Issues and Optimization Strategies in Corporate Investment and Financing Decisions

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Abstract: Since the beginning of the reform and opening-up policy, China has witnessed the emergence of numerous outstanding small and medium-sized enterprises (SMEs). However, these enterprises have been confronted with difficulties in making investment and financing decisions. In order to achieve sustained and healthy development, it is essential to address the challenges pertaining to investment and financing in enterprises. This paper provides an overview of the concept of corporate investment and financing, identifies four key issues in the current landscape, namely information asymmetry, lack of risk prevention capabilities, limited investment and financing channels, and inadequate management mechanisms. The causes and consequences of these issues are analyzed, and corresponding optimization strategies are proposed from both government and enterprise perspectives to enhance the accuracy and scientificity of investment and financing decision-making.

Keywords: Corporate investment; Corporate Financing; Investment and Financing Challenges; Optimization Strategies

1. Introduction

With the development of enterprises, investment and financing decisions have become a core activity in corporate management, directly influencing the long-term health and market competitiveness of businesses. In an increasingly complex and uncertain global economic environment, various risks have become more prominent. As a result, investment and financing operations of small and medium-sized enterprises (SMEs) in China are confronted with a range of intricate challenges. This paper aims to thoroughly analyze the key challenges faced by Chinese enterprises in the process of investment and financing decision-making, and based on this analysis, propose a series of targeted optimization strategies. The findings of this study not only hold value for decision-makers within enterprises but also provide a fresh perspective and theoretical support for government policy-making and academic research.

2. Overview of Corporate Investment and Financing

2.1. Definition of Corporate Investment and Financing

Corporate investment and corporate financing are the two core activities within the realm of enterprise investment and financing operations. Corporate investment refers to the utilization of limited capital resources by enterprises to acquire or create assets, with the expectation of future economic returns or value growth from these assets. These assets can be tangible or intangible in nature. On the other hand, corporate financing refers to the process through which enterprises raise capital to meet their investment or other financial needs. In the context of corporate investment activities, funds flow out from the investing entity and then towards the investment target. Conversely, in the context of corporate financing activities, funds initially flow into the enterprise and are subsequently allocated towards various expenditures. The interplay of factors such as corporate financial management systems, the debt-equity ratio [1], management risk preferences, external market dynamics, and government policy orientation collectively have a significant impact on the outcomes of enterprise investment and financing activities. It is within this nuanced financial management framework that these activities unfold,

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interwoven with complexities [2][3].

2.2. Significance of Corporate Investment and Financing

Corporate investment and financing fundamentally differ in terms of the timing of cash flows and also exhibit significant disparities in the pathways through which funds flow [4]. However, the ultimate objectives of enterprise investment and financing activities remain consistent. These objectives aim to enhance the profitability of the enterprise, expand its production and operational scale, and amplify its market influence, thus positioning the enterprise for an advantageous position in its future development.

Corporate investment holds significant importance for the following four reasons: Firstly, investment is a necessary means for corporate growth and innovation. Secondly, investment forms the fundamental prerequisite for improving capital efficiency. Thirdly, investment serves as an important method for enterprises to mitigate risks. Lastly, investment can compensate for deficiencies in corporate competitiveness.

Corporate financing carries the following four significant implications: Firstly, financing serves as the primary avenue for enterprises to acquire essential capital resources [5]. Secondly, financing allows for the rationalization of capital structure. Thirdly, financing enables risk diversification and hedging. Lastly, financing acts as a lifeline for the brand image of enterprises.

2.3. Main forms of Corporate Investment and Financing

According to the classification based on funding sources, corporate financing can be divided into external financing and internal financing [6]. External financing refers to the process by which an enterprise raises funds from external investors or financial institutions, primarily through bank mortgages and raising capital through securities in the capital market. Internal financing primarily relies on the generated free cash flow from the enterprise's operations, such as extracting a portion of funds from retained earnings or depreciation as financing. Based on the nature of the financing capital, corporate financing can be categorized into equity financing and debt financing. Equity financing is a method of raising funds by issuing or selling shares, which does not require regular repayment of funds by the enterprise. Debt financing is a method of raising funds through borrowing, including bank loans, issuing bonds, or borrowing from non-bank financial institutions. It requires timely repayment of principal and interest according to agreed-upon terms and interest rates.

