. The enterprise's capital chain is broken fall into financial risk. Generally speaking, when the demand for working capital of an enterprise must be the same as the amount of borrowed capital, the more capital the shareholders contribute, the more capital the enterprise supplies, the stronger the guarantee for the demand for working capital of an enterprise's business activities to obtain financing activities, and the greater the resistance to financial risks. To sum up, measuring the change of shareholder's contribution is an important aspect of identifying the financial risk of an enterprise, which can be measured by the change rate of shareholder's contribution.

3.2. The influence and financial risk of reducing the related party transaction of enterprise net profit on the supply of enterprise's own capital

Related party transaction is a double-edged sword. On the one hand, related party transactions bring about the savings of transaction costs and the full use of internal resources, reduce the risk of transactions, and ensure the quality of products. However, on the other hand, the prices and expenses of related party transactions are not determined by the market, but determined by both parties through negotiation. The related party transactions replace the market transaction behavior with the internal administrative instructions of the enterprise, which is divorced from the fair bidding environment of the market. What's more, there are large shareholders [large shareholders refer to the shareholders with large proportion of shares held by the enterprise; controlling shareholders refer to the shareholders with large proportion of shares held by the enterprise The proportion is enough to affect the daily operation of the enterprise and the decision-making of major events. The controlling shareholder must be the major shareholder, but the major shareholder is not necessarily the controlling shareholder. The possibility of manipulation. It can be seen that the related party transactions that reduce the net profit of enterprises mainly refer to the related party transactions under the control of major shareholders. The related party transactions under the control of large shareholders not only cause the change of stock price, but also affect the operation and financial indicators of the enterprise. Because accounting is the reflection of the economic activities of the enterprise, the related party transactions must be comprehensively reflected in the profits, cash flow or owner's equity (undistributed profits), and then affect the supply of the enterprise's own funds [3].

The purpose of different shareholders' participation in collective selection is to realize the appreciation of their own capital, but the interests of shareholders are also contradictory and conflicting. According to the amount of capital contribution, shareholders divide the control right and residual sharing right of the enterprise. Because the major shareholders hold the actual control right of the enterprise, the nature of economic man will urge them to make adverse selection by using information asymmetry to damage the interests of the small and medium shareholders, so as to maximize the common interests of shareholders while sacrificing the interests of the small and medium shareholders to maximize the interests of the major shareholders. Therefore, in the case of centralized or relatively centralized control, related party transactions under the control of large shareholders are considered as the main way for large shareholders to encroach on enterprise resources and infringe on the interests of small and medium shareholders.

4. THE SUPPLY OF BORROWED FUNDS BY BANKS AND FINANCIAL RISKS OF ENTERPRISES

The relationship between banks and enterprises is a kind of transaction relationship formed by two kinds of market transaction subjects: commercial banks and enterprises. Ross (1989) believes that bank enterprise relationship can help banks effectively solve the moral hazard of borrowing enterprises. There is information asymmetry between banks and enterprises. Borrowers have a more detailed understanding of their own financial situation, the expected return and risk of the project to be invested than banks. Therefore, banks are at an information disadvantage from the very beginning. They can only understand the internal information of borrowers from the external financial statements and other channels disclosed by enterprises. However, in order to achieve the purpose of obtaining loans, some loan enterprises will conceal the real situation or provide false information to the bank, so that the bank can make loan decisions based on incomplete and inaccurate information.

4.1. The influence of long-term transaction relationship between banks and enterprises on financial risk of enterprises

In order to obtain bank loans, enterprises must meet the scale, profitability and other index conditions set by banks, but this does not exclude the influence of other factors on enterprise loans. After the formation of an enterprise, in order to carry out business activities, it is necessary to borrow funds in addition to its own funds. The banks that provide loans to enterprises become the external stakeholders of enterprises because they do not participate in the formation of the first level collective choice of enterprises. They do not enjoy the control rights and residual sharing rights of enterprises, and rely on loan contracts to maintain the relationship between them. At this time, most of the loans obtained by enterprises are transactional-debts. For a long time, under this kind of transactional-relationship, some enterprises in our country are overdue and have a high proportion of bad loans, and even some enterprises have maliciously defaulted on the bank's principal and interest, and abandoned their debts, interfering with the normal operation of the bank. Of course, due to the imperfection of the financial mechanism in China, the unreasonable interruption of the loan contract by the bank will also damage the rights and interests of enterprises.

Blackwell and winters (1997) pointed out that enterprises can establish a stable relationship with banks, so that banks can obtain private information of enterprises to improve supervision efficiency, reduce transaction costs, and enterprises also reduce financing costs. Compared with non-state-owned enterprises, banks tend to maintain long-term trading relationship with state-

owned enterprises. This is because the state-owned enterprises are generally large in scale and supported by government departments, so the risk of default is small, and it is easier to obtain the trust of banks. Moreover, the state-owned enterprises usually maintain long-term cooperative relationship with many state-owned banks, which helps them to obtain bank loans. The non-state-owned enterprises are generally small in scale, operate for a short time, and have limited accumulation of their own funds, which can be used as loan collateral. With few assets and lack of government credit guarantee, bank loan discrimination is often encountered.

