

Study on Enterprises Financial Strategy Based on Life Cycle

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Keywords: Enterprise life cycle; Financial strategy; Sustainable development

Abstract: Financial strategy plays an important role in enterprise strategy. The success or failure of enterprise development is inseparable from its financial strategy. Life cycle theory is integrated into enterprise strategy and enterprise financial strategy matrix is reconstructed in the paper. Based on the analysis of the present situation of enterprise financial strategy and its related indexes, the optimization and suggestions of financial strategy are proposed to improve the management level of enterprise

1. Introduction

The Enterprise life cycle theory is an important part of enterprise growth theory. In 1972, Professor Larry E. Greiner of Harvard University put forward the concept of enterprise life cycle in his paper "Evolution and Revolution as organizations grow"[1], which is the first time to be proposed. According to the theory, the life cycle phenomenon exists in every enterprise, and all stages of enterprise's life cycle follow the similar rule. In different stages, enterprises pursue different goals, focus on different issues and different risks.

Financial strategy matrix is used to comprehensively analyze the growth value of enterprise. Based on the financial strategy matrix, it is important for value creation than simple revenue growth. Combined with life cycle theory, using the decomposition of quadrant, the financial strategy matrix can guide all the managers of the organization to pay more attention to cost control, make more effective use of the company's assets, and obtain better return on investment. Therefore, by combining the life cycle with the financial strategy matrix, it is convenient for managers to timely grasp the stage of the enterprise, so as to accurately select the corresponding financial strategy.

2. Theoretical Basis

2.1 Basic Theories of Enterprise Life Cycle.

The enterprise life cycle is very similar to the product life cycle. According to the development characteristics of enterprise, the development of an enterprise is divided into four different stages: growth period, maturity period, recession period, withdrawal period.

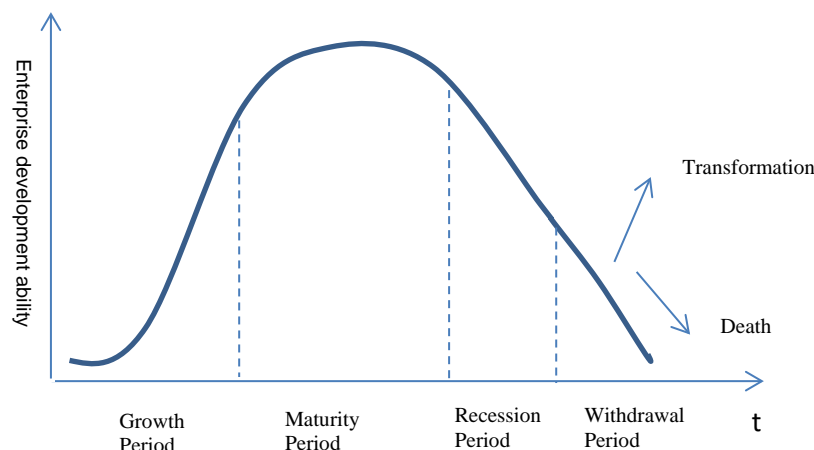


Figure. 1 Four periods of the enterprise life cycle

Generally speaking, the initial period of an enterprise is relatively short. In this paper, initial period and growth period are combined. In addition, most enterprises could not quit actively in recession period. So finally many companies can only quit passively. Under this circumstance, the enterprise recession period and withdrawal period are separately analyzed in this paper. In the recession period, the enterprise can choose strategy actively. While in the withdrawal period, the enterprise can only choose strategy passively.[2]

2.2 The Enterprise Life Cycle Embedded Financial Strategy Matrix.

In growth period, the enterprise develops rapidly. Enterprises are in a period of expansion. In this period, the production scale is expanding continuously, the business volume is rising sharply, the competitiveness of products is gradually enhanced, and the whole enterprise is innovative. However, at this time business activities are not stable. At this period, the financial characteristics of the enterprise are mainly reflected in the following aspects: the financing channels of the enterprise are constantly broadened; the capital input is constantly increased, especially the investment in technology research and development; the cash shortage leads to high operational risks.