According to the involvement of the investing enterprise in the operation and management of the target enterprise, corporate investment can be classified into direct investment and indirect investment [7]. Direct investment involves directly injecting capital into production and operations or directly or indirectly controlling the operational and management activities of other enterprises. Its purpose is to achieve long-term and sustainable investment returns. Indirect investment, on the other hand, entails purchasing bonds or stocks and receiving periodic dividends and interest as investment returns without direct participation in the operational management of the enterprise. It offers advantages such as high liquidity, low risk, and low cost. Based on the investment objectives and directions of the enterprise, corporate investment can be primarily divided into internal investment and external investment [8]. Internal investment refers to the allocation of funds within the enterprise, such as expanding the scale of production and engaging in research and development activities. Its aim is to maintain a competitive advantage in a fiercely competitive market [9]. External investment, on the other hand, involves investing capital outside of the enterprise in other enterprises or projects. This can include purchasing securities issued by other enterprises or collaborating on the development of new projects. The goal of external investment is to improve asset utilization efficiency and acquire stable long-term returns.

3. Major Challenges Faced by Enterprises in Investment and Financing Decision-making at Present

3.1. Information Asymmetry in Investment and Financing

In a market economy, enterprises encounter

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complex development environments and diverse funding needs. However, it is difficult for enterprises to rely solely on internal resources for expansion or strategic upgrades. Therefore, external investment and financing become necessary means for enterprise development. However, in reality, there exists evident information asymmetry between the demand and supply sides of funds, which creates implicit barriers and leads to “adverse selection” and “moral hazard”[10] outcomes. The demand side of funds, holding more information about their own operations and financial conditions, may have an advantage during negotiation and contract execution, which undoubtedly increases the risk borne by the supply side of funds. To mitigate the risk resulting from information asymmetry, the supply side of funds strengthens its scrutiny of enterprises. This not only increases the financing costs for enterprises but also prolongs the financing cycle, impacting the ability of enterprises to respond quickly to the market. Information asymmetry can also lead to misjudgments by enterprises themselves in investment decision-making, negatively affecting their long-term development.

3.2. Lack of Risk Prevention Capabilities in Investment and Financing

The types of risks involved in investment and financing are diverse and intertwined, making risk prevention and management a systematic endeavor [11]. However, during the capital operation process, enterprises often overlook or lack the ability to identify potential risks. Enterprises that solely pursue fund acquisition without considering profitability and debt repayment capabilities often lack comprehensive and in-depth understanding of the external market environment and internal operational conditions. When faced with market fluctuations or industry adjustments, they often lack sufficient adaptability, thereby increasing operational risks. Without suitable profit models and financial planning, these enterprises are prone to be passive in market competition, which affects their long-term development [12]. Additionally, the lack of specialized talents further amplifies the risks in investment and financing operations for enterprises [13]. Sound and effective investment and financing strategies require in-depth industry research, financial model construction, and multifaceted risk assessments. Enterprises without specialized talents find it challenging to develop investment and financing plans that align with their own development needs, and they struggle to make timely and accurate strategic adjustments in response to market changes.

3.3. Conservative and Narrow Investment and Financing Channels for SMEs

In recent years, with the encouragement and support of the government, the financial market has provided assistance to SME). Although SMEs in China have been growing steadily, there still exists a certain gap compared to large enterprises. Due to limitations in terms of scale, capital, and talent, SMEs have lower internal risk-bearing capacity. As a result, they tend to adopt conservative and low-risk approaches when it comes to investment and financing channels and models. Under a conservative corporate culture and traditional management mindset, leaders of SMEs in our country may prefer to stick to conventional and familiar investment and financing avenues, rather than exploring new or more diversified methods. This conservatism often restricts their flexibility to utilize various financing tools in different scenarios. Additionally, strict restrictions on foreign and private capital entering the Chinese financial market contribute to the limited investment and financing channels for domestic enterprises [14]. Moreover, due to the immaturity of our capital market and strict regulations on enterprise IPOs, small and medium enterprises in our country generally resort to bank mortgage loans, with limited utilization of financing methods such as issuing stocks and bonds[15][16].

3.4. Inadequate Investment and Financing Management Mechanisms in Enterprises

Presently, numerous enterprises in our country encounter a deficiency in their management mechanisms when it comes to investment and financing activities. This directly impinges upon their competitiveness and sustainable development. Several enterprises heavily rely on the decision-making of senior management or a select few core shareholders in their investment and financing strategies. Unfortunately, these decision-makers are often confined by their limited information and

experiences, making it arduous to comprehensively consider the long-term needs of the enterprise and the multitude of risks it faces. Consequently, such circumstances frequently lead to erroneous decisions, such as excessive expansion or high-risk investments. Insufficient information disclosure exacerbates the asymmetry of internal and external information, thus influencing the decisions of shareholders and potential investors while leaving the enterprise at a disadvantageous position during the financing process. Simultaneously, the lack of clarity in internal capital circulation information may result in inefficient capital utilization. Many enterprises merely conduct rudimentary risk assessments during the investment and financing stages, lacking a consistent and systematic risk management process. Hence, when confronted with diverse risks like credit risk, market risk, and liquidity risk, enterprises often find themselves ill-equipped and incapable of effectively isolating and transferring these risks.

