

Evaluation of Milkground's Sustainable Growth Ability Based on Higgins Model

Yong Shen *, Wenyang Xu

School of Economics and Management, Southwest Petroleum University, Chengdu, CO 610500, China

* Corresponding author: Yong Shen (Email: Braveshen9700@gmail.com)

Abstract: This paper selects MilkGround, a leading enterprise in the cheese industry, as the research object, and selects the micro-financial indicators of MilkGround from 2016 to 2022 to explore the sustainable growth ability of MilkGround. The article is divided into four parts: the theory of sustainable growth ability and Higgins model; introduce the operation process of MilkGround and analyze its financial status; compare the actual growth rate of MilkGround with the sustainable growth rate, and then analyze the reasons for the deviation between the two; in view of the possible obstacles to the sustainable development of enterprises, some suggestions are put forward to prevent enterprises from detours. Through research, it is found that the sustainable growth ability of MilkGround Company is affected by many factors such as operating efficiency and financial policy. The company should purchase in advance to lock in the price range and purchase quantity, enrich the cheese product structure, consolidate the cheese category leader position, in order to achieve sustainable growth. Based on the case of MilkGround Company, this paper not only studies the sustainable growth ability of MilkGround, but also provides some references for the problems existing in China's cheese industry.

Keywords: Sustainable Growth Capacity; Higgins Model; Operating Efficiency; Financial Policy.

1. Introduction

In recent years, global economic recovery has faced unprecedented challenges due to the COVID-19 pandemic, intensifying market competition and operational risks for enterprises. Against this backdrop, sustainable growth has emerged as a critical issue for corporate survival and value creation, particularly in emerging industries such as China's dairy sector. The cheese market, as a high-potential segment within the dairy industry, has witnessed rapid expansion in China, yet academic research on its development remains scarce, especially from a micro-financial perspective. Existing studies on sustainable growth predominantly focus on macroeconomic or industry-wide analyses (Bongers & Diaz-Roldan, 2019; Bellandi, 2023), while firm-level investigations, particularly in niche sectors like cheese production, are underdeveloped.

Prior research highlights the multifaceted determinants of sustainable growth, including financial policies (Ahsan & Al-Gamrh, 2022), operational efficiency (Vukovic et al., 2022), and the interplay between environmental, social, and governance (ESG) goals (Belliandi, 2023). For instance, Steblyanskaya et al. (2021) identified distinct financial and non-financial drivers of sustainable growth in Chinese and Russian firms, emphasizing the role of cost management and return on investment. Domestically, scholars like Li (2019) and Huang et al. (2019) have explored internal control quality and trade credit financing, respectively, but their findings largely address generalized manufacturing contexts rather than specialized industries. Notably, China's cheese sector—characterized by low per capita consumption yet significant growth potential—remains underexamined, with few studies analyzing firm-specific financial strategies or growth trajectories.

This study aims to bridge this gap by evaluating the sustainable growth capability of Milkground, a leading Chinese cheese producer, through the lens of Higgins'

Sustainable Growth Rate (SGR) model. By integrating micro-financial indicators (e.g., profitability, asset turnover) and operational data from 2016 to 2022, the research seeks to: (1) identify deviations between Milkground's actual and sustainable growth rates, (2) uncover underlying factors affecting its growth equilibrium, and (3) propose actionable strategies to enhance resilience in a volatile market. The findings are expected to enrich academic discourse on sustainable growth theory while offering practical insights for dairy enterprises navigating competitive and resource-constrained environments.

2. Financial status of Milkground

2.1. Company Profile

First, the company's financial policies are formulated and implemented based on its actual circumstances to ensure alignment with its operational needs and characteristics, prioritizing stability. Milkground maintains a stable overall capital structure and adheres to a consistent dividend policy without changes. Second, the company retains its current number of shares and refrains from issuing new equity, complying with the second assumption of the Higgins Model. Its equity structure remains unchanged, with no activities related to stock issuance or capital adjustments. Third, Milkground strives to stabilize operational efficiency without significant fluctuations. Through effective sales strategies and asset management measures, the company ensures that fluctuations in net sales profit margin and total asset turnover rate remain within a reasonable range. Such stability in operational efficiency fulfills the third assumption of the Higgins Model.

