Analysis of Financing Mode of Real Estate Enterprises: Taking Evergrande and Vanke as Examples

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Abstract. The development of the real estate industry has been increasingly restricted, especially after the novel coronavirus. In this case, it restricted development trend is more obvious, and some enterprises have fallen very sharply. This paper mainly analyzes the different financing situations of Evergrande and Vanke in real estate companies. To be specific, this study investigates and analyzes the financing mode of Evergrande and Vanke, combined with the real estate financing mode, and puts forward the future prospects and limitations of these financing models. The research methods we adopt are comparative analysis method and experience summary method. At the same time, we will analyze the differences between Evergrande and Vanke, and discuss why one of them went bankrupt after experiencing restricted development, while the other was able to continue to survive. According to the analysis, it is related to the financing methods they adopted. These results shed light on guiding further exploration of the real estate in the more volatile situation the most suitable financing model as well as policy implementation.

Keywords: Three red lines of real estate; Evergrande bankruptcy; Financing.

1. Introduction

In recent years, the development of China's real estate market has been restricted by various policies [1]. To be specific, the three red lines of real estate include the asset-liability ratio of advance receipts shall not be more than 70%, the net debt ratio shall not be more than 100%, and the cash-to-debt ratio shall not be less than one times. The pre-sale of commercial housing is becoming common, and the recovery cycle of funds is very long.

Many real estate companies have been hit hard by the adverse effects of the COVID-19 and negative population growth [2-6]. Many problems have occurred, and even some leading real estate enterprises have been "in debt and not completed". In this context, the financing method for the real estate enterprise recovery has a great help.

However, this is a double-edged sword. The real estate industry is a capital-intensive industry with prominent features such as large capital demand, long cycle and slow return. The priority to solve the capital problem is the key to make a breakthrough in the real estate industry [7]. Itis closely related to financing, and there are risks in various channels and links of financing. The most prominent manifestation is that when real estate enterprises rely too much on external financing, their risk control will also decrease, which may lead to a shortage of funds.

One of Vanke's main financing methods is bank loans. It relies heavily on bank loans, because the cost of bank loans is low, the amount is high, and the agreed term of loans. In other words, the term of funds available to the enterprise, is relatively long. However, the negative aspect is that excessive bank loans will lead to the increase of the debt ratio of the enterprise. Moreover, if the enterprise cannot operate well, the capital chain may be broken and the enterprise cannot continue to operate. Another major financing method of Vanke is the advance payment, which is the deposit or part of the payment that the enterprise receives from the buyer in advance [8].

Evergrande, as the leader in China's real estate industry, the cause of its bankruptcy is not temporary, but long-term accumulation. Since the listing failure of "Jieke shenshen house" of

Evergrande Real Estate in 2020, Evergrande's capital chain breakage risk appeared for the first time. In November 2020, Evergrande's commercial bill was overdue for the first time, and then the commercial bill became longer and longer overdue [9]. From 2016 to 2020, according to Evergrande's annual reports, Evergrande's financing interest rate rose from 8.09% to 9.49%. It is more than twice as high as Vanke and Country Garden. While Evergrande's financing rate soared, another well-known Chinese real estate company's financing rate dropped from 4.5% to 4.39%. Evergrande expects to raise 400 billion yuan from a mainland listing. If A had gone public and raised $400 billion, its debt problem would have been temporarily solved, but it failed. Although Evergrande's total debt is listed as 1.97 trillion yuan in 2021, the real amount owed to banks and trusts is 5.8 trillion yuan. Moreover, the introduction of the last three red line policies almost blocked the final road of Evergrande financing operation. When it came into effect on January 1, 2021, Evergrande had basically hit three of the three red lines According to regulations, Evergrande cannot borrow any more [10].

This paper mainly discusses the different financing models of Vanke and Evergrande, as well as their advantages and disadvantages. Secondly, it also analyzes the financing problems in the bankruptcy of Evergrande, and the warning that the bankruptcy of Evergrande brings to the future financing models of other real estate companies. The first section mainly introduces the different financing modes and proportions of Vanke and Evergrande. The second section and the third section respectively analyze the financing situation of Vanke and Evergrande. In the fourth section, we will discuss the index differences between the two companies, explain the advantages and disadvantages of different financing models, and explain which matching model is more suitable for the current environment. The last section will summarize the general content of the paper and put forward some real estate companies to analyze the future development prospects.

2. Real estate financing mode

First of all, it refers to bank loans, which means that banks lend funds to real estate companies, such as Vanke Evergrande, at a certain interest rate according to national policies, and agree with them to return them within a certain period. The repayment period for these real estate companies is generally very long, and the loan amount is also high. Hence, this model has always been the backbone of the real estate business development.

