ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

Study on Financial Risk Identification and Control of Y Enterprise

Yuhan Zhang

School of Economics and Management, Xi'an University of Posts & Telecommunications, Xi'an, China

Abstract: *With the development of society, the business of enterprises is also expanding with the expansion of the scale. However, due to the existence of various uncertain factors in the process of enterprise operation, financial risks will inevitably occur. Although this risk cannot be avoided, it is controllable. Early identification of enterprise risks can prevent small risks and avoid greater losses by controlling the identified risks.*

Keywords: *financial risk; identification; evaluation; control*

1. Introduction

1.1. Research background and significance

With the advent of the aging society and the enhancement of public health awareness, the pharmaceutical industry is an indispensable part of our economy, and this industry has a lot of room for development in the future, but the pharmaceutical industry is also a high-risk industry, large investment cycle, long research and development failure rate is high. At the same time, there are numerous enterprises because of poor management and major financial problems or even be delisted. The competition in the pharmaceutical industry is also increasing year by year, if you do not improve your anti-risk ability ,it is easy to be swallowed up by competitors in the fierce market competition.

When the financial risk has not brought losses to the enterprise, it will be identified, the existing risk control, the risk is still in a small stage will be controlled, to avoid the risk aggravation to bring losses to the enterprise, so as to make the enterprise better operation and development.

1.2. Research status at home and abroad

Abroad on the study of financial risk has been a long time, many scholars abroad think before the risk management requires the recognition of financial risk accurately and objectively, so as to manage the risk, in order to avoid damage to the enterprise, but also some scholars think that financial policy is not reasonable for the enterprise financial risk to have planted a seed. At the same time, part of the foreign scholars believe that if only blindly expand business of accounts receivable of whether it will also trigger a financial risk, at the same time, some scholars argue that corporate cash flow turnover, debt which is unable to repay or repay debts to affect the enterprise cash flow is a very big part of the financial risk.

Compared with the research on financial risk at home and abroad, some domestic scholars believe that financial risk is caused by the deviation of financial conditions and financial results from expectations caused by various uncertain factors in the operation process, while some scholars believe that financial risk is mainly caused by a large number of liabilities. On the control of financial risk, some scholars put forward that the control of risk should be more to prevent financial risk, managers should have financial risk to employees to establish a sense of financial risk prevention, the establishment of financial risk early warning mechanism will be the risk in the seedling stage to eliminate.

ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

2. Financial risk related theory

2.1. Definition of financial risk

There are currently two understandings of the definition of financial risk: The first is a broad sense of financial risk, financial risk in the broadest sense of the term refers to the process of enterprises in business of all kinds of unpredictable and uncontrollable factors, enterprise financial activities related deviating from the expected, moreover is affecting business follow-up, the financial risk of the generalized throughout the enterprise's financing activities, investing activities, operating activities and income distribution. The second kind of chivalrous financial risk refers to the risk caused by the enterprise's debt operation and the enterprise's inability to repay the debt [1].

2.2. Characteristics of financial risk

(1) Objectivity: For any enterprise, financial risk exists objectively and cannot be eliminated [2]. This is because there is uncertainty in various activities carried out by enterprises, and this uncertainty will bring financial risks. We can only try our best to reduce financial risks and avoid the aggravation of financial risks to bring greater losses to enterprises.

(2) Uncertainty: the market environment of an enterprise is not immutable but complex and changeable [2]. At the same time, there are some factors beyond the control of the enterprise itself, which will lead to the complex and changeable financial situation of the enterprise, and it is difficult to predict, which makes the financial risk show the characteristics of uncertainty.

(3) Comprehensiveness: in the process of financing, investment, operation, income distribution and other activities of the enterprise, there will be the possibility of financial risks. It can be said that any activity of the enterprise will bring financial risks, and the financial activities of the enterprise will affect each other and have mutual links. Therefore, the financial risk of the enterprise has comprehensive characteristics.

2.3. Classification of financial risks

According to the activities carried out by the enterprise, financial risks can be classified into the following categories.

(1) Financing risk

According to the flow of funds, financing activities are the beginning of the flow of funds. There are two aspects of enterprise financing, one is equity financing, which is the input of the owner, and the other is Creditor's rights financing, which comes from banks and other financial institutions. For equity financing, that is, the part invested by the owner is the enterprise's own funds, and the shareholders of this part of funds need to bear the benefits and risks together with the enterprise. When the enterprise's management and operation are better, the investors can obtain more benefits. On the contrary, when the enterprise has less income or even losses, investors will not be able to obtain the corresponding income. However, the funds raised through debt have a definite repayment period and a definite repayment amount. If the enterprise does not have enough funds to repay the maturing debt, it is easy to cause financial risks.