4. Conclusions and Recommendations

In this study, a thorough investigation was undertaken to delve into the current issues faced by enterprises in their investment and financing operations. Four key problems were identified: information asymmetry, lack of risk prevention capabilities, conservative and narrow channels for investment and financing for SMEs, and inadequate management mechanisms. The causes of these problems were meticulously analyzed. These issues severely impact the accuracy and scientific nature of investment and financing decision-making within enterprises, hindering their overall development. Therefore, based on the identified problems and their underlying causes, this paper proposes the following four optimization suggestions:

4.1 Fully Leveraging the Government's Guiding Role

The sustainable and healthy development of investment and financing activities in Chinese enterprises relies heavily on the guidance of the state and government. Firstly, considering that funding shortage often acts as a major bottleneck impeding enterprise development, it is necessary for the government to establish or expand dedicated investment and financing support funds. These funds should possess a high degree of flexibility to cater to the specific needs of different industries and enterprises of varying scales, thus achieving more effective and precise allocation of funds. Secondly, the government should utilize various fiscal measures, including but not limited to tax incentives, research and development subsidies, and low-interest loans, to encourage enterprises to enhance their investment in technology and innovation. Moreover, the government should actively establish digital platforms for investment and financing services, along with improving the evaluation system for investment and financing operations in enterprises. This will facilitate transparency of investment and financing information, thereby helping to reduce costs for both investors and fund seekers while enhancing the flow of idle funds between enterprises and society. Ultimately, these measures will contribute to maximizing capital efficiency.

4.2 Strengthening Internal Management and Improving Enterprise Investment and Financing Mechanisms

Enhancing internal investment and financing management mechanisms serves as the foundation for the long-term development and sound operation of any enterprise. Therefore, during the investment and financing process, it is crucial for enterprises to establish comprehensive risk management mechanisms. Regular audits should be conducted to examine potential loopholes or non-standard operations within the investment and financing procedures, with prompt adjustments made as needed. Additionally, the internal control system should be refined and applied to every aspect of investment and financing. Enterprises should also adjust and optimize their capital structure based on their business models and market conditions, aiming to maximize the efficiency of their capital utilization. In compliance with legal regulations, enterprises should provide accurate, comprehensive, and timely financial reports, as well as maintain active communication with investors, increasing transparency between the enterprise and investment community to enhance its reputation in the capital market. Establishing an internal information-sharing platform

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enables effective communication among departments and hierarchical levels, facilitating the swift identification of issues and facilitating timely adjustments within the enterprise.

4.3 Rise Investment and Financing Channels

Actively introducing private capital and expanding financing channels is not only a necessity for the self-development of enterprises but also a vital means to respond to the market's diversification and efficiency. Enterprises should recognize that private capital represents not only financial resources but also strategic assets. Private investors often possess extensive industry experience and resource networks, offering multifaceted support to enterprises beyond financial backing. Particularly in the current context of digitization and networking, enterprises should attach great importance to online financing platforms, including but not limited to P2P loans and crowdfunding, to meet their funding needs more efficiently and flexibly. In addition to conventional investments such as expanding production scale or purchasing stocks, enterprises can explore collaborations with private capital through industry funds or joint ventures, aiming to share risks and enhance investment efficiency. This mechanism not only brings in funds but also external professional expertise and strategic resources, further enhancing the core competitiveness of enterprises. Simultaneously, enterprises should consider investing in private equity funds, overseas assets, and emerging industries, while also paying attention to emerging investment tools and platforms, such as digital currencies and the blockchain industry.

4.4 Strengthening the Construction of Enterprise Investment and Financing Teams

The field of investment and financing within enterprises is dynamic and complex. To enhance the accuracy of investment and financing decision-making, it is essential to foster the introduction of multidisciplinary talents. The personnel involved in investment and financing should possess not only traditional expertise in finance and law but also skills in emerging fields such as big data, cloud computing, the Internet of Things, and the digital economy. This will help form a comprehensive and efficient investment and financing team. Enterprises need to conduct regular internal training programs to acquire the latest theoretical and applied knowledge in the field. This should encompass not only the latest financial analysis and risk assessment models but also encompass cutting-edge advancements in scientific computing technology. Furthermore, it is important for enterprises to regularly conduct investment and financing case studies, involving successful or failed cases within their respective industries. Through in-depth analysis of these cases, the investment and financing team can gain a holistic understanding of the various variables and risk factors associated with investment and financing decision-making, thereby improving the quality of such decisions within the enterprise.

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