Enterprises in the mature period tend to develop stably. Enterprises have strong competitiveness in the market. The business activities of enterprises are relatively stable and the business risks are small. Enterprises have clear strategic goals and plans. At this stage, its financial characteristics are as follows: the enterprise makes full use of financial leverage. The capital structure of enterprise is reasonable.

In a recession period, firms become less competitive. Enterprise products are gradually replaced by new products in the market. Enterprise innovation ability is insufficient. Enterprises have operational risks. Its financial characteristics manifest in these aspects: the value of the enterprise is encroaching, and the investment of enterprise is conservative. According to the early operating results of the enterprise, the enterprise still has some cash. But the cash use efficiency is insufficient.

The market competitiveness of enterprise in the recession period is weakened. Its products are gradually replaced by new products in the market. Enterprises are losing market share. The innovation ability of the enterprise is poor. The operation risk is very big in the enterprise.

Enterprises in the withdrawal period have poor long-term development ability, they lose market competitiveness and face financial risk of bankruptcy. Its financial characteristics manifest in these aspects. The profitability is almost zero or negative. They are unable to keep the daily business operation of the enterprise. The value of the enterprise is constantly being encroached.

On analyzing the enterprise value and corporate funding, enterprise's four life cycle of financial characteristics matches financial strategy matrix of the four quadrant standard. So the life cycle and financial strategy matrix can be integrated together to form a new matrix model, as shown in figure 2.

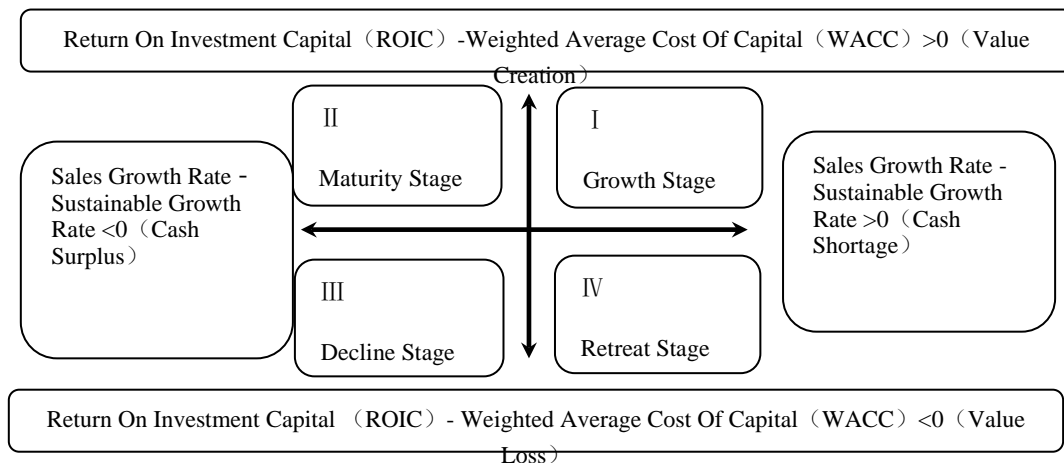


Figure. 2 Life cycle embedded financial strategy matrix

3. Study Design

3.1 Enterprise Introduction

The change on equity of enterprise will cause a large fluctuation in the sustainable growth rate. Therefore, when selecting an enterprise, we exclude enterprises with large changes on equity in recent years. The research company should be choosing among listed companies in China. J Science and Education Group Co., Ltd. (here and after referred to as “J Company”) is selected as the research object. J company was established in 1994. Since it has been established for a long time, it has passed the initial stage of the life cycle. In 1998, China Securities Regulatory Commission had approved the company to offering 30 million stocks to the public. The registered capital of J Company was changed to 100 million RMB after the stock was issued. J Company listed on the Shenzhen Stock Exchange with the stock code of 000812. J Company involves a wide range of industries, including tobacco supporting industry, education industry, real estate industry, trade industry, etc.

3.2 Data Collection.

The data of J Company provided in the paper is collected from the website of Tonghuashun.

3.3 Descriptive Statistics.

The paper uses the financial data of listed companies to calculate the financial matrix of the company. According to the calculation results, the quadrant of the enterprise is analyzed and judged, and reasonable financial advice is given to optimize the financial management of the enterprise.

