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Motivation and Performance Analysis of SUNAC's Deleveraging under the "Three Red Lines" Policy

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Abstract: High leverage is a common phenomenon in real estate enterprises, and high leverage brings high financial risks to enterprises. Effective deleveraging has a certain promotion effect on the development of real estate enterprises. Since the 2008 financial crisis, China's debt has been at a high level and has been growing at a high speed. The leverage ratio of enterprises is extremely high. When the leverage ratio is high, it increases the financial risk of enterprises. In order to gradually reduce financial risks and return the economy to normal development, it is necessary to deleverage. Based on analyzing the leverage characteristics and deleveraging paths of typical real estate enterprises, this paper explores the motivation of deleveraging and the impact of deleveraging on the performance of the enterprises, analyzes whether Sunac China is effective in deleveraging and looks forward to the future, which is expected to provide some reference value for the deleveraging of the real estate enterprises in the future.

Keywords: deleveraging, driver analysis, performance analysis, Sunac China

1. Introduction

1.1. Background of the Study

Since the financial crisis in 2008, China's debt has been at a high level and continues to grow at a high rate, and the leverage ratio of enterprises is abnormally high, which increases the financial risk of enterprises when the leverage ratio is high. To gradually reduce financial risks and return the economy to normal development, it is necessary to deleverage. Although effective results have indeed been achieved in a short period, in the last few years, high leverage is now a common problem in the country's enterprises, especially in the real estate industry. If these companies can't effectively control leverage, it will bring enterprises financial risks, and even affect the stable development of society. After 2015, the "three reductions, one reduction, and one subsidy" policy proposed by the central government, as well as the "three red lines" policy related to the real estate industry introduced in 2020, have all responded to deleveraging and emphasized the importance of deleveraging.

1.2. Significance of the Study

The main reason for choosing Sunac China as a case company is that Sunac China is the head of China's real estate listed enterprises, which has typical high leverage characteristics, and after the

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implementation of the “Three Red Lines” policy, the implementation of the significant effect in one year, from the red line file quickly to the two lines of the yellow line file of the standard, and can be done within half a year to rapidly reduce leverage to two lines to reach the standard of very few real estate companies can do, how to do in the short term to reduce leverage and according to the latest report in 2022, Sunac China return to the previous red line file enterprises, excluding the balance sheet receipts gearing ratio of up to 332%, as well as the cash short-term debt ratio of 0.05, a variety of data facts show that the Sunac China is only effective in the short term, but there are still many problems in the long-running. So it is worth exploring some problems in the process of deleveraging.

1.3. Research Ideas

This paper analyzes the specific path of deleveraging of Sunac China, analyzes the motivation for deleveraging of Sunac China according to the specific methods, and analyzes it from both positive and negative aspects; then analyzes the effect of deleveraging of Sunac China, reflects the effect of deleveraging of the enterprises through the financial performance and non-financial performance, and discovers the problems that may exist in the short term of rapid deleveraging, and finally sums up the outlook in the future.

2. Review of National and International Literature

2.1. Pathways to Deleveraging and Other Related Studies

Regarding the research on the path of deleveraging, Velimir Bole suggests that, macroscopically, it is recommended to emphasize deleveraging based on the sound of the financial and fiscal system [1]. Bole and Trobec study the implementation process of deleveraging process requires the central bank to stand for a perspective to focus on the stability of the financial system [2]. Li compares equity financing and debt financing and argues that equity financing plays an important role in reducing corporate leverage [3]. Xu and Wang argue that scaling back credit to state-owned enterprises and increasing credit to private enterprises can simultaneously achieve structural deleveraging and stable growth [4]. Rogoff seems that excessive leverage is prone to liquidity risk and will increase the chances of financial crisis [5]. Xu et al. verified the relationship between inventory and deleveraging policy through the double-difference method and found that inventory turnover plays a mediator role in the relationship between the deleveraging policy and the ability of enterprise development [6].

2.2. Analytical Study of the Drivers of Deleveraging

In foreign scholars, Bernanke found that excessive corporate leverage has a significant negative impact on the economic growth and financial stability of enterprises [7]. Xavier summarized and analyzed that the reason why enterprises need to deleverage is due to the decrease in consumer demand and low productivity, resulting in increased debt repayment pressure and increasing debt ratio. Therefore, it is necessary to reduce leverage to reduce debt ratio [8]. Ahmed, through research on the company’s leverage ratio, it is clear that a high leverage ratio will make the company more susceptible to negative impacts from external economic environment changes. He believes that maintaining a reasonable leverage ratio can effectively maintain the stable development of the company [9]. Ma and Yu, the research on the relationship between economic growth and leverage shows that within a certain range, deleveraging can promote economic growth, and beyond this range, deleveraging can suppress economic growth [10]. Zhang believes that some companies’ leverage ratios have reached the upper limit of risk tolerance, and cyclical sectors’ leverage ratios have risen rapidly, which may trigger debt problems [11]. Wang pointed out that excessive leverage ratio will increase the pressure on enterprises to repay debts, increase financial risks, and then transmit them from the physical sector to the financial sector, causing instability in the financial system and breeding systemic financial risks [12]. Tan found that the long-term solvency of highly leveraged enterprises is weak, and the solvency of most enterprises has deteriorated in the past two years. The structural characteristics and potential risks exhibited by Chinese enterprises' leverage ratios are related to differences in enterprise characteristics, asset prices, and the evolution of the macroeconomic policy environment [13].