(2) Investment risk

The main reason for investment risk is that an enterprise invests a sum of money in the research and development of a project or product, and the return on investment is uncertain, which makes the output less than the input easily. In addition, although there is expected return on investment, there are too many uncontrollable factors and some projects have a long cycle. This is easy to cause investment risk.

(3) Operation risk

The operation risk of the enterprise refers to whether the working capital of the enterprise can meet the needs of daily business activities, which mainly depends on the speed of fund collection. In general, operating risk is mainly due to the low level of inventory and accounts receivable management. Inventory risk mainly refers to the risk that inventory can not be quickly realized due to the differences between production and sales, so that the enterprise's capital is occupied. The causes of accounts receivable risk mainly because of the customer's operation situation and the uncertainty of credit rating, making enterprises facing payment recovery time and the amount of uncertainty risk, if the account for

ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

a long time cannot recover makes enterprise funds occupied by the other firms and had a higher chance of producing bad debt losses to the enterprise.

(4) Risk of income distribution

When an enterprise generates income and distributes it to investors, such risk will occur. If the proportion of investors is overly high, the proportion retained by the enterprise will be reduced, which will affect the sustainable development of the enterprise cash flow and affect the development of the enterprise. However, if the proportion of income allocated to investors is overly low, it will affect the subsequent financing of the enterprise and cause a negative impact on the subsequent financing.

This paper will identify the financial risks of Y enterprise from three aspects: financing, investment and operation.

2.4. Control of financial risk

The purpose of financial risk management is to avoid the loss of the enterprise, the enterprise in the identification of financial risk after the identification of the financial risk out of the financial risk control, to avoid the expansion of the risk to bring losses to the enterprise.

(1) Financial risk reduction

Financial risk reduction here refers to the reduction in the probability of the occurrence of potential risks. It mainly relies on the formulation of risk control and the effective implementation of measures to reduce the possibility of risk occurrence [3].

(2) Financial risk transfer method

The financial risk transfer method refers to the enterprise financial risk existing in the transfer but not the original of the financial risk of lower [3], simply because of the existence of enterprise financial risk shifted to other companies. For example, you can buy insurance to transfer financial risks, in order to reduce the financial risk of losses to the enterprise.

3. Financial risk identification of Y Company

3.1. Identification of financing risk

Financing risk is one of the risks commonly faced by enterprises in the process of operation, which is mainly because enterprises, through debt financing and debt maturity, are unable to repay the risk. The pressure on companies to repay their debts varies depending on the type and maturity of the debt and the use of the funds raised. Therefore, enterprises should consider not only the funds raised but also the repayment period when financing through debt, as well as the use of the funds raised before financing to do a good job in planning, to avoid short financing and long use. The way of enterprise financing of our country mainly can be divided into: equity financing and debt financing. It mainly includes absorbing direct investment from investors, issuing new stocks, utilizing previous surplus reserves, obtaining loans from banks and issuing bonds. Capital raised through equity is not repaid, but capital raised through debt is repayable within a certain period of time[4]. From the short-term and long-term solvency by time to analyze the solvency of enterprises. The solvency can be measured by current ratio, quick ratio and asset-liability, ratio[6].

Table 1: Y Company financing risk identification table

Project	2021	2020	2019	2018	2017
Current ratio	0.83	0.76	0.74	0.84	0.92
Quick ratio	0.68	0.59	0.58	0.65	0.70
Asset-liability ratio	67.45%	66.12%	68.76%	69.34%	75.95%

Data source: Financial statements of Y Company and NetEase Financial website

It can be seen from Table 1 that the current ratio of company Y is in a state of fluctuation, declining continuously from 2017 to 2020, although it is slightly increased in 2021, it is still in a state of decline compared with 2017, and it is generally considered that 2 is the appropriate indicator. However, it can be seen from Table 1 that the current ratio of company Y in recent years is consistently much lower than the accepted value. Compared with the current ratio, the quick ratio is the current assets that can be quickly realized except inventory, which can better reflect the quick realization ability of an enterprise. This index is widely considered to be appropriate when 1. The quick ratio of Y company has

ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

been fluctuating in the past five years. From 2020 to 2021, there is a significant increase, but compared with 2017, it is still a decrease. Although the decrease is small, the quick ratio of Y company has been lower than the accepted standard value in the past five years. Asset-liability ratio is a measure of long-term solvency indicators of numerical said the greater the enterprise's long-term debt paying ability is poor, although asset-liability ratio is roughly five years Y company is in a state of decline, but compared with the standard 50% its asset-liability ratio is on the high side, although doing so can ensure the equity of enterprises will not be diluted but bring larger repayment pressure. Therefore, it can be seen that Company Y has shown certain risks in its solvency, which will bring about financing risks to Company Y.

