ATLANTIS PRESS
Advances in Economics, Business and Management Research, volume 203
Proceedings of the 2021 3rd International Conference on Economic Management and Cultural Industry (ICEMCI 2021)

Regulation on China Internet Finance: An Analysis of Ant Group's IPO Failure

Xintong Feng[1,*,a,†] Xiaoyi Wang[2,*,b,†] Ziming Yang[3,*,c,†]

[1] *College of Liberal Arts & Sciences, University of Illinois Urbana-Champaign*
[2] *College of International Economics and Trade, Shanghai University of International Business and Economics*
[3] *College of Liberal Arts & Sciences, University of Illinois Urbana-Champaign*
[*]*Email:* [a]*xf9@illinois.edu,* [b]*695837592@qq.com,* [c]*zimingy2@illinois.edu*
[†]*These authors contributed equally.*

ABSTRACT

Internet Finance is a new financial business model and gets applied more and more in China with the development of the internet. Although it provides is more convenient and faster service, internet finance also brings more system risks to China's financial market. Especially after the IPO failure of Ant Group, more attentions are focused on China's Internet financial regulatory system. The purpose of this article is to study whether it is over-regulated in China's Internet Finance industry. By reviewing other researches on China Internet Finance and SWOT analysis of Ant Group, the study concludes that the Ant Group is eligible for IPO. Its IPO failure is the need of the China finance market to control the system risks. But the strict supervision is not overregulated since it is helpful to protect consumers and investors by decreasing the system finance risk, maintaining the order of the internet financial market in China, and increasing economic vitality. The regulation is not just for Ant Group but for the entire Chinese Internet finance industry.

Keywords: *Internet Finance, China, Regulation, IPO, Ant Group, SWOT*

1. INTRODUCTION

Internet Finance refers to a new financial business model. Traditional financial institutions and Internet companies provide more efficient fund transfer, payment, and investment services by using Internet technology and information communication technology. Internet Finance is more convenient and faster in most finance activities. With the popularization of the Internet and technological innovation, Internet Finance has also developed rapidly in China. According to the 2020 China Internet Finance White Paper, the growth rate of China's Internet finance industry was as high as 48.9% from 2014 to 2019 [1]. Following China's inclusive finance and consumption stimulus development, the demand for credit financing is continuously rising. The China Finance Association predicts that by 2023, the transaction volume of China's Internet finance industry will exceed 5 million100 million yuan [1].

In the past few decades, China's traditional financial services, which refers to the financial activities only with the businesses of deposits, loans, and settlement, has always used a relatively single business product and service to create 80% of financial profits with 20% of high-end customers [2]. While, unlike traditional finance, Internet Finance upholds the concept of inclusive finance, widely serving mass customers and keeping growing through rapid financing, microfinance, and mobile payments. Under the internet finance model, customers can break through the constraints of time and region to find the financial resources they need. Its services are more direct with a broader customer base. The number of users of Internet finance in China has exceeded 1000 million [2]. And the fast-developing Internet finance has also gradually changed the structure of the traditional financial industry in China, with the transaction volume of internet finance increasing year by year.

However, due to the explosive growth of Internet finance, its chaotic market competition environment, internal transactions, and monopoly issues have become increasingly prominent. At the same time, because Internet finance is highly dependent on big data, cloud computing, and other emerging technologies, its technical risks continue to increase. Once financial risks occur, they will be more contagious and bring greater systemic financial risks. Therefore, it brings more challenges to China's financial market transaction order, the security of funds, and the financial system. However, most of the regulatory policies of China's Internet financial industry are based on traditional financial models, and risk control is not perfect enough to adapt to the rapid development and change of the industry. To improve the passive status of the regulatory model, China has continuously introduced corresponding macro policies as well as micro rules, such as Credit Financing Standards, Initial Public Offering (IPO) rules for technology financial companies, and Third-Party Payment Rules, to better control the systemic risks of China's Internet finance. But these policies have also made many practitioners question whether there is over regulation. A typical case influenced by these policies is the IPO failure of Ant Group, which provides microfinance services and is an influential company in China's Internet finance industry.