4. Case Analysis of J Company

4.1 Calculation of Financial Matrix Related Indicators.

Table 1 calculation table of sustainable growth rate of J Company from 2013 to 2017

Items	2017	2016	2015	2014	2013
Sustainable Growth Rate	3.87%	3.10%	9.91%	7.97%	13.32%
Sales Growth Rate	88.13%	-10.37%	-7.50%	11.23%	5.88%

Table 2 EVA calculation table of J Company from 2013 to 2017

Items	2017	2016	2015	2014	2013
NOPAT	77458301.93	54890991.08	140115795.50	103845058.40	105234130.00
Average invested assets(RMB)	1334213061.29	1356850502.01	1316549541.53	1166922171.62	1061257848.78
WACC	9.75%	7.03%	7.32%	8.70%	11.77%
EVA	-52627471.55	-40495599.21	43744369.06	2322829.469	-19675918.8
ROIC	5.81%	4.05%	10.64%	8.90%	9.92%

Table 3 Financial strategy matrix calculation table of J company from 2013 to 2017

Items	2017	2016	2015	2014	2013
Real Growth Rate-Sustainable Growth Rate	84.26%	-13.47%	-17.41%	3.26%	-7.44%
ROIC-WACC	-3.94%	-2.98%	3.32%	0.20%	-1.85%
Quadrant	IV	III	II	I	III

4.2 Financial Matrix Analysis of J Company.

The revenues of J Company increase year-on-year with the net profit increase attributed to the parent company. The growth comes from the new projects of the real estate, which had been confirmed as income of the sales portion according to the relevant stipulations of the accounting standard in the reporting period of 2017. Removing the impact of new real estate projects on enterprise's income, and just depending on the change in EVA, the ROIC – WACC of the J Company has been negative for two years. J Company is in the third or fourth quadrant of the financial strategy matrix. This shows the characteristic of value loss.

The character of third quadrant is value loss and cash surplus. Because the existing resources are not fully utilized and the profitability is poor, the company is at risk of being merged and acquired. These kinds of enterprises should carefully analysis their future financial situation and seek new profit growth points actively. The character of fourth quadrant is value loss and cash shortage. The main problem of enterprise in the fourth quadrant is low growth rate instead of poor profitability. Simply increase the growth rate of enterprise may be harmful to its development. These kinds of enterprise should try to minimize losses in future business development.

Thus, it is suggested that J Company continue to enhance the development of its major business such as tobacco matching business and education industry. The J Company can make a breakthrough on its development through reform and innovation. Besides, J Company should pay more attention on connotation enhancement and extension development of education industry. And put education industry in front of other industries on company's industry composition. Taking trade industry subsidiary as principal part to promote industrial upgrading and explore more flourishing industrial field such as internet smart campus, and keep enlarging the trade share, keep seeking new profit growth spot. Due to the stability of the whole real estate industry, it is recommended to reduce investment of real estate industry to increase the return on investment capital.

Table 4 Analysis of J Company's financial strategy and suggestions

Financial strategy	Financial strategy and suggestions
Funding Tactics	Divest their non-core business; sell their idle asset to raise funds.
Investment strategy	Reduce investment on real estate industry; increase investment on education industry; promote the development of trade industry, turn to new investment points or investment area.
allocation strategy	Don't distribute profits, put limited resources to education, trade and new area.

5. Discussion

The choice of financial strategy should build both on macro environment and industry environment. Financial strategy matrix used in this paper is only considering sustainable growth and value growth conditions, which helps enterprise to choose proper strategy to develop itself. However, the exotic environment of enterprise is not considered in this paper. So in the subsequent studies, the exotic environment factor, which affects the choice of enterprise financial strategy, should be studied.

6. Conclusions

In this paper, Life cycle theory is combined with enterprise strategy to reconstruct enterprise financial strategy matrix. J Company is used as an example to carry on index calculation and analysis. After calculation and analysis, the proper financial strategy is proposed. The study in this paper can provide a method for enterprise to choose proper financial strategy.

Acknowledgements

The work is supported by the scientific research project of Education Department of Shaanxi Province “Research on financial strategy of sustainable development of enterprises in Shaanxi province based on enterprise life cycle”(Contract No. 18JK1053)

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