2.3. Performance-Related Studies on Deleveraging

Corporate performance has been a powerful tool for assessing the business conditions of enterprises. A part of scholars has studied the impact of deleveraging on corporate financial performance. Many domestic and foreign scholars analyze the impact on corporate financial performance from the perspectives of the company's capital structure, the four major indicators mainly profitability, and the company's size decision. Qiu and Cheng jointly found that deleveraging can reduce debt costs, be more conducive to corporate investment, and demonstrate better business performance [14]. Shen studied the impact of debt-to-equity deleveraging on the financial performance of Yunnan Tin Industry Company and found that all four indicators have improved. The conclusion indicates that the financial situation of the company has been alleviated, and operational efficiency has significantly improved [15]. Zhang conducted empirical research to demonstrate that deleveraging debt companies in the past can improve their financial performance, and financial risk plays a mediating role in it. The company should set an appropriate asset-liability ratio based on its situation, reduce financial risks, and achieve long-term development [16]. Most domestic and foreign scholars have also empirically measured the impact of deleveraging on corporate performance. Oyakhilome analyzed the negative impact of financial leverage on corporate performance and profitability through empirical linear regression analysis [17]. Morri mentioned that the impact of deleveraging on performance is studied and analyzed separately from two aspects: capital structure and debt level [18]. Panagiota et al. aimed to study the impact of financial leverage on fintech companies and found that financial leverage harms corporate profitability and performance [19]. Wang et al. used the double difference method to analyze the causal effect of deleveraging on corporate performance, and found that deleveraging policies significantly affect corporate performance by improving debt repayment ability and reducing financial risks [20].

2.4. Literature Review Summary

Through the summarization and conclusions of domestic and international literature research, there are many types of research on deleveraging, domestic and international scholars summarize the research related to deleveraging from the impact on enterprise financial risk, enterprise financial risk, and enterprise asset allocation, as well as the relationship with inventory, and even the promotion of the asset utilization rate and other factors to explore the deleveraging research. For the way of deleveraging mainly from equity financing, government intervention, the issuance of new shares, and other methods of deleveraging, at the same time found that many scholars on the drivers of deleveraging and performance of certain research analysis, the study is mostly considered from the macro and micro perspective of the market environment and leverage and other aspects of the analysis of the enterprise why the need to deleveraging, the macro level is linked to the economy, consumers, moderate deleveraging. It is conducive to the rapid development of enterprises, and on the micro level, it is found that the reasons for deleveraging are mostly due to the increased pressure of enterprises to repay debts, elevated financial risks, and the debt ratio is only increasing; now, scholars mainly analyze the financial performance of enterprises from the aspects of society, epidemic, and corporate decision-making, etc. Most of the deleveraging is positive to the four major indexes of financial

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performance, and a few of them have pointed out that there are still some problems in the middle; the analysis of the performance of enterprises mainly adopts double-differential analysis, which is the most important method. Performance analysis mainly adopts double different methods and factor analysis methods to analyze the enterprise performance through empirical research industry listed companies related data, mentioning the enterprise through improving solvency, profitability, cost reduction, cost stickiness, and other aspects to affect the enterprise performance.

3. Industry Background of Sunac China

3.1. Basic Situation of China's Real Estate Industry

As a basic and leading industry of China's national economy, real estate plays an important role in China's economic growth. The GDP of the real estate industry will account for close to 6.5% of the total GDP of the gross national product in 2022, and the overall leverage ratio of the real estate industry (part of the GDP/total GDP) is also on the high side from a macro point of view. However, as a capital-intensive industry, real estate enterprises need a lot of capital, and its entire recovery cycle is very long, from the acquisition of land for a project to enter the market sales, then to deliver the property, the enterprise needs to continue for several years of a large amount of cash flow to support; not to mention that, for large and medium-sized enterprises, it is often several projects are developed at the same time, so for the demand for capital is huge, such as a project investment is not produced, it could be hundreds of millions of dollars. For most enterprises, it is difficult to meet their own development needs by relying solely on their capital flow, so they need to ensure that the development and sales of the company's capital flow through continuous financing, as shown in Figure 1.

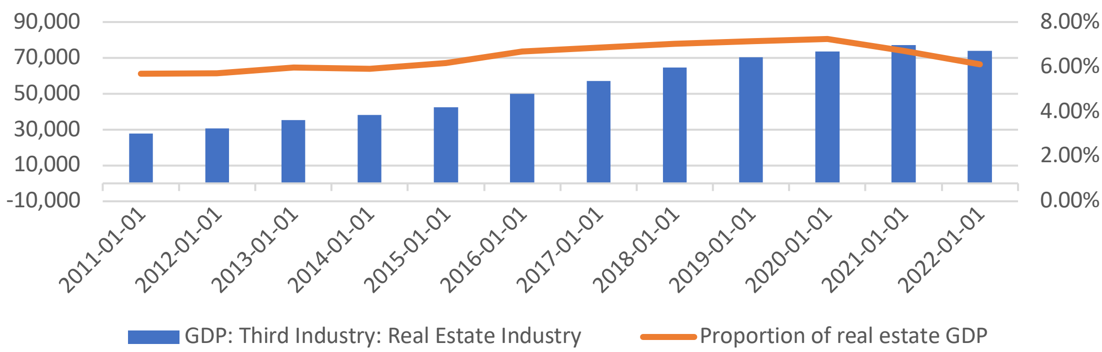

Figure 1: The proportion and proportion change of GDP in China's real estate industry from 2011 to 2022.

According to Figure 2, it can be seen that the proportion of indirect financing of China's real estate enterprises exceeds 80% almost every year, while direct financing accounts for less than one-fifth of the total financing. The common financing in China includes bank loans, credit loans, and so on. More listed companies in China's real estate industry choose debt financing, then equity financing and the proportion of endogenous financing is smallest. This high-debt, low endogenous financing structure is not conducive to the good development of the real estate industry, because the enterprise should have cost consciousness, to use the least amount of money to achieve maximum value. While endogenous financing is supposed to be an effective and safe financing method for enterprises to prioritize, if they choose to give up this method due to the limitations of their business operation and blindly raise their debts to finance, it is difficult to maintain the long-term development of the enterprises in this way.