IPO refers to an enterprise that sells its shares to the public for the first time. It can help enterprises raise funds to attract investors, enhance liquidity, improve the corporate structure, and facilitate management. In China, only joint-stock companies with a registered capital of more than 30 million yuan have the basic qualifications to apply for IPO. Before applying, they must have been in business for more than 3 years and gain an annual net profit of 30 million yuan without change in senior management in the past three years. After the China Securities Regulatory Commission is approved, the enterprises can get IPO successfully on the Shanghai Stock Exchange, Shenzhen Stock Exchange, or Hong Kong Stock Exchange. On October 21, 2020, the China Securities Regulatory Commission disclosed that it approved the IPO registration of Ant Group. But on the evening of November 3, Ant Group issued an announcement and suspended its IPO.

Scholars hold different views on the IPO failure of Ant Group. Wang argued that it was because of their irregular accounting and unreasonable information disclosure [3]. Jiang indicated that Ant Group has a high risk of mixed operation, which does not meet the standards of the China Securities Regulatory Commission [4]. While Zhao believed that the failure was due to the strict policy restrictions from the regulatory needs of China's internet finance industry [1].

So, does the failure of the IPO of Ant Group arise from internal causes such as irregular accounting mentioned above? Or external causes such as over supervision? The most recent researches focus on a single aspect of analysis. Based on these controversies gap, this study would provide a SWOT analysis to research the multiple causes of the IPO failure of Ant Group and whether there is over supervision in China Internet Finance. This article would examine in more detail in two parts to test the hypothesis that the IPO failure of Ant Group is due to the supervisions, but the supervisions are not excessive. The first part is a literature review on China Internet Finance. The second part is the analysis of Ant Group and its IPO failure. At the end of the article, the study would get some conclusions on supervision of China Internet Finance.

2. LITERATURE REVIEWS

Many researches have been carried on China Internet Finance, related to discussions of concepts, risks, advantages, supervision, and the impact.

2.1. Traditional Finance

Traditional finance refers to the daily deposit, loan, and settlement business handled by the banking industry. Customers and bank staff directly conduct business transactions face-to-face, with a fixed location and fast information feedback. Guo stated that it is the first choice for the elderly and some middle-aged people because of the higher reliability. While due to its relatively small coverage, high operating costs, and complicated process, traditional finance is getting more inefficient [5].

2.2. Internet finance

Internet finance mainly refers to providing customers with more diversified financial business content through the Internet platform, such as bonds, stocks, insurance, financial products, etc. With the development of the Internet, the advantages of Internet finance are gradually manifesting. It is not a simple integration of the traditional financial and the Internet but will make the finance activities more efficient. With its more applications in a different industry, internet finance is divided more detail into 8 main types, including traditional financial internalization, mobile payment, and third-party payment, internet currency, online credit investigation, online insurance, P2P network loans, crowdfunding financing, and the application of big data in securities investment [6].

2.3. Risk of Internet finance

However, because of the complexity of Internet finance, Zhu and Chen believed that the promotion of Internet finance has a potential impact on financial stability. Without changing the nature of finance, it is more dependent on the accuracy of data and network effects [7]. Li analyzed the vulnerability of individual institutions, the path of risk transmission, information asymmetry, and the rapid expansion of the financial technology market and believed that Internet finance would lead to systemic risks. Tsai and Peng also believed that the application of Internet finance would aggravate the spread of financial risks and bring risks with new non-financial factors [8]. However, Liu stated that Internet finance is a sunrise industry that can improve financial vitality. The Chinese government should actively encourage companies with a good reputation, sufficient funds, and legal procedures to join the Internet finance industry [9].

2.4. IPO and Supervision

Considering the convenience and high stability risks brought by Internet finance, China has continuously introduced more strict supervision, especially on IPO. Lu put forward that IPO refers to an enterprise that sells its shares to the public for the first time. It can help enterprises raise funds to attract investors, enhance liquidity and improve the corporate structure and facilitate the management. Still, the over-regulation on IPO may stifle Internet financial innovation and vitality [10]. Li and Liu believed that the current supervision of China Internet Finance is too rigid. Under the principle of flexible supervision, the policies should be appropriately liberalized, adaptive supervision on IPO should be pursued, and the legalization of Internet financial supervision should be actively promoted [1, 9]. Yi thought that these supervisions are better for the development of China Internet Finance. The protection of consumers and investors will help promote the long-term sustainable development of Internet finance companies [11]. She believed that strict supervision is not the root cause of IPO failure. Most internet finance companies are traditional loan shark companies under the cloak of Internet technology, and the IPO itself has relatively high financial risks [11]. While Zu argued that the IPO failure is affected by the unstandardized supervision, the regulatory authorities have not formed a standardized understanding of Internet finance companies, which has caused difficulties in the classification and failed to reach a consensus on the qualitative nature of these companies [12].