3.2. Identification of investment risk

In the process of investment activities, due to a variety of uncontrollable factors, the income generated by investment will deviate from the expectation. And the income originally has the unpredictability, the general investment period is also relatively long and other characteristics, so that the investment risk exists objectively. This paper uses return on equity, net interest rate on total assets and net profit margin on sales to identify Y company's investment risk.

Table 2: Y Company investment risk identification sheet

Project	2021	2020	2019	2018	2017
Return on equity	2.39	0.31	4.57	5.62	4.89
Net interest rate on total assets	0.75	0.09	1.41	1.81	0.90
Net profit margin on sales	1.17	0.15	2.07	2.70	1.62

Data source: Financial statements of Y Company and NetEase Financial website

The higher the value of return on equity is, the stronger the enterprise's ability to make profits with its own assets is. On the contrary, the higher the value of this index, the stronger the enterprise's profitability is, while the lower the value of this index, the weaker the enterprise's profitability is. The greater the value of the net interest rate of the total assets of the target companies make use of all assets, profitability is stronger, the smaller the index numerical words that all companies use assets profitability is weak, the index value rise suggests that companies with total assets profitability stronger, and with all their assets if fall suggests that enterprises profitability. The higher the value of net profit rate on sales is, the stronger the enterprise's ability to obtain net profit from operating income is; the lower the value is, the weaker the enterprise's ability to obtain net profit from operating income is. The rise of this index indicates that the enterprise's ability to obtain net profit from operating income is becoming stronger in a period of time. It can be seen from Table 2 that the return on equity of Company Y has always been in a state of fluctuation, and the fluctuation range is large in some years. In 2020, the return on equity directly decreased from 4.57% in 2019 to 0.31%, although it recovered somewhat in 2021, it still decreased twice compared with 2017. It indicates that Y company's profitability in using self-used assets is unstable and has declined in recent years. Although the value of return on total assets is quite different from that of return on equity, its upward and downward trends in the past five years are generally similar to that of return on equity. It declined substantially from 2019 to 2020 and then began to rise in 2021, and although it increased, it still declined slightly compared with 2017. This also indicates that the profitability of Company Y by using total assets is unstable and needs to be improved. It can be seen from Table 2 that the net profit rate on sales showed an upward trend from 2017 to 2018, but it continued to decline in the following two years, with a large decline in 2020, and then began to rise again in 2021. The value of this index in 2021 was still smaller than that in 2017. The five-year value of this index reflects that Y company's ability to obtain net profit from operating income is unstable and needs to be improved. Based on the above analysis, it can be known that Y enterprise has a certain investment risk.

3.3. Operational risk identification

Table 3: Y Company operational risk identification sheet

Project	2021	2020	2019	2018	2017
Accounts receivable turnover	4.58	4.18	4.48	4.57	4.55
Inventory turnover	3.94	3.54	3.63	3.34	2.81
Total asset turnover	0.64	0.60	0.68	0.67	0.56

Data source: Financial statements of Y Company and NetEase Financial website

From Table 3, it can be seen that from 2017 to 2021, although the accounts receivable turnover ratio

ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

of Y enterprise is in a stable state, its index value is not high on the whole, that is, the turnover of accounts receivable is slow. It can also be seen that Y enterprise's management level of accounts receivable needs to be strengthened. From 2017 to 2021, the inventory turnover ratio was roughly on the rise, but its overall level was not high, which reflected that Y's inventory occupied a high level of capital, and the inventory management level also needs to be strengthened. And for the total asset turnover Y enterprise performance is even less satisfactory. Through the above analysis, the operation risk of Y enterprise is identified.

4. Causes of financial risk

4.1. Single financing method

Although Y Company's financing sources are not only the investment it has received, most of its financing sources are loans. Over-reliance on loans will cause great repayment pressure to Y company. Moreover, it takes a long time for pharmaceutical companies to invest and recover. Once the debt is due and cannot be repaid in time, the project will be stopped due to capital problems, and even the cash flow of the enterprise will be broken, making the enterprise fall into financial crisis. The financing of Y company not only relies too much on borrowing, but a large part of the borrowing comes from short-term borrowing. Compared with long-term borrowing, short-term borrowing is easy to obtain, but it brings greater risks to the enterprise, and will also affect the subsequent financing.

Because Y company's capital structure needs to be improved because it relies too much on a financing method, and the enterprise relies on debt management. The high asset-liability ratio makes the enterprise's debt paying ability weak, and makes the subsequent financing ability of the enterprise lower, and the financing risk it faces will also increase.

