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Assessing the Liquidity and Liquidity of Enterprises - Learn Through Commercial Banks: A Special Type of Enterprise

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Abstract
Financial index analysis is an important part of fundamental analysis. Analyzing ratios involves comparing numbers to each other to create ratios and then using these ratios to assess whether a company's performance is in decline or growth.
Knowing how to calculate and use financial ratios is not only meaningful to financial analysts, but is also very important to investors as well as to businesses themselves and creditors. Financial ratios allow us to compare different aspects of a business's financial statements with other businesses across the industry to consider its ability to pay dividends as well as its ability to repay debt.
Financial statements are a snapshot, a financial "picture" of a business at a specific time and during a specific period. But to understand more deeply the "story" behind the numbers and find important messages about business performance, financial security, and future prospects... of the business; Administrators and investors need to read, understand and analyze financial statements at a deeper level, especially about the solvency and liquidity of the business. By clearly understanding and applying these analytical indicators, managers and investors can not only "read" financial reports accurately and clearly but can also "continue writing" the story. Business success.

Keywords: Solvency, Liquidity, Differentiation

1. Introduction
The solvency of an enterprise is the financial capacity that an enterprise has to meet the needs of paying all short- and long-term debts to individuals and organizations that have a relationship with the enterprise. Enterprises with good solvency indicators demonstrate that they have financial capacity to ensure the ability to pay debts. If the enterprise's index shows poor solvency, it shows that the enterprise has financial problems and has many risks leading to insolvency in the future.
Liquidity (or in English, Liquidity) is a term used in finance to express the degree of flexibility of an asset when being traded, bought and sold on the market with virtually no impact on the asset. Market price of that asset. Here, the degree of flexibility of an asset is understood as the ability to convert into different types of assets with prices or currencies of that asset.
Distinguishing between liquidity and solvency will help businesses boost production and business activities and overcome difficult times.

2. Research methods
The article uses qualitative research methods including two basic methods: data collection, synthesis and analysis and evaluation. Based on the synthesis of data related to solvency and liquidity, the article distinguishes the difference between solvency and liquidity at enterprises.

3. Distinguish between liquidity and solvency of an enterprise
3.1 Liquidity of the enterprise
3.1.1 Overview of corporate liquidity
* Concept:
For businesses, liquidity (also known as liquidity or liquidity) is a business term used to describe the extent to which any asset can be quickly bought or sold in the market. Without affecting the market price of that asset. The time period for buying and selling goods is usually short-term.

Thus, the liquidity of an enterprise is characterized by the ability to convert assets in that enterprise into cash. A business has high liquidity if it is always available and has many people buying and selling at the same time in large volumes.

* Classify the liquidity of assets in the enterprise
For businesses, if they want to conduct production and business, it is necessary to have two items: assets and capital. In particular, assets are the entire potential to serve the business activities of the enterprise or the economic potential of the enterprise, representing the benefits that the enterprise will gain in the future. Assets include mobile assets and fixed assets.
In particular, current assets are short-term assets that are regularly rotated during the business process. Current assets only participate in one production and business cycle, changing physical form and transferring all value into manufactured products. Therefore, current assets are highly liquid assets. For businesses, current assets are divided into five categories and arranged from high to low liquidity as follows: cash, short-term financial investments, receivables, short-term advances, and inventory. Among the types of liquid assets mentioned above, cash has the highest liquidity and can always be used directly for payment, circulation, and storage. Inventories have the lowest liquidity because they have to go through the distribution and consumption stage to convert into receivables, and then from receivables after a period of time, they will be converted into cash.

* Causes of liquidity risk in businesses
Among the five types of current assets, inventory is an important cause of businesses' liquidity difficulties.
Because when inventory increases sharply, it will cause businesses to have an imbalance in revenue and expenditure. Reality also shows that inventory is a big problem for businesses when aggregate demand in the economy declines.
As a result, businesses have an imbalance in revenue and expenditure. The number of businesses with imbalanced revenues and expenditures has been very high in recent years, about 66%, and tends to increase gradually.