Based on the reviews of all parties, scholars analyzed the development of Internet finance, affirmed the positive role of financial technology, and pointed out the coexistence of new risks and benefits in the development of Internet finance, arguing differently on the supervision.

3. SWOT ANALYSIS OF ANT GROUP

Ant Group is founded in 2014, mainly engaged in mobile payment and microfinance services. Its predecessor is China's largest mobile payment platform-Alipay. Ant Group once became the world’s largest financial “unicorn”. Only in 2019, the year before the IPO, it made a net profit of 17 billion yuan, according to Ant Group’s financial report. And in the six years before the IPO, Ant Group has created more than 70 billion yuan profits [13].

On July 22, 2020, Ant Group disclosed its letter of intent and announced the issuance plan. On September 18, the IPO Committee of the Shanghai Stock Exchange Science and Technology Innovation Board approved the IPO application of Ant Group. But on the evening of November 3, Ant Group issued an announcement and suspended its IPO due to the changes in the regulatory policies.

3.1. Strengths

Ant Group is China's largest internet finance service provider and has a huge active user base. Because of its extensive recruitment of top internet and financial talents, Ant Group has developed the best domestic Internet security system and ultra-high cloud computing capabilities in China. It can handle users’ financial transactions quickly, safely, as well as accurately. Starting with Alipay's mobile payment, it has also built a comprehensive service platform consisting of mobile payment, internet mic-loan, and digital life. Until June 30, 2020, the total domestic and overseas payment through Ant Group has reached 118 trillion and 621.9 billion yuan [13]. Ant Group has promoted the development and convergence of the Financial Internet market in China more quickly, connecting digital payments in more than 200 countries and regions worldwide, involving 1 billion users, 80 million merchants, and 2,000 financial institutions partners [13]. More companies related to the payment process can obtain users’ transaction data and habits. Therefore, the Internet Finance market can better understand what customers need based on the collected data, then provide personalized and differentiated services.

3.2. Weakness

The most obvious weakness is the fund risk. More than half of Ant Group's profits come from small loans. Currently, about 500 million individuals have obtained micro-loans, amounting to up to 1.73 trillion yuan. However, only 20 million normal operators can access the credit services, with the amount only about 400 billion yuan [13]. Therefore, the loan ratio is extremely unbalanced. And in terms of sources of lending funds, Ant Group mainly engages in cooperation with commercial banks. Its funds are less than 2%, so the sources of lending funds are also extremely unbalanced [13]. The unbalanced finance means that it has very high leverage and a weak ability to resist financial risks, which would also lead to a higher risk of financial crisis chain reaction in China's whole finance internet market.

3.3. Opportunities

The best opportunity is its IPO. If Ant Group launched IPO successfully, it will raise more funds and reduce its debt ratio, reducing excessive reliance on banks and the risk of capital chain shortages. The credit rating of Ant Group will also be improved. At the same time, the IPO can enhance the company's brand, help Ant Group gain greater user trust and market share, promoting the improvement of the company's management level.

3.4. Threats

While most threats come from the supervision and IPO risk, the strict supervisions restrict the expansion of financial services in Ant Group. And Ant Group also has to face the operation uncertainty brought from the change in policies. Under the China Securities Regulatory Commission Announcements about new IPO Rules for Internet Finance Companies, Internet finance companies must contribute no less than 30% in their loan business funds. While the Ant Group is only about 2%, so the IPO of Ant Group is getting harder. Even if Ant Group can launch IPO successfully, the IPO may bring more risk because it sharply increases the control risk of fund balance and leverage in return, since the IPO valuation of Ant Group is up to 2.1 trillion. It can affect the total internet finance market obviously during Covid-19 in China Economy[13].

4. RESULTS

Based on the SWOT analysis, Ant Group itself is eligible for IPO as it has enough profits. It can help gain greater user trust in China's Internet Finance market, promoting the development and convergence of the Financial Internet market in China more quickly. But it also brings a very high chain crisis risk to the whole Internet Finance market due to its huge financial volume and extremely high leverage. Especially the current economy is the downturn in China because of the Covid-19.

