

Original Paper

Research on the Motivation and Effect of Longfor Group's Transformation to Asset-light Operation Mode

Siqi Li¹

¹ School of Economics and Management, Lanzhou University of Technology, Lanzhou City, Gansu Province, China

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Abstract

Since the real estate marketization reform in 1998, China's real estate industry has continued to focus on asset operation mode, at that time in the golden period of the industry, real estate enterprises only need to hoard a lot of land, wait for the appreciation of the land and then resell, you can get considerable returns. However, in the context of the current slowdown in the economic growth of China's real estate industry, it is difficult for commercial real estate enterprises to continue to operate with heavy assets, so such enterprises begin to seek transformation, and want to change a profit model to match the current market. As a new way for enterprises to accumulate core competence and maximize value, "asset-light operation" model has been highly valued by the academic and business circles. This paper takes Longfor Group, a representative real estate enterprise, as the research object, and makes an in-depth analysis of the company's finance from the perspective of its financial characteristics and financial performance, in order to provide certain theoretical references for the successful application of the transformation and development of similar companies.

Keywords

longfor Group, asset-light operation model, financial performance evaluation

1. Introduction

Asset-light refers to resources that can create value for enterprises. Compared with heavy assets such as plants and equipment, which are costly and difficult to transform, asset-light is more flexible. It includes not only tangible monetary funds and some current assets, but also intangible assets such as brand value, research and development capability, sales channels, talent reserve and customer relationship. Light assets reflect the soft power of an enterprise.

The traditional operating model obtains income through asset appreciation, which relies too much on

the massive investment of assets in the early stage. However, after the transformation from heavy asset to light asset, the asset structure of real estate enterprises will be clearer, and the reduction of interest-bearing liabilities will reduce the financing pressure correspondingly, which is conducive to the return of cash flow. When the market environment changes, Due to its sufficient cash flow to facilitate the liquidation of the inventory of housing enterprises, operating risks are reduced, and the development of housing enterprises will be more stable. Longfor Group has been implementing the transformation of its asset-light strategy since 2017, and is one of the first real estate enterprises to implement the asset-light operation model. With cooperative development business as the core, Longfor Group has gradually diversified its asset-light business and become a leading real estate enterprise implementing the asset-light model. Based on this, this paper chooses Longfor Group as the case object to study the impact of asset-light operation mode on its financial performance from four aspects: solvency, profitability, operating capacity and development capacity.

2. Overview of Longfor Real Estate Company

Longfor Group Holdings Co., Ltd. was founded in 1993 in Chongqing, formerly known as Longfor Real Estate Co., LTD. In 2009, Longfor Group was listed on the main board of the Hong Kong Stock Exchange. Its business scope covers a wide range of businesses, including real estate project development, long-term rental apartments, commercial operations and intelligent services. Longfor Group has always been adhering to the original intention of "treating you well for a lifetime", and is committed to providing consumers with more warm, more considerate and detailed diversified services. By the end of 2023, Longfor Group's business has spread across more than 100 cities across the country, developed more than 1,200 projects, accumulated construction area of more than 16 million square meters, more than 6,600 cooperative brands, won the "China's Top Ten real estate development Enterprises Comprehensive strength" enterprise for 12 consecutive years, and was selected as a constituent stock by Hang Seng Index in 2021. Officially entered the ranks of blue chip stocks.

3. The Motivation of Longfor's Transformation to Asset-light Operation Mode

3.1 Improve the Asset Structure and Enhance the Solvency

Under the "asset-heavy" business model, real estate enterprises must go through the whole capital cycle process from land acquisition, development to sales. However, due to the long recovery cycle of real estate projects and the large amount of capital investment in the early stage, the cost of capital occupied by enterprises is also at a high level, which is prone to problems such as capital turnover difficulties. In addition, with the changes in the domestic environment, the rapid rise of housing prices and the heavy tax burden pressure have led to enterprises having to pay more costs to get land, which has brought extremely adverse effects on the development of the real estate industry. In the asset-light operation mode transformation plan, Longfor Group focuses on the adjustment of asset structure. By stripping off assets with high resource occupancy rate and poor turnover capacity, capital occupation of non-current

assets is reduced, cash flow security is effectively guaranteed, and the solvency of the enterprise is improved.

