

## Original Paper

# Research on Debt Crisis Identification and Collaborative Resolution Mechanism of Listed Private Enterprises

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### Abstract

*In recent years, the Central Economic Work Conference has continuously emphasized the importance of supply-side structural reform, effectively resolving the local debt crisis to alleviate China's economic development and promote the sustainable development of China's economy. Under the influence of the new crown epidemic, listed private enterprises are facing a huge debt crisis, which has led to the continuous growth of local debt, so effectively resolving the debt crisis of listed private enterprises will be conducive to the healthy development of China's economy. This paper identifies and analyzes the debt crisis of listed private enterprises from the aspects of macroeconomic environment, industry competition background and enterprise operating ability, and proposes a synergistic approach from the government, creditors and enterprises themselves to resolve their debt crises and achieve sustainable development of enterprises.*

### Keywords

*debt crisis, private enterprises, debt risk, financial leverage*

## 1. Introduction

Since the 2015 Central Economic Work Conference clearly pointed out that to promote economic development, we need to pay more attention to improving the quality and efficiency of development, and stabilizing economic growth needs to pay more attention to supply-side structural reform, and in

2016, economic and social development in 2016 should strategically adhere to the principle of seeking progress in stability, grasp the rhythm and intensity, and tactically grasp the key points, mainly to grasp the five major tasks of de-capacity, de-inventory, de-leveraging, cost reduction, and making up for shortcomings, of which deleveraging is the core goal of achieving structural reform. It has always been the main theme of China's macroeconomic regulation and control. According to the estimates of the Chinese Academy of Social Sciences and the Bank for International Settlements, the leverage ratio of China's enterprise sector is estimated to be between 130% and 170%, and the leverage ratio is on the high side. In addition, affected by many unfavorable factors such as the new crown pneumonia epidemic, the international economic environment has become more complex, the downward pressure on China's economy has increased, the competition in various industries has become more and more fierce, and more and more uncertainties have appeared in the production and operation process of enterprises, not to mention private enterprises. In the case of the deteriorating business environment, enterprises are facing huge financial risks, once the debt chain, logistics chain, and industrial chain problems occur, resulting in the deterioration of the financial situation of the enterprise, thus falling into a debt crisis. When an enterprise falls into a debt crisis, it will not only damage the interests of creditors, investors and other stakeholders, but also seriously affect the daily production and operation activities of the enterprise, leading to the further expansion of financial risks among different entities, and finally causing serious consequences. Without the support of the government, there will be insufficient turnover of operating funds, lack of funds to maintain the project, and the yield will continue to decline, so the enterprise will have a serious shortage of cash inflow from operating activities, and its own hematopoietic capacity cannot be supplied, and finally unable to repay the principal and interest of the due debt, so that the listed private enterprises face the risk of delisting and even be forced to go bankrupt.

At the meeting of the Political Bureau of the Central Committee of the Communist Party of China on July 24, 2023, it was pointed out that "it is necessary to effectively prevent and resolve local debt risks, formulate and implement a package of debt plans", and resolving local government debt risks has become the top priority of China's economic work, which is directly related to the virtuous cycle of the national economy and the release of local government vitality, and is related to the sustainable development of national finance and economic security. As of the end of 2022, the scale of China's statutory government debt was 60.93 trillion yuan, and the debt ratio was 50.35%; The balance of Chinese bonds was 25.87 trillion yuan, accounting for 42.46%, and the balance of local government debt was 35.06 trillion yuan, accounting for 57.54%. The growth of local government debt will affect the financing of local private enterprises, and the financing burden of listed private enterprises will be aggravated, which will inevitably constitute debt risk. It can be seen that properly handling the debt crisis of listed private enterprises will effectively resolve local debt risks, which is very important for promoting the healthy and sustainable development of enterprises.

## **2. Identification of Debt Crisis of Listed Private Enterprises**

### *2.1 Market Environment*

#### **2.1.1 Economic Environment**

The development of listed private enterprises needs to keep up with the times, and the macroeconomic environment will directly affect the sustainable development of enterprises. If the macro economy continues to grow, the sales environment of private enterprises will be relatively healthy, the daily business activities of enterprises can be effectively carried out, the profitability and debt repayment ability of enterprises can be effectively guaranteed, the debt risk of enterprises can be reduced, and the debt crisis of enterprises can be resolved. On the contrary, if the macro economy is blocked, the overall environment will decline and the daily business activities of the enterprise will not be carried out in an orderly manner, and the enterprise will face unstable cash flow and capital disruption, which will lead to triggering debt risks and facing debt crises. For example, at the end of 2019, affected by the new crown epidemic, the local geographical blockade and online business development caused by the rapid spread of the disease made it impossible for many enterprises to transform and stagnate their business, which had a great impact on China's economy, and more enterprises were affected by the epidemic and broke out into debt crises, especially listed private enterprises and self-employed individuals.