In summary, Milkground satisfies all three assumptions of the Higgins Model. By developing and executing contextually tailored financial policies, maintaining a stable equity structure, and sustaining consistent operational efficiency, the company ensures financial robustness and

long-term profitability.

2.2. Four Major Capabilities Analysis

2.2.1. Debt Solvency

Table 1. Milkground's debt-paying capacity indicators

Year	Short-term solvency		Long-term solvency	
	Current Ratio	Quick Ratio	Ownership ratio	Debt-to-asset ratio (%)
2016	1.23	1.15	0.87	46.57
2017	1.92	1.7	1.25	55.64
2018	1.04	0.9	1.21	54.71
2019	1.13	0.95	0.93	48.19
2020	1.29	1	0.85	40.73
2021	2.71	2.34	0.4	26.74
2022	1.99	1.67	0.45	34.43

From the table above, it can be seen that Milkground's current ratio and quick ratio remained around 1 from 2016 to 2020, reaching above 2 in 2021, indicating that the company's short-term solvency was relatively stable in previous years and showed significant improvement in 2021. However, according to foreign studies, the ideal current ratio is generally considered to be 2, while the ideal quick ratio is 1. It is evident that Milkground's current ratio before 2021 was below the standard level, while the quick ratio remained relatively normal, suggesting that the company's current assets were relatively small compared to its current liabilities, with a high proportion of cash in its current assets. However, another important factor to consider is that Milkground operates in the dairy industry, where excessive inventory is undesirable. Therefore, the industry standard for the current ratio should be lower than 2. Thus, Milkground's short-term solvency is still very strong.

In addition, the sudden increase in short-term solvency indicators in 2021, which differs significantly from previous years, suggests that the company's high proportion of cash might impact its sustainable growth ability. Milkground should address this issue promptly to maximize its potential. However, data from the 2022 interim report shows that both indicators have declined, indicating that the company has recognized this issue and is making adjustments.

2.2.2. Operational Capacity

Operational capability generally refers to a company's fundamental ability in production, procurement, and sales. Strong operational capability can enhance production efficiency, increase cash flow, and improve profitability.

Table 2. Milkground's Operational Efficiency Indicators

Year	Total Asset Turnover	Inventory Turnover	Current Asset Turnover
2016	0.27	6.19	0.62
2017	0.41	7.81	0.93
2018	0.46	6.19	1.07
2019	0.68	7.83	1.69
2020	1.03	8.86	2.77
2021	0.91	6.97	1.77
2022	0.68	5.19	1.17

As shown in the table, Milkground's total asset turnover experienced a rise followed by a decline, with the decline occurring in 2021. Additionally, except for 2020,

Milkground's current asset turnover remained relatively low in other years. According to the company's profile, Milkground raised funds in 2021, significantly increasing its assets. Combined with the previously mentioned increase in the asset-liability ratio after the fundraising, it is evident that the company also increased its liabilities. A decline in total asset turnover is generally attributed to factors such as decreased sales revenue, inventory buildup, non-performing assets, excessive idle funds, or increased liabilities. Given the low current asset turnover, it can be inferred that Milkground currently faces an issue of underutilized idle current funds.

The inventory turnover ratio is used here to further explain the total asset turnover. Milkground's inventory turnover ratio has shown volatility, peaking at 8.86 in 2020 before declining, reaching its lowest point of 5.19 in 2022, indicating a risk of inventory buildup and a downward trend in operational capability. In the cheese industry, inventory buildup can significantly impact business operations and is particularly detrimental to performance. The decline in Milkground's inventory turnover ratio over the past two years is mainly due to issues across the entire supply chain, including production input, inventory management, and sales fund recovery. This situation is clearly unfavorable for Milkground's sustainable growth capability.

2.2.3. Profitability

Profitability refers to a company's ability to generate profits over a specific period and serves as the most direct objective for any enterprise. This capability is typically evaluated using financial metrics such as the net profit margin, return on assets (ROA), and return on equity (ROE). Strong profitability indicates that a company can deliver sufficient returns to shareholders and investors while enhancing its market competitiveness.