3.2 Improve Profitability and Enhance Core Competitiveness

If Longfor Group continues to rely on the original sale of real estate and providing property services for capital turnover, it will bear too much risk. With the continuous regulation of housing prices by national policies, Longfor Group's profit model of reserving land for development and selling after housing prices rise is no longer suitable for market development. The slowing down of sales speed slows down the project turnover speed and aggravates the decline of profitability of the real estate industry. In order to improve this situation, Longfor Group began to transform to the asset-light operation model, changing the original profit model from asset appreciation to value-added service income. This model allows enterprises to reduce investment in projects during operation, make full use of brand value and improve management ability to enhance core competitiveness of enterprises, and thus bring excess returns.

3.3 Expand Financing Channels and Ease Financing Pressure

Due to the restrictions of the national regulation policy on the real estate industry and the impact of the operation of the real estate enterprises themselves, most of the real estate enterprises still obtain the early investment capital through bank credit loans or mortgage loans. At the same time, the strict credit conditions of major banks and the strict control system of real estate enterprises have brought unprecedented financing pressure to enterprises, and the capital chain is facing the risk of breaking. Therefore, Longfor Group has developed financing channels by issuing corporate bonds, special bonds and other financing methods, making full use of brand value and good credit level, and reducing corporate financing costs by virtue of its financing resources accumulated over the years in the market.

3.4 Accelerate the Expansion of Scale and Achieve Strategic Layout

In today's environment, the competition in the real estate industry is becoming more and more fierce. In order to cope with the risk of being eliminated by the market and achieve sustainable development, Longfor Group established the strategic goal of "regional focus, multi-formats" as early as 2004, and gradually realized its grid layout in the first and second-tier high-level cities in China. Most of Longfor Group's projects focus on the development of middle and high-end residential and commercial real estate, and most of the projects are developed with business districts as the core, usually concentrated in the central areas of cities. Therefore, Longfor Group needs more capital investment in the process of realizing the comprehensive layout strategy. The transformation of the asset-light operation mode can reduce the financial pressure faced by Longfor Group in the early development process, and invest limited funds into more projects, thus accelerating the development of new markets for Longfor Group and helping it realize the strategic layout of business.

4. The path of Longfor Group's Transformation to Asset-Light Operation Mode

4.1 Introduce Cooperative Development Mode

At the beginning of 2015, Longfor Group carried out the layout of cooperative development business in an all-round way, and Longfor Group has cooperated with Standard Chartered Bank and Canadian pension fund. Starting from Chongqing, we completed the layout and development of commercial real estate projects in Chengdu, Shanghai and other places, and the number and scale expanded year by year. In addition to real estate development, Longfor Group's long-rent apartments and other projects have also begun to introduce partners. The operation mode of stock split cooperation can enable Longfor Group to have more initiative in resource allocation, speed up the project development process, provide new financing channels for enterprises, greatly reduce the development risk, and achieve the purpose of asset-light "small stock trading".

4.2 Implement the Destocking Strategy

Longfor Group has been actively responding to the call of national policies, reducing inventory and debt, and building a scientific supply, marketing and inventory management system. The system runs through every link of the project operation, adopts flexible dynamic monitoring strategy, and realizes the whole process management of supply and inventory according to the changes of real-time indicator data to ensure that the enterprise inventory can be maintained at a low level. The company has adopted a very prudent and pragmatic strategy in inventory reduction and debt structure optimization, such as holding a series of housing marketing activities every year such as Longfor House Exchange Festival, Longfor House Sharing Festival and commercial gold rush season, showing its competitive advantage in the future market.

4.3 Develop Value-added Services

In order to accelerate the transformation process of the asset-light operation model, Longfor Group focuses on the field of value-added services, aiming to break the traditional business framework and strive to achieve comprehensive leadership on the multi-field track. Among them, the launch of Longfor U Xiang Jia APP is a highlight of its commitment to providing professional and efficient property management and services. This new service business shows strong capital turnover ability, and the initial capital investment is relatively controllable, which makes Longfor's business layout in the five years of asset-light transformation to achieve rapid regional expansion. With the increasingly diversified business structure of the company, the revenue of various service businesses has repeatedly reached new highs, becoming the mainstay of the corporate revenue plate.