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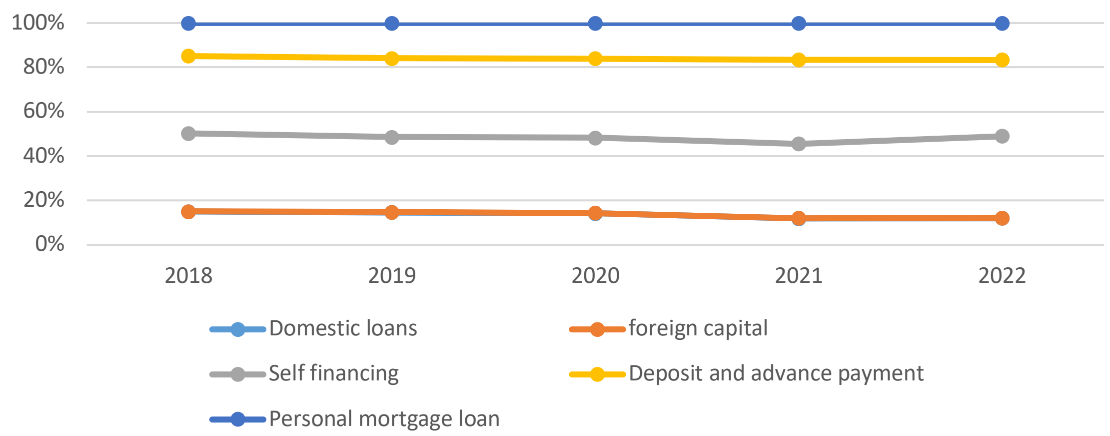

Figure 2: Composition of Actual Funding Sources in China's Real Estate Sector as a percentage from 2018 to 2022.

3.1.1. Current Status of Major Levers in China's Real Estate Industry

Since 2008, the financial crisis has greatly impacted the economic development of various industries in China, including the real estate industry. After a major shock, China introduced a series of stimulus policies to achieve economic recovery, including ten measures to expand domestic demand and the "Four Trillion Investment Plan". President Xi Jinping's "Three Goes, One Down, One Supplement" policy at the Central Committee meeting and the imminent need for "deleveraging" in the real estate industry. According to the relevant research and analysis, the real estate industry in recent years in keeping up with the development of national policies and their conditions, its leverage rate has maintained at about 70% high. In 2022, the "Three Red Lines" policy was introduced after a slight improvement, but not much, which also caused the central government to promote a deleveraging process. As a leading enterprise in China's real estate industry, Sunac China Holding Limited has been keeping up with the development of the times.

3.1.2. Analysis of the Causes of the Deleveraging in the Real Estate Industry

Deleveraging is a development in line with policy trends: In recent years for the real estate industry, the state and competent agencies continue to tighten the real estate industry financing environment and regulatory provisions, including the need to maintain the security of the financing system. In the period of rapid development of the real estate industry, many real estate enterprises seized market opportunities, pursued investment returns, in keeping with the policy environment, to diversify the way multi-channel to increase investment and financing efforts, China's real estate industry, the main focus of bank loans as the main way of financing to raise funds.

Since real estate companies are not isolated and often involve many upstream and downstream sectors of a project's operations, developments in the real estate industry may also affect these sectors, bringing better operational benefits or increasing risks. Real estate companies are more affected by industry policies. In a political environment where external financing sources are tightening, cash flow is likely to collapse if highly leveraged companies cannot keep up with their turnaround capacity, leading to a cross between real estate companies and financial institutions defaults, The bond market poses more serious financial risks. Therefore, to maintain the security of the financial system, the funds flow of the real estate sector must be controlled. Also, our real estate enterprises must comply with national policies, abide by the relevant regulations, and control corporate debts and liabilities.

Deleveraging is a requirement to reduce business risks: While many real estate companies do their best to raise capital to increase leverage to expand and capture markets, not all of them can make economic value out of that credit capital. Many highly leveraged real estate companies are passively mired in new debt to pay off debt. In addition, under the high-leverage mode of operation, the capital chain of the company is relatively tight, and the company's ability to resist risk is weak, while the real estate industry itself is a capital-intensive industry with a long capital recovery cycle, and it is an industry that is influenced by policies. For some small and medium-sized real estate companies, when the real estate market is in good condition, the leveraged expansion mode can still be maintained, but once the sales receipts can not be paid back promptly, it may be caught in a vicious circle of borrowing new and repaying the old, and even borrowing new and repaying the old is difficult to maintain, and at this time, the company's capital chain will be at risk of default. Therefore, to reduce the operating risks of real estate companies, and better comply with the development of the environment, the real estate industry must go to deleverage.

3.2. Sunac China Case Study

3.2.1. Basic Overview of Sunac China

Founded in 2003, Sunac China was successfully listed in Hong Kong in 2010. Two years later, Sunac China moved into the mainland and formed a strategic layout of five core cities, namely Beijing, Tianjin, Shanghai, Chongqing, and Hangzhou, with a wide range of projects from development to sales. After nearly a decade of steady development, Sunac China is also the largest property owner and one of the largest cultural operators in China. Sunac China is the largest property holder and operator in China. Sunac China is a national leader in industrial integration and operation, as well as in comprehensive urban development. Sunac China has developed for 18 years, in which real estate has always been its core industry. While doing a good job in real estate, Sunac China has also ventured into the five sectors of conferences and exhibitions, services, healthcare, recreation and tourism, and culture. In 2020, Sunac China's real estate sales were ranked fourth for four consecutive years. In addition, Sunac's overall strength has been ranked among the top ten estate enterprises in China and the first place of super product power of Chinese Real Estate Enterprises.

3.2.2. Leverage Situation of Sunac China Before the Introduction of the "Three Red Lines" Policy

Revenue of Sunac China: According to Figure 3, the operating income of Sunac China has been growing steadily since 2015. In the middle, costs maintain the same trend, suggesting that Sunac China is expanding until 2020. While it can be seen that from 2015 to 2017 the growth rate of operating income has been rising, the enterprise is accelerating the expansion, and in 2019, the growth rate slowed down, which also indicates that the expansion speed of Sunac China is decelerating. In 2016, Sunac China was attempting to hoard a large amount of land, which led to the growth of revenues and the net profit instead of the decline of the situation. In 2017 the revenues were still in the upward growth and the growth rate of the net profit reached more than twice, which is also been in an upward phase. This shows that the overall revenue capacity of Sunac China is relatively robust and has been in a steady state of profitability.