In the case of a stable epidemic situation and a recovery of the economic environment, the government's policy guidance will directly affect the future operation of enterprises, thereby affecting the sustainable operation of enterprises. At the macro level, if the government introduces relevant policies to support the development of a certain industry, it will directly bring good news to the relevant industries, so as to accelerate the return of funds to the enterprise to achieve the rapid development of the enterprise, effectively respond to and improve the debt risk of the enterprise, and strengthen the operating ability of the enterprise. On the contrary, if the government does not support the development of a certain industry, withdraws relevant support or introduces policies to support other industries, enterprises in this field will also face restrictions on business activities and the inability to return funds, which will exacerbate the debt risk of enterprises and cause a debt crisis. For example, in recent years, the government's support for the development of new energy vehicles, major automotive industry enterprises have accelerated the development and promotion of new energy vehicles, and the related businesses are also accelerating, enabling BYD and other car companies to successfully transform into the new energy market; On the contrary, some fuel vehicle companies are unable to adapt to the market development of new energy vehicles, resulting in a sharp decline in vehicle sales and even facing the crisis of bankruptcy.

#### **2.1.2 Industry Environment**

The fierceness of industry competition directly affects the development of enterprises in the industry, the more fierce the industry competition, the greater the pressure on the survival of enterprises, and the more difficult it is to achieve high-speed development; The less competitive pressure in the industry, the fewer enterprises of the same type, the easier it is to develop, and the greater the profit can be

obtained at a larger cost, so as to achieve higher net profit and reduce debt risk. Such as the current new energy vehicle industry, government policy guidelines and the general trend, all car companies are transforming to new energy vehicle research and development, the number of industry competitors is large, so that enterprises are facing greater competitive pressure, the competitive cost of enterprises is gradually increasing, and the cost-effective new energy vehicles are pushed forward, making the fuel vehicle industry decline rapidly, the cost of sales of enterprises increases and the income is difficult to improve, which makes it difficult for enterprises to repay debts through sales, and enterprises are prone to debt crisis. However, when there is a market close to monopolistic competition in a certain industry, and the company's products are in short supply or have a low cost in the market in order to achieve smooth sales and make a profit, such enterprises can achieve higher product sales revenue and net profit at a relatively low cost, so as to improve the ability of the enterprise to repay the debts owed and avoid the occurrence of debt risks. At the same time, the market value of the industry also determines the development ability of the enterprise, and the market demand for the industry is stable and continues to grow, so the daily development of the enterprise in the state of market saturation can be stable and continuous to ensure its solvency and achieve sustainable development; However, when the industry is gradually eliminated with the development of the market, even if the operating ability is strong, it will eventually face the current situation of declining sales and become insolvent and produce a debt crisis. For example, in recent years, the growth rate of China's consumption of highly polluting energy such as coal has slowed down, which has caused some listed companies engaged in coal energy business to have a serious revenue decline and affected the profit status and debt repayment ability of such enterprises, and some coal-based energy companies have even entered the "ST" ranks.

## *2.2 Enterprise Capabilities*

### *2.2.1 The Governance Structure Is Flawed*

The governance structure of a listed company will directly determine its ability to cope with the debt crisis, and the improvement of the governance structure will make the financial activities of the enterprise more rigorous and scientific to achieve the goal of sustainable development. If an enterprise has an unreasonable or unsound governance structure, it will directly lead to loopholes in the financial management activities of the enterprise, reduce its operating efficiency, and even cause violations of the operation of senior management, which is easy to break out of debt crisis. The governance structure problems that often arise in the development process of listed enterprises include: the controlling shareholder does not perform the duty of loyalty, thereby putting his own personal interests above the interests of the company, resulting in behaviors such as insider trading and related party transactions; The board of directors lacks independence, which makes it unable to effectively supervise and restrain the behavior of controlling shareholders, which is not conducive to the supervision of the company's financial activities; The board of supervisors does not play a supervisory role, so it is unable to effectively supervise the business activities of the enterprise, and the supervision of the financial behavior and liabilities of the enterprise is not effective, and the problems cannot be discovered and

prevented in time; Managers fail to effectively restrain and motivate, so that they cannot give full play to the maximum value of managers in corporate governance, and even managers go into debt for personal interests to pursue short-term high returns, thus harming the interests of the company.