4.4 Export Brand and Management

As far as Longfor Group is concerned, establishing a good reputation and strong brand influence can not only significantly enhance the added economic value of its products, but also effectively attract and gather a group of high-quality partners. To this end, Longfor Group has successfully created three unique commercial brands, namely "Sky Street", "Jiayue Yun" and "Xingyue Yun". Launched the highly acclaimed "Crown Apartment" brand in the field of long-term rental apartments; At the same time, in the real estate development sector launched "Yan Lanshan" and "ZiChen" and other highly praised brands. Moreover, Longfor Group has been actively fulfilling its social responsibilities,

devoting itself to public welfare undertakings such as elderly care, poverty alleviation, education, and environmental protection, and has specially set up the public welfare brand project of "Longfor New Year Goods" to further establish a positive social image. With the gradual improvement of the group's brand influence, the brand output under the asset-light operation mode will bring more significant value-added income, injecting strong impetus for the Group's sustainable development.

5. Financial Performance Analysis of Longfor Group under the Asset-light Operation Mode

5.1 Solvency Analysis

Solvency analysis can reveal the degree of financial risk borne by enterprises and help to predict the financing prospects of enterprises. This paper selects current ratio, quick ratio and asset-liability ratio to study the change of debt-paying ability of Longfor Group in asset-light mode.

Table 1. Indicators of the Solvency of Longfor Group from 2013 to 2023

| A given year | Current ratio | Quick ratio | Asset-liability ratio |
|--------------|---------------|-------------|-----------------------|
| 2013 | 1.36 | 0.3 | 72.41 |
| 2014 | 1.5 | 0.41 | 70.1 |
| 2015 | 1.69 | 0.54 | 66.07 |
| 2016 | 1.51 | 0.42 | 66.59 |
| 2017 | 1.32 | 0.4 | 70.73 |
| 2018 | 1.49 | 0.5 | 72.22 |
| 2019 | 1.48 | 0.49 | 74.45 |
| 2020 | 1.44 | 0.5 | 74.81 |
| 2021 | 1.44 | 0.53 | 74.66 |
| 2022 | 1.61 | 0.64 | 70.36 |
| 2023 | 1.66 | 0.7 | 66.24 |

It can be seen from Table 1 that Longfor Group has a poor performance in the current ratio index, which is due to the poor inventory liquidity of real estate enterprises, long sales cycle and weak short-term debt repayment ability. From the analysis of the overall quick ratio of Longfor Group, the company's overall quick assets will not be able to support all the working capital, but in the long run, the quick ratio of Longfor Group is on the rise. Before 2018, the quick ratio remained at about 0.4, and after 2018, after a series of transformation measures, the quick ratio has been significantly improved. It fluctuates around 0.5. In general, the short-term solvency of Longfor Group is relatively weak, and there is room for improvement. Generally speaking, the lower the value of asset-liability ratio, the smaller the debt pressure of enterprises, and the better long-term solvency. The asset-liability ratio of Longfor from 2013 to 2015 has been declining, especially in 2015, the decline is large, and Longfor's

long-term solvency has been optimized. However, after 2015, the index grew slowly and only reached 74.81% in 2020. In-depth analysis found that the reason for the increase in debt scale was mainly the issuance of a large number of bonds with low financing costs after the asset-light transformation, as well as the substantial increase in advance housing payments. Overall, Longfor's asset-liability ratio is still at a low level among real estate enterprises. In the follow-up development, Longfor needs to pay more attention to the problem of long-term borrowing, reasonably control the proportion of long-term borrowing in liabilities, and reduce the long-term debt repayment risk as much as possible.

5.2 Profitability Analysis

Enterprise operation capacity can reflect the turnover of enterprise assets and help to identify the utilization rate of enterprise assets. In this paper, the net profit rate on sales, gross profit rate on sales, return on equity and net profit rate on total assets are selected to measure the profitability of Longfor Group under the asset-light model.