3.1.2 Liquidity of commercial banks - a special type of enterprise

* Concept of Bank's liquidity:
The liquidity of a commercial bank is the immediate ability to meet the needs of withdrawing deposits and disbursing committed credits.
- Sources of liquidity for banks include: deposits to be received, income from providing services, credits to be earned, sale of assets being operated and used, loans borrow from the money market.
- Activities that create the need for liquidity include: customer withdrawals of deposits, customer loan requests, payment of other payables, costs for the process of creating products and services banks, pay dividends to shareholders.
- In terms of time, a bank's liquidity needs include both short-term and long-term.
+ Immediate short-term liquidity needs include: transaction deposits or mature term deposits, monetary market mobilization tools... within the scope of short-term liquidity needs term.
To meet liquidity needs of this type, commercial banks are required to maintain a fairly large level of highly liquid assets (cash in funds, deposits at the Central Bank and other securities). Other financial institutions, Government securities...)
+ Long-term liquidity needs are created by seasonal, cyclical and trending factors. For example, individuals' need to withdraw money or borrow money often increases especially on days close to festivals of the year to cover spending and shopping.
To meet this type of liquidity need, commercial banks need to reserve the ability to provide capital from many different sources and at a higher level than short-term liquidity needs. Specifically: it is necessary to set a plan to attract new deposits, long-term loan agreements from the public or from the reserve funds of other banks...

* What happens when the Bank's liquidity is limited?
When commercial banks are unable to provide adequate cash for immediate liquidity needs; or supply enough but at high cost, then the bank will face liquidity risk. In other words, this is the type of risk that appears in cases where the bank lacks solvency due to not being able to promptly convert assets into cash or not being able to borrow to meet the requirements of payment contracts.

* Causes of liquidity risks at commercial banks:

- Banks borrow too much deposits and reserve funds from individuals and other financial institutions, then convert them into term investment assets.
  Therefore, an imbalance in term between capital source and capital use occurs for banks. It is a rare case that the cash flow recovered from investments is exactly balanced with the cash flow being spent to cover previously mobilized capital.
- Due to sensitivity to changes in investment interest rates, especially deposits. When investment interest rates increase, some depositors withdraw their capital from banks to invest in places with higher rates of return, and borrowers may delay loan requests and be more aggressive. Access credit with lower interest rates. Thus, interest rate changes affect both depositors and borrowers and both impact the bank's liquidity status. Furthermore, trends in interest rate changes also affect the market value of assets that banks can sell to increase their liquidity supply and directly affect the cost of borrowing in the market. Currency market.

* What obstacles will commercial banks encounter when facing liquidity risks?
For Banks - considering the credit intermediary function, when facing liquidity risks, banks will suffer losses:
Forced to race to mobilize capital leading to high deposit interest rates.

- High deposit interest rates force high credit interest rates and make it difficult to lend.
- When forced to pay deposit interest but cannot lend clearly, the Bank will suffer a loss.
- Failure to meet withdrawal needs leads to loss of depositors' confidence (including interbank transactions).
- Does not meet disbursement needs for credit grants.

In short, liquidity and liquidity management require administrators and analysts to be really careful between supply and demand. If they do not clearly understand the nature of the problem, loss of liquidity will cause serious consequences.

3.2 The enterprise's ability to pay

* Concept:
A business's solvency represents its ability to meet debts that come due at any time.

* Mobilized resources to meet the enterprise's solvency
To pay the above debts, mobilized sources include:
- For total short-term debt:
Enterprises can use the following amounts to make payments including: cash and cash equivalents, short-term financial investments, receivables, part of inventory (including: finished products, goods, goods, etc.) Goods for sale and other short-term assets).
Thus, the elements: purchased goods in transit, tools in warehouse, raw materials in inventory, and unfinished production and business costs belong to inventory. Although they can be converted into money, in the process of production and business, businesses cannot convert it into money to repay debts and they can only be converted into money to pay debts when the business goes bankrupt, is sold or has its ownership changed.

- For short-term debt that is due or overdue:
Because the debt is due and overdue, the business must pay immediately, so the amount of cash and cash equivalents used for quick payment only includes two elements: cash and short-term financial investments.
In reality, there are creditors who instead of asking for money, but the business does not have the ability to use the money to repay the debt, the creditor can accept to take the goods and finished products of the business to deduct from the amount of debt to be paid. Then the value of goods and finished products will be determined to calculate the solvency of the business.

* How is a business with high solvency demonstrated?
An enterprise has high solvency when it always has enough financial capacity (cash, cash equivalents, various types of assets...) to ensure payment of debts to individuals and organizations with relationships. With businesses during business operations.