### 2.2.2 Business Decisions Are too Blind

Mistakes in business decisions are often the root cause of debt crises in listed companies. The shareholders of listed private enterprises expand their business objectives, and the management is overconfident and lacks decision-making judgment, allowing the enterprise to expand blindly without reasonable prediction, pursuing the maximization of corporate investment returns, and ignoring the consideration of relevant factors, resulting in a debt crisis. It is usually manifested as: the management makes overly aggressive business decisions, improperly borrows to expand wantonly, and the production capacity rises while the cost increases, resulting in overloaded debt, unbalanced capital structure, and high financial leverage, which leads to financial risks and debt crisis. The management's blind pursuit of high-capacity production leads to the inability to guarantee product quality, hindered marketing, and makes it impossible for operating funds to be returned, resulting in operational risks, and making it impossible to repay debts due on time. The common characteristics of enterprises in debt crisis are to adopt aggressive business strategies to blindly expand and occupy the market, while ignoring the load of their own production capacity, blindly pursuing the growth of sales and profits, which makes it difficult to maintain the company's capital turnover, and the cash flow cannot be effectively turned over and is burdened with higher debts and dishonesty, forming a vicious circle and falling into a debt crisis.

### 2.2.3 There Are Weaknesses in Cash Flow Management

The reason for the occurrence of debt itself is that the enterprise carries out financing and financing for the purpose of policy operation to strengthen its own cash flow, and the effective operation of the enterprise makes its profitability higher than the interest borne by the debt, so as to achieve positive operation and avoid debt risk. However, this requires enterprises to have better cash flow management capabilities. Listed private enterprises are susceptible to adverse effects such as economic downturn and insufficient internal profitability in the process of operation, resulting in poor product sales and declining profits, resulting in the inability to maintain the economic performance of the enterprise, huge losses in net profit, insufficient internal capital turnover, and the inflow of operating cash flow is far lower than the amount of funds required for production and operation, which makes the long-term negative operation lead to the inability to repay the due debts on time, the phenomenon of insolvency, and the risk of bankruptcy. Enterprises in debt crisis are mainly due to the fact that they are unable to repay huge debts, lack sufficient funds to support daily operations, and their capital turnover capacity is not enough to resist the maturity time limit of debts. Therefore, the primary task of sustainable development of enterprises is to ensure that the assets of enterprises can provide the daily needs of production and operation, reasonably manage the cash flow of business activities, help to accelerate the turnover of enterprise assets, improve the ability to realize assets, so as to accelerate the development

of enterprises through debt, rather than facing debt risks due to inability to repay debts.

### **3. Collaborative Resolution Mechanism for Debt Crisis of Listed Private Enterprises**

#### *3.1 Actively Coordinate Debt Maturity with Debtors*

When a listed private enterprise is facing a debt crisis, it can seek negotiation with the debtor to alleviate the crisis. According to the General Principles of the People's Republic of China Civil Law, if the debt should be repaid and is temporarily unable to be repaid, the debtor may repay it in installments with the consent of the creditor or the ruling of the people's court. Where they have the ability to repay but refuse to do so, the people's court is to make a judgment to compel repayment. If the debtor really has no money to repay the debt, or is unable to pay off the debt in a short period of time, then the creditor can negotiate with the debtor face-to-face and ask the debtor to repay the debt in installments on the premise of ensuring his livelihood, but the debt must be paid off in the end. On the one hand, the debt repayment period can be negotiated with creditors, and all creditors hope that there is a debt to collect rather than a distant term, and the debt term is still negotiable; On the other hand, it is possible to negotiate the interest rate on the debt with creditors, because the global economic development has been limited due to the new crown epidemic, and the business situation is not very good, for creditors, they also hope that the company will be able to repay the debt on its own, so reducing the interest rate is also negotiable.

In addition, when a listed private enterprise is unable to fulfill its obligations to creditors even if it postpones or lowers interest rates, the company can implement debt restructuring to cope with the crisis. The core of debt restructuring is a new debt repayment agreement reached between the creditor and the debtor in accordance with the relevant agreement reached or the court ruling. Debt restructuring can be to reduce the debt burden of the enterprise by paying off debts with assets, converting debts into equity, or modifying other debt conditions, so as to cope with the debt crisis and ensure the sustainable operation of the enterprise itself.

#### *3.2 Seek Funding to Broaden Access to Financing*

China's private enterprises are relatively simple in the way of capital supply, their financing costs are high, and there are few financing channels, so they often face the problem of financing difficulties, which hinders the sustainable development of enterprises. For private enterprises, there is no government capital injection, so most of the funds come from bank loans. Bank borrowing will be relatively higher in debt interest rates, which makes it easy for enterprises to bear greater pressure to repay principal and interest, resulting in high financial leverage risks. Enterprises should seek equity financing while borrowing from banks, so as to achieve a balanced capital structure of the enterprise and carry out diversified financing methods to reduce financial risks. Equity financing refers to the financing method in which the shareholders of an enterprise are willing to give up part of the ownership of the enterprise, introduce new shareholders through the capital increase of the enterprise, and increase the total share capital at the same time. The company does not need to repay the principal

and interest of the funds obtained from equity financing, but the new shareholders will share the profits and growth of the enterprise with the old shareholders. Therefore, equity financing can not only enrich the working capital of the enterprise, but also be used for the investment activities of the enterprise. For example, equity pledge financing can be chosen, that is, the pledgor uses its equity as the subject matter of the pledge to provide security for its own or others' debts, so as to guarantee loans to banks and other financial institutions; Implement allotment of shares to public issuance of securities, private placement of shares, and capital market financing and securities lending to raise funds for production and operation of enterprises, broaden the source of funds, and avoid debt risks.