Table 2. Profitability Indicators of Longfor Group from 2013 to 2023

| A given year | Net profit margin on sales | Gross profit margin on sales | Return on equity | Return on total assets |
|--------------|----------------------------|------------------------------|------------------|------------------------|
| 2013 | 20.8 | 27.8 | 24 | 6 |
| 2014 | 17.1 | 26.5 | 19.7 | 5.4 |
| 2015 | 19.75 | 27.44 | 17.47 | 5.1 |
| 2016 | 18.13 | 29.08 | 15.66 | 4.48 |
| 2017 | 22.86 | 33.9 | 19.04 | 4.29 |
| 2018 | 18.04 | 34.14 | 21.33 | 3.73 |
| 2019 | 17.58 | 33.63 | 20.88 | 3.16 |
| 2020 | 15.63 | 29.28 | 19.77 | 2.82 |
| 2021 | 14.23 | 25.31 | 20.45 | 2.91 |
| 2022 | 13.1 | 21.17 | 18.25 | 2.93 |
| 2023 | 9.48 | 16.92 | 8.74 | 1.73 |

It can be seen from Table 2 that the gross profit margin and net profit margin of Longfor Group are declining in fluctuations. Since 2019, the gross profit margin and net profit margin of Longfor Group have reached a turning point and started to decline continuously. This is because the Group has begun to increase its investment in energy conservation and emission reduction, which will inevitably reduce the amount of net profit of the company, which is also one of the reasons for the decline of net profit margin of the company. From the trend of ROE, it can be seen that the ROE of Longfor Group reached a peak in 2018, but there was a temporary decline after 2018. The main reason for the decline in the rate of return is that Longfor Group began to get involved in emerging areas in 2018, invested a lot of

money and time to seize market share, and the associated costs have brought a heavy burden to the capital chain of the enterprise. The index of return on total assets of Longfor Group dropped from 6.00% to 1.73%, which is affected by the tightening policy of China's real estate industry on the one hand, and on the other hand, Longfor Group's continuous expansion of new businesses and new regions requires a large amount of cost input. In general, due to the tightening of real estate policies and the impact of the real estate market environment, the profitability of most real estate companies shows a downward trend, and the asset-light transformation has controlled the decline of Longfor to a certain extent.

5.3 Operational Capacity Analysis

The operational capacity of the business, that is, the ability of the company to operate different business assets and obtain maximum returns. This paper analyzes the turnover rate of the main assets of Longfor Group to evaluate the group's operating capacity. It is generally believed that the faster the turnover of assets, the better the enterprise.

Table 3. Operating Capacity Indicators of Longfor Group from 2013 to 2023

| A given year | Inventory turnover | Accounts receivable turnover rate | Turnover of current assets | of Turnover of total assets |
|--------------|--------------------|-----------------------------------|----------------------------|-----------------------------|
| 2013 | 0.43 | 118.99 | 0.44 | 0.31 |
| 2014 | 0.48 | 58.22 | 0.49 | 0.33 |
| 2015 | 0.43 | 27.41 | 0.41 | 0.27 |
| 2016 | 0.43 | 23.3 | 0.42 | 0.27 |
| 2017 | 0.36 | 29.5 | 0.39 | 0.25 |
| 2018 | 0.37 | 48.11 | 0.38 | 0.27 |
| 2019 | 0.35 | 53.17 | 0.35 | 0.26 |
| 2020 | 0.37 | 64.18 | 0.34 | 0.26 |
| 2021 | 0.43 | 70.3 | 0.37 | 0.27 |
| 2022 | 0.54 | | 0.42 | 0.3 |
| 2023 | 0.52 | 51.65 | 0.37 | 0.24 |