* Conversely, what happens when a business becomes insolvent?
A business becomes insolvent when its financial capacity is not enough to cover its debts, and the business will soon fall into bankruptcy.

* Method for assessing the solvency of an enterprise:
From the above analysis, we see: to analyze and evaluate the solvency of an enterprise, the following 6 indicators can be used:
- Overall debt payment ratio:
+ Formula:
Overall debt coverage ratio
(H)= (Total assets)/ (Liabilities)
+ Meaning: The overall debt payment ratio reflects how many assets a dollar of debt is secured by. If $H < 1$, the business is unable to pay. If $H \geq 1$, the enterprise has sufficient and excess payment capacity. The higher the ratio, the safer it is for creditors. But if it is too high, financial leverage will be low, and businesses may not be able to grasp business investment opportunities that bring high profits.
- Short-term debt payment ability ratio:
+ Formula:
Short-term debt solvency ratio= (Short-term assets)/ (Short-term debt)
+ Meaning: This indicator shows that with the total value of current short-term assets, does the enterprise ensure the ability to pay short-term debts? If this indicator approaches 1, the enterprise has enough short-term assets to pay short-term debt. The higher this indicator is, the better the ability of the business to pay short-term debt and vice versa because a part of short-term assets is invested from a stable capital source, increasing autonomy in financial activities. If this low target persists for a long time, the business may be financially dependent, negatively affecting business operations.
- Quick ratio:
+ Formula:

Quick ratio = (Current assets - Inventories)/ (Short-term debt)

+ Meaning: quick ratio indicates the ability to quickly pay assets that are easily converted into cash for short-term debt. If this indicator is < 0.75, the company's payment situation is in difficulty. If $0.75 \leq$ this indicator ≤ 2, the company's payment situation is at an average level. If this indicator is > 2, the company's payment situation is good and there are many advantages in payment. If this indicator is too high, it is not good, indicating slow capital turnover and low capital use efficiency.
- Instant solvency ratio (Conversion ratio into cash from short-term assets)

+ Formula:
Current ratio= (Cash and cash equivalents)/ (Short-term debt)

+ Meaning: The instant solvency ratio indicates the ability of money to pay immediately for overdue and due debts at any time. If this indicator is higher, the immediate payment ability of the business is good. However, this target is too high, if prolonged, the cash capital of the enterprise will be idle, stagnant, and the efficiency of capital use will be low. If this indicator is too low and persists for too long, the business may be dissolved or go bankrupt.
- Loan interest payment ratio

+ Formula:
Interest coverage ratio = (Earnings before interest and taxes (EBIT))/ (Interest payable)

+ Meaning: this indicator shows how many times the total interest payable during the period from capital mobilization activities can be paid by the company.
- Short-term debt repayment ability ratio (in cash).

+ Formula:
Short-term debt service ratio (in cash)=(Net cash flow from

business activities)/(Average short-term debt)
+ Meaning: indicates how many times the average short-term debt can be repaid by the net cash flow generated from business activities.

3.3 Distinguish between liquidity and solvency of an enterprise

Lack of liquidity is easily confused with solvency. A company is insolvent when its total assets (short-term + long-term) are less than its total liabilities (short-term + long-term).

In other words, when that company sells all its assets, it cannot pay off all its debt. On the other hand, liquidity only refers to short-term assets versus short-term liabilities. If current assets are less than short-term liabilities while total assets are more than total liabilities, the company lacks liquidity but is still solvent. In this case, the company is having problems with payment deadlines, but in terms of time, if the company has enough time to sell all its fixed assets, the company will pay off all its debts. It is necessary to clearly distinguish between solvency which is a concept based on total assets and total liabilities, while liquidity is a concept based on short-term assets and short-term liabilities.

4. Conclusion

Businesses should regularly evaluate financial indicators & analyze financial reports to grasp the business status, thereby making the right decisions to optimize operational efficiency and performance. Depending on the characteristics, characteristics, scale... of each enterprise, through calculating and evaluating financial indicators of liquidity and solvency, comparing indicators according to reporting periods, comparing indexes with businesses in the same industry, with industry average indexes, administrators, investors, creditors... can have a comprehensive view of the business situation, potential and risks of the company.

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