### *3.3 Equity Restructuring to Enhance Capital Strength*

Equity restructuring refers to a type of enterprise restructuring in which the shareholders or shares held by the shareholders of the enterprise are changed, mainly including equity transfer and capital increase and share expansion. Equity transfer refers to the transfer of part or all of the equity or shares owned by the shareholders of an enterprise to others; Capital increase and share expansion refers to the increase in the capital of the enterprise by raising shares from the society, issuing shares, investing in shares by new shareholders or increasing investment by original shareholders to expand equity. Equity restructuring generally does not need to go through liquidation procedures, and its creditor's rights and debts continue to be valid after the equity restructuring. Therefore, the way of equity restructuring can realize the resolution of the debts of the original shareholders through equity transfer or capital increase and share expansion, alleviate the pressure on the operating funds of the enterprise, and protect the interests of creditors and the normal operation of the enterprise to the greatest extent. If high-quality external investors are introduced through capital increase and share expansion, it can increase the capital of enterprise development, enhance the capital strength of enterprises, and promote long-term development. According to the source of funds, the capital increase and share expansion of enterprises can be divided into exogenous capital increase and share expansion and internal capital increase and share expansion, of which the exogenous capital increase and share expansion is the use of private equity to introduce high-quality domestic and foreign strategic investors and financial investors, through the increase of corporate funds, expand shares, enhance the capital strength of enterprises. However, equity restructuring means the transfer of equity, so in some cases, it will lead to the original shareholder losing control of the original listed company.

### *3.4 Improve the Company's own Operation and Management to Increase Profitability*

Improper business decision-making of listed private enterprises is the root cause of their debt crisis, so in order to solve the debt crisis, it is indispensable to enhance the enterprise's own operation and management capabilities. The effective operation and management of an enterprise can ensure the competitiveness of its own products, enhance the capital turnover capacity of the enterprise, increase the cash flow of the enterprise, and enhance its debt repayment ability, thus avoiding the formation of a debt crisis. First, enterprises should strengthen their daily operation and management. In the process of production and operation, enterprises should ensure and control the capital flow of their procurement,

production, sales and other links, reduce unnecessary cost consumption as much as possible, control product costs and improve product quality, so as to achieve effective realization of products. Second, enterprises should strengthen the management of accounts receivable. The operation of enterprises is generally inseparable from sales business, and long-term credit sales will lead to the inability to return funds, insufficient cash inflow from operating activities, and the phenomenon that debts cannot be repaid on time. Third, it is necessary to rationally formulate and plan the use and investment behavior of enterprise funds. It is necessary to have a long-term plan for the capital management of enterprises, fully consider the funds required for the production and operation of enterprises, be vigilant against blind investment, and prevent the phenomenon of excessive cost of enterprise assets caused by the occupation of working capital, and the occurrence of debt crisis due to the rupture of the capital chain. Therefore, enterprises need to pay enough attention to their own business decisions and strategic management in order to improve their profitability and avoid the form of debt crisis.

#### 4. Conclusion

Debt crises are common in the development of listed private enterprises, and it is difficult for private enterprises to maintain good business practices due to the lack of government support, the volatile economic environment, and the high interest rates of bank loans. Under the pressure of the macroeconomic environment, government policies, industry competition, etc., listed private enterprises will inevitably have problems such as unbalanced corporate governance structure, blind implementation of business decisions, and weak cash flow control, resulting in the inability of enterprises to repay their debts on time and resulting in debt crises. Therefore, listed private enterprises should seek help from the government and creditors to improve their own operating capabilities and resolve the debt crisis. From the government's perspective, in accordance with relevant legal provisions and policy guidance, negotiate with creditors on debt repayment terms and interest rates to alleviate the debt maturity crisis; From the perspective of creditors, private enterprises should protect the interests of creditors through equity financing or equity restructuring, and increase the inflow of funds to repay debts to resolve the debt crisis; From the perspective of the enterprise itself, the enterprise should enhance its own operation and management capabilities, ensure the normal operation of capital flow from the daily business, improve the profitability of the enterprise, and make it higher than the value of debt repayment, so as to enhance its own debt repayment ability, avoid the debt crisis from the root, and enhance the sustainable development ability of the enterprise.

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