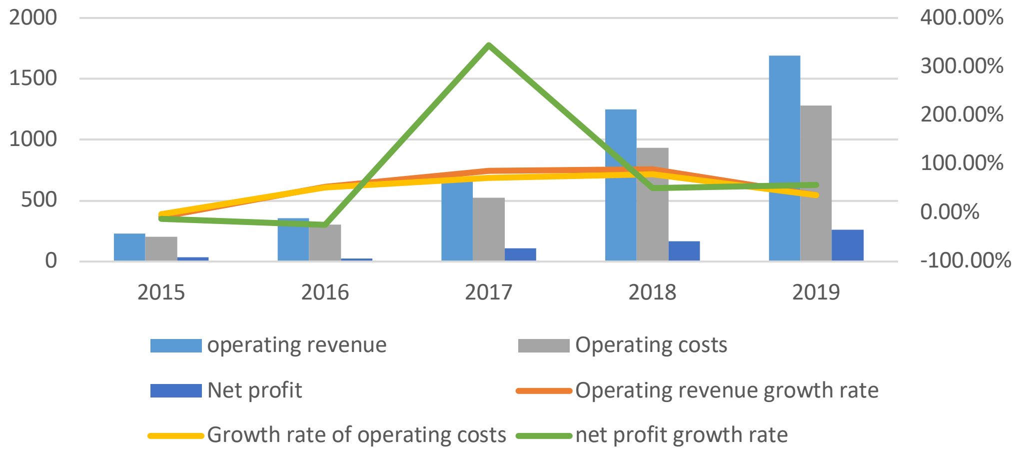

Figure 3: Line Chart of Selected Financial Data of Sunac China, 2015-2019.

Business Strategy of Sunac China: Sunac China has diversified its strategic development with real estate as its core and center of gravity, and its total business scope consists of six business segments, namely Sunac China Real Estate, Sunac China Services, Sunac China Cultural Tourism, Sunac China Culture, Sunac China Conferences and Exhibitions, and Sunac China Healthcare and Recreation. The specific business of these six operating segments covers all aspects of real estate development, property services, conferences and exhibitions, tourism and vacation, theme parks, commercial operations, hotel operations, medical and recreation, IP development and operations, and film and television content production and distribution. According to the company's annual report, the amount of sales revenue from 2017 to 2020 has been increasing along with the expansion of the company's sales, which shows that Sunac China is mainly focusing on sales operations, and the proportion of sales has been increasing.

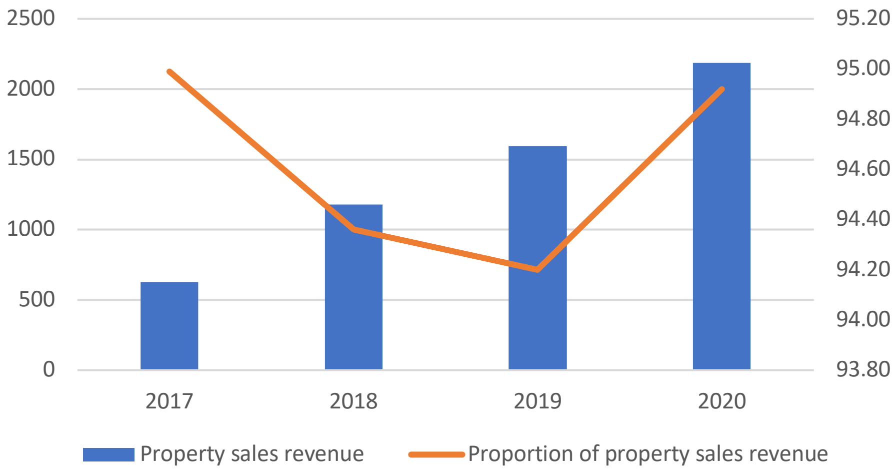

Figure 4: Breakdown of sales revenue of Sunac China from 2020 to 2019.

Leverage of Sunac China: In 2016 and 2017, Sunac China's debt ratio reached a historic high. According to the data, from 2016 to 2017, as analyzed above, Sunac China's revenue significantly increased, and during this period, Sunac China's financing scale experienced a significant increase. In 2016, the financing scale of Sunac China increased to 122.1 billion yuan, while in 2015, this amount was 35.2 billion yuan, an increase of 246% year-on-year in 2016. Since then, the annual

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financing scale of Sunac China has never been less than 100 billion yuan. From Figure 5, it can be seen that Sunac China's financing method is mainly through borrowing and issuing common stock company bonds, which is mainly through debt financing, while equity financing is relatively rare. This approach can retain control of the company, but it will increase the company's debt ratio, which will impose a certain burden on the company's financial flow.

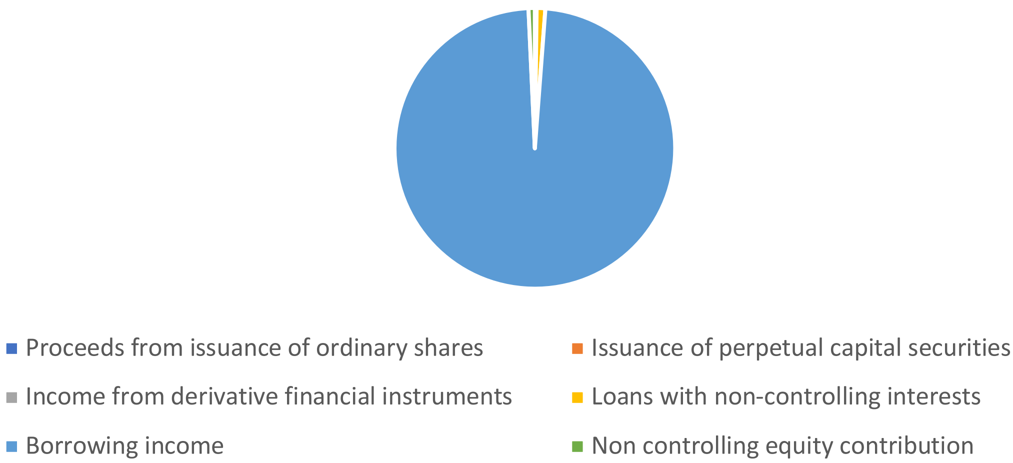

Figure 5: Proportion of Financing Structure in Sunac China from 2018 to 2019.