4.2. The influence of Bank Association on financial risk of enterprises

Bank Association means that the directors or senior managers of an enterprise have working experience in banks and other financial institutions. The Bank Association of enterprises promotes the information communication between banks and enterprises, and enhances the trust of banks to enterprises. Through private relations, banks can obtain the financial status, operating results and other relevant real information more quickly and reliably. The bank work experience of directors or senior managers can help them to accurately transmit the enterprise related information needed by the bank, reduce the borrowing threshold of the bank and obtain a higher credit limit. The information communication resolve the information asymmetry between banks and enterprises, and help enterprises improve the probability of obtaining loans. Booth and deli (1999) found that if a director or senior manager of an enterprise has banking experience, the asset liability ratio of the enterprise will increase. Allen et al. (2005) found that due to the imperfection of capital market and financial system in China, the informal financing channel of bank association plays a very important role.

4.3. The influence of the bank sending directors to the enterprise on the financial risk

It is a higher level of the combination of industry and finance that banks send directors to enterprises. From the perspective of banks, the object of bank loans is mainly enterprises. How the financial situation of enterprises has a decisive impact on the turnover of bank loans. Because the key to the flexible turnover of bank loan funds lies in the full recovery of loans to enterprises. By sending directors to participate in the operation and management of the enterprise, the bank has deepened the internal relationship between the borrower and the borrower, as well as the understanding of the strength and reputation of the enterprise. In this way, the bank can provide the enterprise with relatively loose loan policies and relatively low financing costs, so that the enterprise has enough borrowed funds, which is convenient for the enterprise to strengthen the financial management, so that

the enterprise's capital turnover is fast and efficient. High, increase the deposit of enterprises and enhance the solvency of enterprises, not only increase the source of bank loan funds, but also can timely recover the matured loans, forming a virtuous loan fund cycle. From the perspective of enterprises, the existence of bank dispatched directors not only alleviates the difficulty of enterprise borrowing, but also, as an independent third party, forms certain supervision over the daily business activities of enterprises, effectively prevents the collusion of board members, reduces the phenomenon of other directors and senior managers occupying the working capital of enterprises, and ensures the business activities of enterprises. Efficiency and order reduce the financial risk of enterprises.

4.4. The influence of bank credit on financial risk of enterprises

Bank credit refers to a kind of operation mode in which a bank, depending on its own strength and reputation, provides funds for an enterprise, or undertakes debts on behalf of an enterprise, and the enterprise pays its principal and interest back. Bank credit takes credit as the link, and realizes the combination of industry and finance through the creditor's right and debt relationship between banks and enterprises. With the development of economy and the expansion of business scale, the leverage of bank credit becomes more and more important. From the practice of foreign enterprises, the average asset liability ratio of many large-scale foreign enterprises is gradually increasing, and more and more attention is paid to obtaining external funds. The liabilities formed by these external funds mainly come from some relatively fixed large banks, forming a group enterprise focusing on the liabilities of large banks.

5. CONCLUSION

Shareholders and banks are the main suppliers of corporate capital. Under certain circumstances, they affect the probability of corporate financial risk.

The supply of enterprise's own capital refers to the capital provided by the internal stakeholders and the capital accumulation formed through the business activities of the enterprise. The change of shareholder's contribution and the speed of enterprise's own accumulation affect the supply of enterprise's own funds, the guarantee of financing activities to the working capital demand of enterprise's business activities, and the fluctuation of enterprise's financial situation. When the demand for working capital of an enterprise is certain, the withdrawal of investment by shareholders or the behavior of major shareholders in hollowing out the enterprise will reduce the supply of the enterprise's own capital, thus reducing the supply of the enterprise's capital, which may result in the situation that the supply of the enterprise's capital cannot meet the demand for working capital, and

increase the probability of the enterprise's financial risk. With the decrease of internal stakeholders' contribution, the probability of financial risk is higher. The related party transactions under the control of large shareholders occur frequently, and the probability of financial risk is high.

By establishing a stable bank enterprise relationship with the bank, the enterprise solves the problem of borrowing difficulty to a certain extent, obtains more loans with lower financing cost, guarantees the working capital demand of business activities, and reduces the probability of financial risk. When the demand for working capital of an enterprise is certain, the innovation of bank enterprise relationship is realized by changing transaction debt into relationship debt, or introducing personnel with bank working experience as directors or senior managers. The combination of industry and finance has broken the traditional mode of equity penetration. The dispatch of directors and bank credit from banks to enterprises is helpful to solve the problem of insufficient funds borrowed by enterprises and ensure the normal operation of enterprises. When the enterprise is state-owned, the bank is willing to establish a long-term trading relationship with the enterprise, and the probability of financial risk is low. When an enterprise introduces a person with a banking background as a director or senior manager, it forms a bank association, and the probability of financial risk is low. Financial institutions send directors to enterprises, forming an effective third-party supervision, and the probability of financial risk is low. There are bank loans or supply chain financial loans in enterprises, so the probability of financial risk is low.

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