5. DISCUSSIONS

The IPO failure of Ant Group is more because of the supervisions. These supervisions are not an over-regulation to stifle innovation but a market risk control because of its extremely high leverage. Under new IPO Rules for Internet Finance Companies issued by the China Securities Regulatory Commission, Internet finance companies must contribute no less than 30% in their loan business funds. The rules affect most IPOs of Internet finance companies in China. Like Ant Group, other China’s major Internet finance companies, such as JD.com, Xiaomi, and 360 Group, are all far from the required levels. To launching IPO successfully, they must control their high leverage and adapt to new regulations because the government must control the system finance market risk through strict supervision. These strict supervisions are helpful to protect consumers and investors by decreasing the system finance risk, maintain the order of the internet financial market in China. Only when the benefits and risks get balanced can the IPO of Internet Finance Companies in China get healthy and long-term development, increasing economic vitality.

The conclusions of this article are a supplement to previous researches on the IPO of Internet Finance companies in China. Since most of them focus on analyzing companies’ internal causes, such as unreasonable information disclosure or irregular finance accounting, while without enough consideration of the strict supervision effect on IPO failure. The research indicates that companies such as Ant Group are eligible for IPO, but the market needs strict supervision to control the risk. The changes in financial regulation are not just for Ant Group, but the entire Chinese Internet finance companies.

But the analysis in this article is only based on Ant Group. Although Ant Group is very representative, more extensive analysis is needed since Internet finance in China is very complex. And the future study may focus more on how the internet finance companies adapt to new regulations in China.

6. CONCLUSIONS

This article has presented multiple reviews on China Internet Finance. It takes a SWOT analysis of Ant Group to study whether the failure IPO of Ant Group is due to the strict supervision and whether it is over-regulated on Internet Finance in China. By taking the analysis and discussions, this research identifies that although Internet Finance brings convenient and faster service, it also brings more system risks. The IPO failure of Ant Group is due to the strict supervision because the China regulatory authorities have to control the high leverage and decrease the system risk of China finance market. But the internet finance market in China is not over-regulated since these regulations help maintain the order of the internet financial market in China, protect the consumers and investors, and get healthy and long-term development. The conclusions of this article are a supplement to previous researches on the IPO of Internet Finance companies in China because most of the previous works focus on the analysis of companies’ internal causes. And the SWOT analysis can be used fundamentally in more similar cases analyses. Although Ant Group is very representative, more extensive analysis is needed since Internet finance in China is very complex. There can be more detailed and accurate research on the regulatory status of China's Internet finance regulatory status by doing more analysis. Thus there would be more reasonable policy recommendations put forward.

REFERENCES

[1] S. Zhao, Research on the Risks and Supervisions of Internet Finance in China, Technology and Economic Guide, 11 (201) 3-4. DOI: https://doi.org/10.3969/j.issn.1004-9207.2015.17.033

[2] Y. Feng, Development and Research Review of Internet Finance. Journal of University of Electronic, Science and Technology, 34 (2018) 15-17.

[3] L. Wang, Internet Financial Supervision under Separate Supervision, Technological Economy and Management Research, 143 (2019) 33-34.

[4] M. Jiang, Suggestions on China's Financial Technology Regulatory Policy, Financial Sight, 124 (2021) 23-26. DOI: https://doi.org/10.12245/j.issn.2096-6776.2021.05.18

[5] H. Guo, Case Analysis of Risk Generation of Online Financial Platform, Brand and Standardization, 13 (2014) 1-3.

[6] Z. Gao, Countermeasures of China's Internet Finance Development, first ed., Chinese Industry and Economy, 2020.

[7] R. Zhu & X. Chen, Regulatory Response Strategies of Fintech Company, Financial Forum, 154 (2016) 43-44.

[8] C.h. Tsai & K. J. Peng, The FinTech Revolution and Financial Regulation: The Case of Online Supply-Chain Financing, Cambridge University Press, 2017. DOI: https://doi.org/10.1017/als.2017.8

[9] M. Liu, Potential Risks of Internet Finance, Southern Finance, 65 (2020) 32-33.

[10] C. Lu, Why is the IPO of Ant Group Suspended? China Academic Journal Electronic Publishing House, 33 (2020) 12-14.

[11] R. Yi, Risk Analysis of Financial Technology Company and Supervision Countermeasures, Financial Forum, 21 (2021) 11-12. DOI: https://doi.org/10.16127/j.cnki.issn1003-1812.2021.03.008

[12] Y. Zu, Ant Group's listing suspension-over-regulation or reining in the precipice, Monthly Hainan Finance, 103(2021) 4-7. DOI: https://doi.org/10.3969/j.issn.1003-9031.2021.04.005

[13] Ant Group, Ant Group Prospectus, 2020.