The "Three Red Lines" policy issued by the Central United Ministry of Housing and Urban-Rural Development requires pilot real estate enterprises: the asset-liability ratio excluding advance payments shall not exceed 70%; The net debt ratio shall not exceed 100%; The cash to debt ratio shall not be less than one time. According to the touchline situation of the "Three Red Lines", real estate enterprises are divided into four levels: "red, orange, yellow, and green". If all three red lines touch, it is in the red gear; if two lines are touched, it is in the orange range; if a line is touched, it is in yellow gear; if none of the three red lines are touched, it is in the green gear. Before the policy implementation of Sunac China, which is before 2021, all three indicators did not meet the standards and were listed as red-line enterprises. According to the changes in the graph, it can also be seen that Sunac China has transformed from a red-line enterprise to a yellow-line enterprise that meets two standards in six months, indicating that the effect of deleveraging is rapid and significant, as shown in Figure 6, Figure 7 and Figure 8.

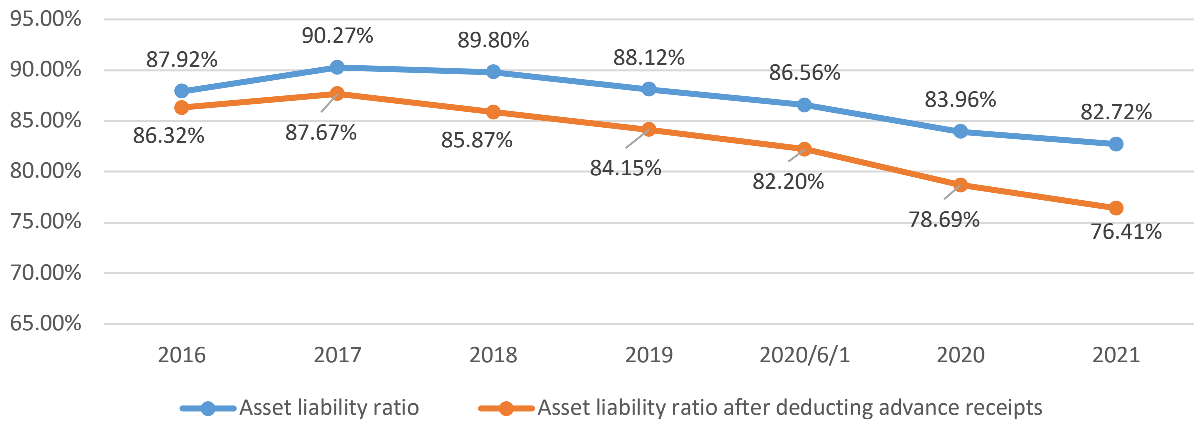

Figure 6: Changes in Indicators Related to Sunac China's "Three Red Lines" Policy - Asset Liability Ratio.

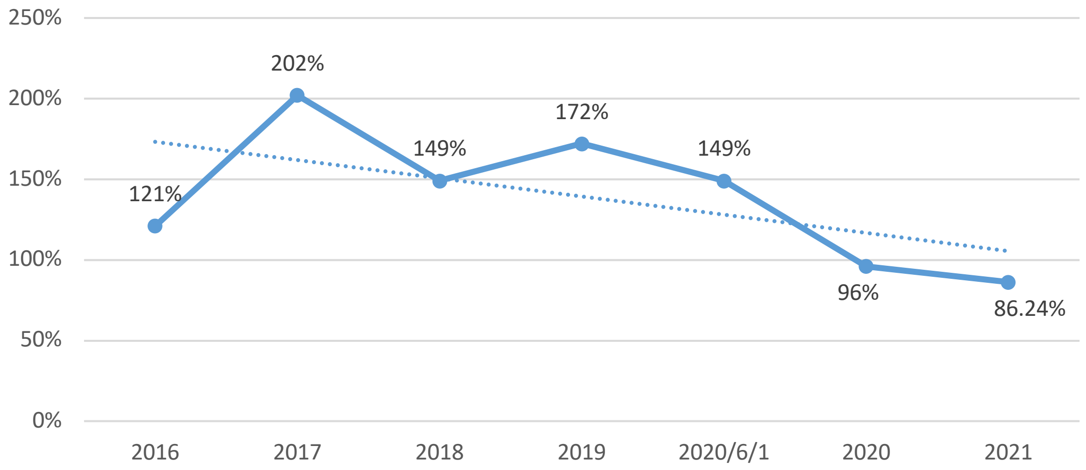

Figure 7: Changes in Indicators Related to Sunac China's "Three Red Lines" Policy - Net Debt Ratio.

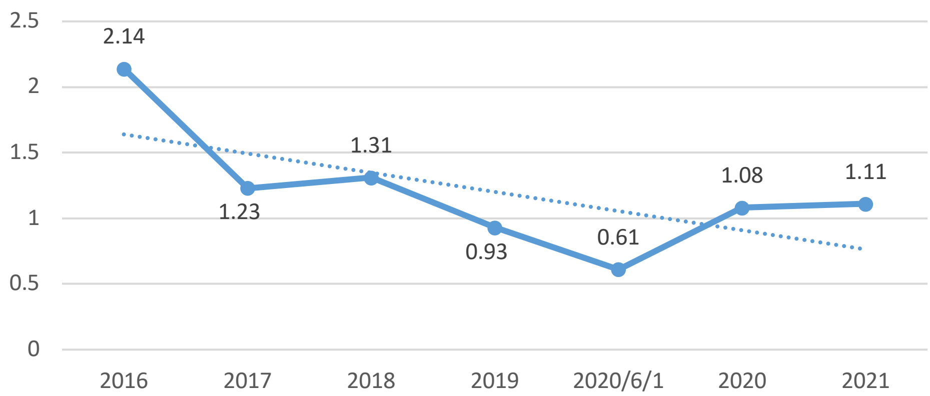

Figure 8: Changes in Indicators Related to Sunac China's "Three Red Lines" Policy - Cash Short Debt Ratio.