The second is the real estate trust, which is to issue a certificate of income to bring together the funds of most investors, and then the real estate developer implements the trust plan through specialized trust companies and other institutions to form funds with a certain investment scale. A trust fund in which the funds of the trust plan are used in real estate development in the form of trust loans, and the comprehensive income of his investment is distributed proportionally to investors. There is also an IPO, which means an initial public offering (Initial Public Offering) refers to the first time a company sells its shares to the public through a stock exchange. One can get more money in the open market.

3. Vanke Financing Analysis

Vanke Enterprise Co., Ltd. was established in 1984. After more than 30 years of development, it has become a leading real estate company in China. As shown in Table 1, a market share of around 2.6 is extremely high for a real estate company. Vanke Group has abundant funds and diversified financing methods, mainly bank loans. Vanke has excellent solvency, and CCXI has given a credit rating of AAA to the Yifang Factoring Vanke Supply Chain Finance No. 38 asset-backed special plan product issued by Vanke Group in Ping An Securities on January 22, 2019. It shows that the Vanke Group has strong anti-risk capability, i.e., default risk is extremely low.

However, with the country's regulation of bank loans and the impact of social background on the development of real estate companies, Vanke suffered losses in 2014. In the same year, Vanke completed the conversion of B shares to H shares and was listed on the Hong Kong Stock Exchange.

In recent years, domestic real estate has become saturated and financing in overseas markets has prevailed. Vanke is the leader of Chinese real estate companies going abroad. In 2004, Vanke successfully financed twice through overseas markets. In 2007, it successfully raised US$250 million in Hong Kong. Equity financing is also one of Vanke's main financing methods. Compared with debt financing, equity financing has no repayment pressure and has a low risk factor. However, it will affect the control of the company, so equity financing needs to be controlled reasonably [10].

REITs are a popular financing method today, which can bring a large amount of financing to real estate companies. Vanke has applied it well and achieved success. REITs have advantaged that other financing methods do not have, such as flexibility and financing risks. Therefore, financing through REITs is an important means for Vanke to develop external financing. The stock price evolution of it is shown in Fig. 1.

Table 1. 2016-2020 Profitability Index Comparison Table

index	2016	2017	2018	2019	2020
Operating income (Vanke Collection group)	24047623.69	24289811.02	29767933.11	36789387.75	41911167.77
industry average	9488.41	9999.89	11530.24	14230.45	15689.31
Industry total operating income	900915163.70	958968006.40	1129245843.04	1423892424.30	1622443943.20
Vanke Group market share	2.67%	2.53%	2.64%	2.58%	2.59%
operating profit	39002277.88	5081291.64	6749861.25	7823134.21	8927894.14
Industry average value	913.47	1222.99	1893.43	2489.12	2942.19

Unit: ten thousand yuan.

Fig. 1 The price evolution of Vanke.

4. Evergrande financing analysis

Since 2016 Evergrande has benefited from demolitions. In this massive demolition supported by the state, Evergrande as well as many real estate companies emptied a large amount of inventory of houses previously accumulated in third and fourth tier cities. Not only that due to many demolished households buying new houses at that time, many real estate industries led by Evergrande even increased their prices, but even so there were still many people going to buy houses. Nevertheless, when that round of shantytown was over, Evergrande became stock again because of the large number of houses re-built before, i.e., he chose to continue gambling on a wave in order to clear this stock. 2017 Evergrande booked a loss of 7.0 billion [11].

However, for Evergrande at that time, they did not care about these losses. They thought it would successfully help them afternoon was just after the IPO and they would get more equity financing. However, on the 9th of November 2020 Evergrande announced that their plan to list on the shell of Shenzhen Housing, which they had been preparing for four years, had failed, which meant that the equity financing they had previously projected had also failed. In the same year, the state issued new financing regulations and the three red lines of real estate financing restricted a number of real estate companies. Unfortunately, Evergrande Group, which had been operating with high leverage and high debt, stepped on all three red lines and encountered bank financing risks, and Evergrande's capital chain was also in systematic risk [12].

Immediately afterwards, in 2020, the sales of Evergrande's period houses were hit hard because of the epidemic. Many houses could not be sold at low discounts. Evergrande's semi-monthly report for 2021 showed that Evergrande's contracted sales from January to June 2021 were RMB356.7 billion, but Evergrande's liabilities in one year were as high as RMB240 billion, which was mainly made up of loans and bonds from financial institutions. It also has 5,824 billion in payables due in a year, most of which is made up of commercial paper. Evergrande's sales in June July and August 2021 will total 150 billion. At the same time Evergrande expects to see a significant drop in sales in September. This has also led to a further blow to his cash flow due to the continued deterioration of his sales returns as well. The results are summarized in Table. 2 and 3. The price evolution is presented in Fig. 2.