As can be seen from Table 3, although the inventory turnover rate of Longfor Group did not show an upward trend after the asset-light transformation began in 2014, it is still relatively stable. After the transformation of Longfor Group, the operating income increased year by year, but the change trend of inventory turnover was inconsistent with it. The reason is not unrelated to the increase in the scale of enterprises and the rapid increase in inventory. Coupled with policy constraints, the liquidity of enterprise inventory is restricted to a certain extent. The turnover rate of accounts receivable of Longfor Group plummeted during 2015-2016, mainly because Longfor Group implemented the strategy of

"expanding depth", accelerated the pace of layout in major cities across the country, added reserve land and opened a large number of new projects, but there was a long period from the start of the project to the sale. At the same time, in order to promote the sale of commercial housing, Longfor Group adopts credit sales, so accounts receivable rise sharply. After 2016, Longfor Group improved and strengthened the accounts receivable management system, and the indicator stopped the downward trend and continued to rise. The total asset turnover rate of Longfor has remained at 30% in the past ten years, which is relatively stable. The main reason is that Longfor introduces third-party investment through the transformation of operation mode, uses a small amount of funds to obtain the control of projects, and improves investment efficiency. The turnover capacity is not affected by the industry, and the asset-light operation mode contributes greatly to the ability to strengthen turnover.

5.4 Development Ability Analysis

Table 4. Development Capability Indicators of Longfor Group from 2013 to 2023

| A given year | Net profit growth rate | Revenue growth rate |
|--------------|------------------------|---------------------|
| 2013 | 27.55 | 48.82 |
| 2014 | 3.94 | 22.84 |
| 2015 | 7.59 | -7 |
| 2016 | 1.83 | 15.55 |
| 2017 | 37.65 | 31.53 |
| 2018 | 28.88 | 60.66 |
| 2019 | 12.93 | 30.42 |
| 2020 | 9.08 | 22.2 |
| 2021 | 19.26 | 21.04 |
| 2022 | 2.13 | 12.17 |
| 2023 | -47.25 | -27.87 |

As shown in Table 4, in terms of net profit growth rate, Longfor Group's net profit growth rate has always been positive, and achieved the highest annual net profit growth rate of 37.65% in 2017. The trend is relatively stable, indicating that Longfor Group's development is still relatively stable after the transformation to asset-light operation mode, and net profit has been rising steadily. In terms of operating income, from 2013 to 2014, although the total operating income was growing, the growth rate was declining, and even reached a negative value in 2015. In 2016, the growth rate of total operating income returned to positive value and increased rapidly, reaching the highest value of 60.66% in 2018. In 2020, the growth rate declined. But it's still pretty impressive. The slow growth before 2015 May be due to the relatively small scale of asset-light in the early stage of transformation, the overall downward trend of the real estate industry, and Longfor lost some sales revenue by withdrawing

customers with poor credit in order to ensure sales quality. In 2023, the growth rate of net profit and operating income of the company are both negative, due to the impact of the downward trend of the real estate industry. By the end of 2023, Longfor Group has achieved positive operating cash flow, optimized debt structure and resisted market risks. In general, after starting the asset-light operation mode, Longfor's profits are rising steadily, and the enterprise is developing rapidly and stably. Asset-light operation is conducive to the improvement of the growth ability of real estate enterprises.

6. Conclusions and Recommendations

Under the current macroeconomic background, real estate enterprises with heavy asset operation are facing multiple challenges such as declining return on equity, high financing pressure, high asset-liability ratio and cash flow pressure. By analyzing the financial performance of Longfor Group before and after the transformation of asset-light operation mode, it is concluded that the asset-light operation mode has a positive impact on Longfor Group. However, enterprises also need to strengthen the effective management of inventory assets. At the same time, the high asset-liability ratio of enterprises also hides greater financial risks. Enterprises need to strengthen the optimization of asset liability structure and the implementation intensity of cost control. Reasonable business layout can help enterprises explore and open up new high value-added business areas, so as to effectively avoid the performance decline risk and long-term debt risk under the single real estate development business. While enjoying the advantages of economies of scale brought by the asset-light operation mode, Longfor Group should also continuously improve its operation and management system, and increase investment in R&D and innovation to ensure that it continues to maintain its core competitiveness in the fierce market competition. Only in this way can the asset-light operation mode move forward steadily and achieve sustainable development.

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