4. An Analysis of the Drivers of Deleveraging in Sunac China

4.1. A Brief Analysis of the Deleveraging Implementation Path

Firstly, Sunac China took the initiative to control the scale of interest-bearing liabilities, decreasing from 322.9 billion in 2019 to 304.1 billion in 2020, a decrease of 6%; At the same time, the structure of interest-bearing liabilities was adjusted, and Sunac issued long-term credit bonds and other securities in 2020 to replace short-term maturing debts. By the end of 2020, in the interest-bearing debt structure of Sunac China, the amount of long-term debt is 2.31 times that of short-term debt, and the proportion of long-term interest-bearing debt in interest-bearing debt has significantly increased. In addition, Sunac China significantly slowed down its pace of land acquisition in 2020. According to statistics from Zhongyuan Real Estate, the total new land acquisition amount of Sunac China in the first and second quarters of 2020 was 233 billion yuan, while the land acquisition amount in the first two quarters of 2019 was as high as 648.3 billion yuan, reflecting that Sunac has slowed down its own pace of land acquisition and avoided the situation of high enthusiasm and high prices in the second quarter of the land market. Throughout 2020, the land acquisition area of Sunac China significantly decreased to 23.84 million square meters, a year-on-year decrease of 41.1%; The land sales ratio is 0.54, a decrease of 0.2 compared to 2019, indicating a significant decrease in land acquisition efforts.

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4.2. Analysis of Underlying Factors

4.2.1. Strategically: Recognize the Reality and Plan for a Rainy Day

In 2019, Sunac China included “controlling debt and reducing leverage” in its three-year key plan. Based on ensuring a relatively stable net debt scale, as analyzed earlier, it vigorously acquired land, reduced the debt ratio, and optimized the leverage ratio by accelerating profit realization and thickening equity. Sunac China focuses on real estate as its core and core business, and its total business scope consists of six major sectors: Sunac China Real Estate, Sunac China Services, Sunac China Culture, Sunac China Conference and Exhibition, and Sunac China Medical and Health Care. The specific businesses of these six business sectors cover various aspects such as real estate development, property services, conference and exhibition, tourism and vacation, theme parks, commercial operations, hotel operations, medical care, IP development and operation, and film and television content production and distribution. It is precisely because of the advanced strategic arrangement that sets the overall tone for Sunac China that Sunac China can quickly achieve its goal of reducing leverage after the release of the three red-line financing regulations.

4.2.2. Operationally: Active Revenue Generation to Maintain Great

In the past three years, Sunac China’s total operating revenue has been 126.245 billion yuan, 171.974 billion yuan, and 233.048 billion yuan, respectively, maintaining a sustained growth trend; At the same time, the net profit of each year was 16.567 billion yuan, 26.028 billion yuan, and 35.644 billion yuan, respectively, maintaining a growth trend. Stable net profit directly contributes to the owner’s equity of the enterprise, which is the most direct method for the healthy deleveraging of the enterprise, as shown in Figure 10.

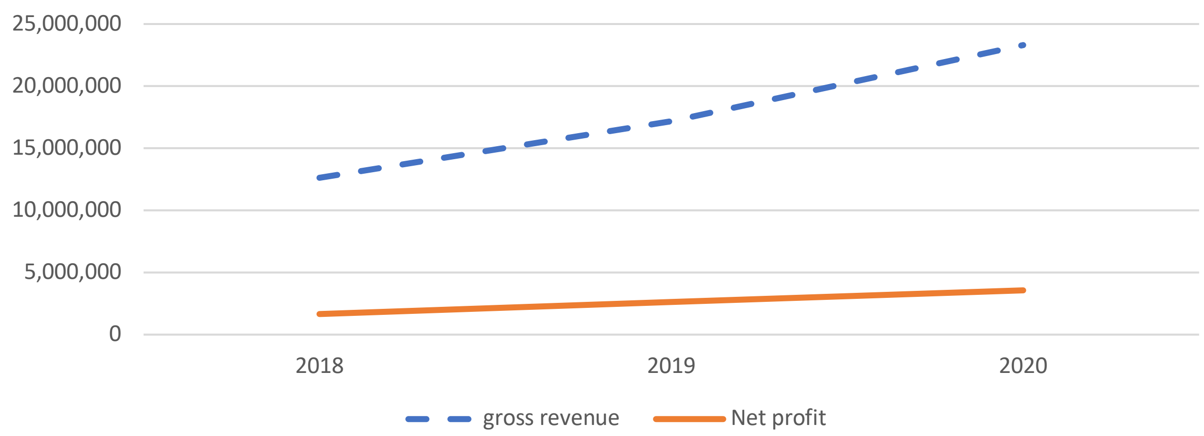

Figure 9: Changes in operating income and net profit of Sunac China, 2018-2020.

In terms of cash flow, as shown in Figure 10, Sunac China’s cash flow has also been developing steadily over the past three years, with strong cash management capabilities keeping its ending cash and cash equivalents balance rising steadily. Continuously rising net profit and operating income, as well as cash returns, set a good tone for Sunac China’s development and provided a basic guarantee for the company’s deleveraging.

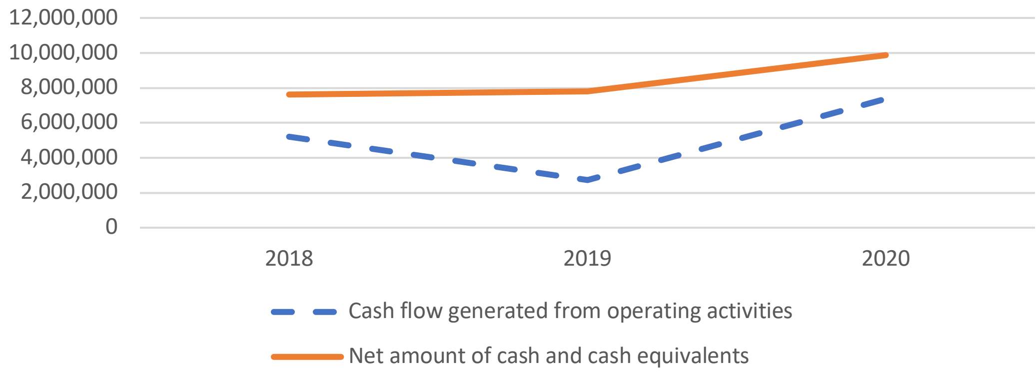

Figure 10: Changes in cash flows in cash flows from operating activities of Sunac China, 2018-2020.