Table 2. Loan of Evergrande in 2020 and 2021.

	loan	
	2021	2020
within a year	2,400	3355
1 to 2 years	2568	1666
2 to 5 years	1643	2035
more than 5 years	107	109
	5718	7165

Table 3. Accounts payable of Evergrande in 2020 and 2021

	Accounts payable
2021	962904
2020	838452

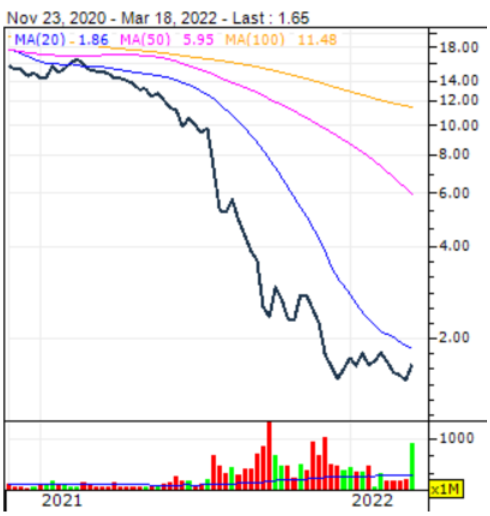

Fig. 2 The price evolution of Evergrande.

5. Comparisons and recommendations

In 2014, Vanke's Chairman Yu Liang mentioned that Chinese real estate was starting to become saturated. It meant that the market for real estate in China was not as popular after the next ten years, and he successfully listed on the Hong Kong stock market. In addition, it put the focus on property as well. 2016 saw Vanke lose its position as the top real estate seller in China for the first time, and this was when Evergrande hoped to replace Vanke as the real estate leader, and this was when Vanke started to get a lot of benefits from the newly launched demolition in 2016, not only by previously squeezed house inventory in the third-tier cities sold, but also homeopathic price increases, however this time Vanke was originally based on real estate, and later expanded its industry to add logistics, property and other businesses.

In 2017, under the process of preparing for listing, Evergrande sold all the Vanke shares previously purchased to the Shenzhen Metro Group, resulting in a loss of more than 7 billion for Evergrande at the time, which also laid the groundwork for his subsequent bankruptcy. On 9 November 2020 Evergrande however officially announced the failure of his listing plan which he had been preparing for four years. Vanke completed its first H-share offering in 2019. The year of 2021 became the only company in mainland China to carry dividends in H-shares and delivered another record one-off. Looking at the financial indicators, Vanke's gross margin is significantly higher than Evergrande's, but Evergrande's NAV remains the lowest, even though it uses many leverage benefits, but instead this has a negative impact on him, but in 2020 both companies' gross margin and NAV are declining, presumably also due to the impact of the epidemic. The Chinese real estate industry will still see a downward trend in the future and it is unlikely that prices will soar again in the short term, so companies should not rely on their capital for financing.

6. Limitations & Prospects

The real estate market is gradually saturated. The industry scale has reached its peak, and the growth rate has slowed down. The compound growth rate in the past five years is only 2.6%, and the probability of negative growth in 22 years increase. Before 16 years, the industry was in line with the growth rate of 9.7%; after 2016, it dropped to 2.6%. The growth rate has slowed down for five consecutive years, and the industry scale has peaked. There is a high probability that the follow-up will fall from a high position. The decline of the industry scale means that the cake will become smaller and smaller. Revenue continues to decline, and the sales trend of housing companies is estimated to be a 40% year-on-year decline in the cumulative sales of TOP30 housing companies from January to February. The sliding range is between 40-50%; the month-on-month decline in February 2022 is 18%, and the policy support is not effective. De-financialization of real estate companies. The scale will decline from a high level, the industry will continue to clear, and the market concentration will gradually increase. Problem housing companies thunder, industry mergers and acquisitions Increasing, small housing enterprises will gradually withdraw from the real estate industry.

7. Conclusion

In summary, Evergrande's bankruptcy was foreshadowed. One of the main reasons for Evergrande's bankruptcy, which would have been the failure of his plan to borrow money to go public, i.e., led to a huge loss in his accounts. Evergrande's story also serves as a warning to other real estate companies. In the future, the real estate market will not be as prosperous as it was in the past, but will slowly become saturated. Various policies in the future will also have many restrictions on the operation and financing of real estate companies. Vanke realized this problem early on, hence it has pursued stable development over the years. Real estate is a capital and capital-intensive industry. The current real estate financial system is in the process of gradual exploration and establishment. Under the new market environment, real estate enterprises and financial institutions should be more responsive to the market rules and seek new breakthroughs. At present, China's real estate market is gradually transitioning from a residential + incremental market to a stage of stock assets + long-term mechanism. The securitization of real estate gold financing is an important initiative for storing funds, which can enhance the management of corporate assets operations and help enterprises holding quality properties to achieve project financing or exit. Overall, these results offer a guideline for addressing the risk of real estate corporation as well as policy implementation of government.

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