4.2. Low product profitability

From the financial information of Y company, it can be seen that although the operating income of Y company is increasing year by year, it is in a state of large fluctuation, and the profitability is unstable. The main reason is that Y company has a low ability to control expenses, which makes sales expenses high.

4.3. Insufficient R&D investment

As a pharmaceutical company, we should have core competitiveness so that we can have advantages in the fierce market competition. Pharmaceutical companies invest heavily in research and development, and it takes a long time to produce results, and the failure rate of research and development is high. A new drug needs a long time and many steps from the beginning of research and development to the approval to enter the market. The failure of any link in the middle will lead to the failure of research and development, resulting in the waste of early investment. When the enterprise R&D investment is insufficient, the enterprise will have weak R&D ability and insufficient innovation ability, unable to find new products to break through the homogeneity of market products, and have no advantage in the competition of the same industry.

4.4. Poor management of accounts receivable

It is known that Y Company has a large number of receivables, and the accounting and subsequent collection of receivables are all the responsibility of the financial department. However, it is obvious that the smooth collection of receivables cannot rely on the work of only one department, but requires the cooperation of multiple departments. Neither did the development of new customers, and the subsequent collection of funds was not related to the performance of personnel.

5. Control measures

5.1. Expand financing channels

In order to avoid the expansion of financial risks caused by the single financing method and affect the subsequent operation of the enterprise, Y enterprise should change the single financing method to

ISSN 2616-5902 Vol. 4, Issue 14: 35-40, DOI: 10.25236/AJBM.2022.041406

avoid the dependence on short-term borrowing. It can be financed by issuing new shares or absorbing direct investment from investors, or by relying on the company's previous retained earnings. Efforts will be made to reduce the asset-liability ratio to an appropriate level, while using financial leverage without putting enterprises at risk. If the single financing method cannot be changed, the dependence on short-term debt should also be reduced, so as to improve the management ability of enterprises and change their financial status, so as to obtain long-term loans from banks, so as to reduce the debt repayment pressure of enterprises, or issue long-term bonds through financial institutions.

5.2. Prudent investment

For investment, it is necessary to fully evaluate the feasibility of a project and the subsequent benefits. Before investing, we should conduct sufficient research and pay close attention to market changes in order to adjust our policy and strategy in time. As a pharmaceutical company, it should conductfull research on the market and make a full forecast on the market prospect before researching and developing new drugs. For the investment of other enterprises, it is necessary to fully investigate the strength of the enterprise and the development prospects of the industry in which the invested enterprise is located.

5.3. Increasing investment in research and development

As a pharmaceutical company, innovation is crucial to the development of the company, and R&D output and R&D investment are positively correlated with R&D investment to some extent. Therefore, if Y company wants not to be in a weak position in the fierce market competition, it needs to increase its R&D investment and get rid of the problem of product homogeneity in the market to improve its competitiveness.

5.4. Scientific management of accounts receivable

For the collection of accounts receivable, the collection plan should be divided according to the aging of accounts, the collection of accounts receivable should be specific to specific positions or personnel, and the collection of accounts receivable should be bound with the performance assessment of sales personnel, so as to maximize the enthusiasm of the collection personnel, and timely collection of funds to avoid bad debts[5]. Cash discounts can be offered to customers to force repayment.

At the same time, when developing new customers, we should fully investigate new customers, understand their subsequent repayment ability, and formulate scientific credit policies to divide customers, so as to avoid the influence of too wide credit policies on the recovery of subsequent funds.

6. Conclusion

In the process of identifying and controlling financial risks, this paper chooses Y enterprise as the case company. This paper identifies the financial risks of Y enterprise, analyzes the causes of the identified risks, and puts forward specific measures to control risks according to the causes of risks. The measures Y Company can take to control risks include expanding financing channels, prudent investment, increasing R&D investment, and scientific management of accounts receivable.

References

[1] Tu Hongwei. Company to prevent and resolve financial risks to explore [J]. Journal of accounting, 2014 (29): 116-118. The DOI: 10.16144 / j.carol carroll nki issn 1002-8072.2014.29.097.

[2] Zhang Suhui. Enterprise financial risk and agent system [J]. Probe, 2012 (3): 51-52 + 47.

[3] Huang Wanting. Research on enterprise financial risk control [J]. Friends of Accounting, 2013(23):77-79.

[4] Qiao Meixin. Analysis of enterprise financing activities [J]. Journal of Shanxi University of Finance and Economics, 2015,37(S1):93+103.

[5] Tian Mei. Corporate financial risk identification and countermeasures analysis [J]. China Foreign Capital, 2020(20):69-70.

[6] Wang Huaju. Identification and Prevention of Enterprise Financial risk -- Taking the bankruptcy of Smart Union Group as an example [J]. Financial Supervision, 2017(15):95-99.