4.2.3. Debt Pressure From Frequent Mergers and Acquisitions

Starting in 2012, Sunac China began to acquire projects and land across the country. In the history of high-speed mergers and acquisitions, there have been well-known real estates companies such as Greentown, KAISA, Yurun, Raycom, Jinke, and Wanda. Although there are successes and failures, the successive mergers and acquisitions have continued to increase Sunac China's popularity as well as its ability to expand. In 2017, it was even more fierce, launching 10 consecutive mergers and acquisitions, including participation in Wanda's "merger of the century". According to statistics, Sunac's mergers and acquisitions involved an amount of up to 106.50 billion yuan. Sunac China seized high-quality land in the market for construction, building, and sales. Because acquiring land requires a large amount of capital, which usually needs to be delivered as soon as possible, real estate companies usually maintain a high leverage ratio, and the faster the company grows, the higher the leverage ratio is. While expanding its power through mergers and acquisitions Sunac has also gained a certain asset base for subsequent deleveraging. Through successive mergers and acquisitions of several well-known enterprises, Sunac China has also acquired a large number of high-quality land reserves at seasonable land prices, which will support the group's sound development in the future, but the mergers and acquisitions have brought considerable pressure on operating liabilities.

4.2.4. Debt Financing Accounts for a Relatively Large Proportion of Financing Modalities

The significant increase in the financing scale of Sunac China is mainly due to its rapid increase in land reserves through mergers and acquisitions in the past two years. In 2016, Sunac China achieved a total of 16 mergers and acquisitions with a total investment of over 59.5 billion yuan; In 2017, although Sunac China did not have as many M&A projects as in 2016, with only 10 M&A projects throughout the year, the funds involved were far ahead of the previous year, reaching 95 billion yuan, including a 91% equity stake in 13 cultural tourism projects of Dalian Wanda Commercial Real Estate Co., Ltd. ("Dalian Wanda Commercial"), which cost 43.844 billion yuan to acquire, This has laid the foundation for the development and diversified transformation of Sunac China's cultural and tourism sector. The increase in M&A projects will naturally lead to an increase in the cash flow required for the acquisition. With the expansion of the land reserve layout of Sunac China, the financial pressure on Sunac China is also increasing. Sunac China borrowed a huge amount of funds due to its early large-scale land acquisition. Once the funds cannot be withdrawn or the withdrawal speed is too slow, Sunac China will need to bear a huge amount of debt, and may even need bankruptcy liquidation to repay the debt. The enterprise bears enormous financial risks.

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4.2.5. Unreasonable Capital Structure and High Financing Costs

The current liabilities of Sunac China accounted for a relatively high proportion and remained stable for several years. In 2016 and 2017, Sunac China made a large number of land acquisitions and obtained funds through debt financing, which led to a high proportion of current liabilities in total liabilities, increased short-term debt repayment pressure, and a high gearing ratio. Meanwhile, with the development of the company's strategy, the equity ratio was also been at a high level until the introduction of the policy in 2020, when there was a very obvious improvement. According to the specific situation of Sunac China, it should integrate all factors, adjust the ratio of long-term liabilities to short-term liabilities to a reasonable range, and optimize the debt structure, so that the debt risk of Sunac China can be reduced and the debt ratio of the enterprise can be maintained at a reasonable level, and improve the quality of the enterprise's operation. In addition, Sunac should also strengthen its internal governance and improve the quality of its operations, to reduce the risks faced by the company, as shown in Table 1 and Figure 11.

Table1: Capital structure data of Sunac China.

Year	Asset liability ratio	equity ratio	Current liabilities/total liabilities	Non-current liabilities/total liabilities
2016	87.92%	7.28	55.82%	44.18%
2017	90.27%	9.28	75.15%	24.85%
2018	89.80%	8.8	65.44%	34.56%
2019	88.12%	7.42	71.08%	28.92%
2020	83.96%	5.23	73.49%	32.88%
2021	89.40%	8.44	89.17%	34.60%

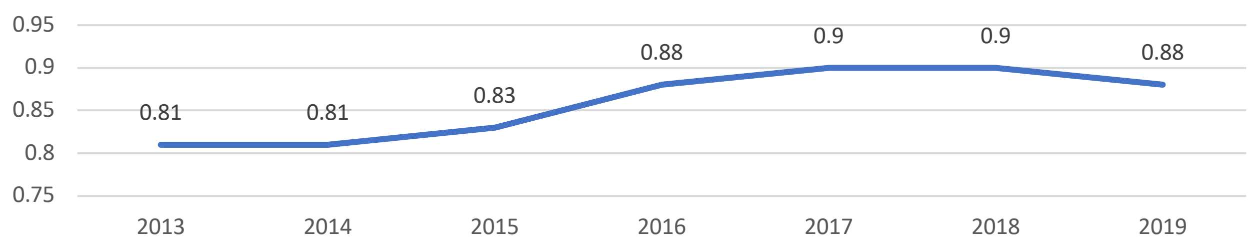

Figure 11: Change in Gearing Ratio of Sunac China, 2013-2019.

5. Performance Analysis of Deleveraging in Sunac China

5.1. Financial Performance Analysis

5.1.1. Solvency Indicators

As can be seen from Table 2, the quick and current ratios have been declining since 2017, reflecting the fact that the financing of the company has not been fully utilized. The quick assets of Sunac China are not enough to offset its current liabilities. According to the analysis above, Sunac China has been buying a lot of land during the deleveraging period, resulting in increased pressure on its liabilities, which in turn has caused two major indicators to decline and its short-term solvency to weaken.

Table 2: Analysis of solvency Indicators of Sunac China, 2017-2021.

Year	Current ratio	Quick ratio	Asset liability ratio(%)
2017	1.30	0.48	90.27
2018	1.17	0.45	89.80
2019	1.17	0.39	88.12
2020	1.22	0.39	83.96
2021	0.97	0.25	89.40

5.1.2. Profitability Indicators

From Table 3, it can be seen that the overall profitability indicators of Sunac China are showing an upward trend, with an upward trend before effective deleveraging in 2020 and a decline due to the epidemic after 2020. The net profit margin on sales can reflect the level of return on sales revenue of a company over a certain period. From Table 2, it can be seen that the net profit margin on sales of Sunac China increased significantly in 2017 and reached its peak, followed by a decline. It returned to its peak in 2020 and did a lot of work before deleveraging. However, it showed a negative value in 2021, which greatly affected the net profit margin on sales and return on equity.

Table 3: Analysis of Profitability Indicators of Sunac China, 2017-2021.

Year	Net profit margin on sales %	Roe %	Earnings per share growth rate %
2017	17.71	32.81	2.89
2018	13.98	32.92	0.37
2019	16.63	37.21	0.58
2020	17.15	34.16	0.31
2021	-21.17	-36.78	-2.06

5.1.3. Indicators of Operational Capacity

From Table 4, it can be seen that before effectively achieving the goal of deleveraging, Sunac China had significant growth in all three indicators before 2020, but quickly fell back to the previous values in 2021, indicating that Sunac China had made various strategies to respond to the introduction of policies before the introduction of the “three red lines”.

Table 4: Analysis of Operating Capacity Indicators of Sunac China, 2017-2021.

Year	Inventory turnover rate	Fixed asset turnover	Total Asset turnover
2017	0.24	3.35	0.15
2018	0.29	2.85	0.19
2019	0.31	2.88	0.21
2020	0.35	2.99	0.23
2021	0.32	2.31	0.18

5.1.4. Capacity Development Indicators

From Table 5, it can be seen that the total asset growth rate, net profit growth rate, and revenue growth rate of each major indicator are significantly decreasing, which directly reflects the overall operating level of the enterprise and whether it can efficiently profit in the future. Although the deleveraging effect of Sunac China is obvious, in terms of recent development, it has not been very beneficial for revenue and profit.

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Table 5: Analysis of Development Capacity Indicators of Sunac China, 2017-2021.

Year	Total Assets Growth Rate %	Net profit growth rate %	Operating revenue growth rate %
2017	112.53	344	86.80
2018	15,01	50.55	89.52
2019	34.05	57.11	36.22
2020	15.38	36.95	35.51
2021	6.15	-207.35	-14.12

5.2. Non-Financial Performance Analysis

5.2.1. Protection of Creditor's Rights and Interests

The demand for funds by real estate enterprises is enormous, but due to the current slower development speed of the real estate industry, this reflects the importance of the scale of real estate enterprises. Large-scale enterprises have a better chance of surviving in this unfavorable environment, but large-scale enterprises often come with greater financial needs. Enterprise funds generally consist of self-owned funds and funds borrowed from external sources through various financing channels. Investors with their funds belong to the owners of the enterprise, while funds borrowed through financing tools belong to creditors. From the financial statements of Sunac China, it can be seen that the proportion of borrowed funds in its capital structure is relatively large, which means that protecting the rights and interests of creditors is very important for Sunac China. Creditors are in a passive position as they no longer have any rights related to the company other than those stipulated in the contract they have signed. Once the company is unable to repay its debts on time, the rights and interests of creditors will be lost. Therefore, the efficient and stable operation of Sunac China is very important for creditors. The deleveraging of Sunac China is conducive to the stable operation of the enterprise and also helps to protect the rights and interests of creditors.

5.2.2. Reducing Corporate Financial Risk

The financing methods of enterprises can be roughly divided into two categories. The first type is owner investment, which has little risk as the funds belong to the company's assets and there is no pressure to repay them. Even if the company's efficiency is not high due to poor management, there is no need to worry about not being able to pay off the debts. The owner needs to bear this part of the loss on their own. However, Sunac China belongs to a listed company, and if poorly managed, it will directly lead to a decline in the company's stock, making it impossible to raise enough funds in the capital market to ensure the normal operation of the enterprise. The second type is borrowing funds from external sources, and the risks of this type of financing method are much greater than those of the first type. The funds borrowed from external sources still need to be repaid, often accompanied by high-interest rates and limited repayment periods, which will bring great pressure to enterprises. Sunac China borrowed a huge amount of funds due to its early large-scale land acquisition. Once the funds cannot be withdrawn or the withdrawal speed is too slow, Sunac China will need to bear a huge amount of debt, and may even need bankruptcy liquidation to repay the debt. The enterprise bears enormous financial risks. Therefore, Sunac China actively carries out deleveraging to enhance the company's debt repayment and financing capabilities, which is conducive to reducing the company's financial risks.

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6. Conclusions and Outlook

Sunac China has done a lot of measures strategy in the whole deleveraging process, the overall is more benefits, but it also does have some problems caused by some of the enterprise's financial indicators in the deleveraging after a substantial deterioration, through the above analysis summaries some experiences. Through the strategy, financing structure, capital organization, business management, and other aspects of the future of Sunac China with a development perspective.

6.1. Broadening of Financing Channels

The main financing channel for Chinese real estate enterprises is still bank loans, but through comparison, it is found that the proportion of bank loans by Rongchuang China is relatively higher. In the current environment where the government restricts a large amount of bank funds from flowing to real estate enterprises, real estate enterprises can no longer rely too much on banks as traditional financing channels to raise funds. Rongchuang China should try its best to innovate and expand financing channels.

6.2. Improvement of Capital Structure

As the higher debt of Sunac China has caused an increase in financing costs, it harms the performance of the company. Therefore, based on controlling the continued increase in the scale of debt, Sunac China should broaden its financing channels and increase the raising of funds that do not require the payment of interest, to reduce financing costs and enhance its performance. Excessive debt is mainly caused by its excessive interest-bearing liabilities, and high dividends despite insufficient cash. Therefore, enterprises should control the scale of liabilities from the following aspects. On the one hand, to reduce the scale of interest-bearing liabilities. On the other hand, to increase the endogenous funds and reduce the dependence on liabilities.

6.3. Maintaining Corporate Sustainability

Wang Mengde, executive director and chief executive officer of Sunac China said, under the influence of many factors, the real estate market in 2021 has entered a period of downturn. How to break the game for various product brands has become a major concern in the industry. As a veteran real estate developer, Sunac China has taken the lead in launching a new strategic layout and strengthening the real estate business upgrade, to seek sustainable and efficient development. In recent years, as the epidemic subsided, the real estate industry began to recover, releasing pent-up demand for housing. These gradually recovering market conditions have also given Sunac China more opportunities to generate more profits. At the same time, the People's Bank of China and the China Banking Regulatory Commission have adjusted the differentiated housing credit policy, giving real estate enterprises more room for lending. These favorable conditions have given the real estate industry more hope, and have seen better room for development for Sunac China in the future.

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