Table 3. Milkground's Profitability Indicators

Year	Net Profit Margin (%)	ROA (%)	ROE (%)
2016	6.17	1.66	1.68
2017	0.44	0.18	0.37
2018	0.87	0.40	0.89
2019	1.10	0.75	1.54
2020	2.60	2.67	4.55
2021	4.33	3.96	4.97
2022	3.54	2.42	3.05

As shown in the table, the three metrics experienced a sharp decline in 2017, followed by gradual recovery in subsequent years. However, another downturn occurred in 2022. Analysis reveals that since 2017, Milkground shifted its strategic focus to its core cheese business to secure market dominance, rapidly expanding its marketing network and workforce, particularly in retail channels. Consequently, the company achieved significant revenue growth. However, substantial upfront investments—including slotting fees, barcode licensing fees, and other one-time retail channel costs—led to a surge in overall sales expenses, resulting in the sharp decline of these metrics in 2017. As marketing campaigns gained traction, revenues surged notably from 2020 onward, driving improvements in profitability indicators. However, by 2022, rising raw material costs eroded profit margins, leading to another decline in these metrics. Overall, Milkground's profitability remains precarious, characterized by heavy reliance on competitive marketing expenditures and unstable

earnings. Over the long term, its weak profitability poses challenges to sustainable growth.

2.2.4. Growth Capacity

Development capability refers to a company's ability to innovate and grow over the long term, achieved through product innovation, technological research and development, and market expansion. The most direct indicator of development capability is the net profit growth rate. Strong development capability enables a company to continuously update its products and services, enhance its core competitiveness, and achieve sustainable growth.

Table 4. Milkground's Net Profit Growth Rate

Year	Net Profit Growth Rate (%)
2016	111.72
2017	-86.72
2018	148.66
2019	80.73
2020	208.16
2021	160.55
2022	-11.74

As shown in the table, Milkground's net profit growth rate has exhibited significant fluctuations, with negative growth observed only in 2017 and 2022, while the remaining years demonstrated exceptional performance. In 2016, Milkground officially went public and initiated a major asset restructuring, transitioning from its previous mining operations to a distinctive dairy and cheese manufacturing business. The integration of new assets during this restructuring process yielded superior profitability compared to the original assets. Additionally, the company generated investment income from internal asset restructuring, resulting in a turnaround from losses to profits during the study period. Consequently, key metrics such as earnings per share (EPS) and net profit growth rate showed substantial improvement. However, the 2017 data revealed a decline, primarily due to two factors: (1) the absence of investment income generated from the previous year's asset restructuring, which amounted to RMB 52.233 million, and (2) the company's aggressive focus on expanding its cheese business to gain market dominance. During this period, Milkground rapidly expanded its marketing network and workforce, particularly in retail channels. While sales revenue increased significantly, the company incurred substantial upfront costs, including slotting fees, barcode licensing fees, and other one-time expenses, leading to a sharp rise in overall sales costs. Furthermore, the company recognized significant costs related to its restricted stock incentive plan.

In the following years, Milkground actively developed new products tailored to market demands, with its cheese sticks becoming a successful product targeting children. Simultaneously, the company expanded its distribution channels and marketing reach, attracting new customers and collaborating with high-profile celebrities for endorsements. These efforts contributed to remarkable growth in cheese and dairy product sales. However, in 2022, external environmental changes led to a decline in revenue and increased raw material costs, resulting in a negative net profit growth rate.

3. Growth Capability Analysis Using the Higgins Model

3.1. Actual Growth Rate

The actual growth rate of an enterprise refers to the realized growth level within a specific period, typically expressed as a percentage, and serves as a critical indicator for evaluating sustainable growth capability.

Table 5. Milkground's Actual Growth Rate

Year	Revenue (RMB)	Actual Growth Rate (%)
2016	511,569,156.44	41.76
2017	981,998,082.71	91.96
2018	1,225,689,926.53	24.82
2019	1,744,349,052.12	42.32
2020	2,846,807,171.16	63.20
2021	4,478,305,561.69	57.31
2022	4,829,537,951.87	7.84

As clearly illustrated in the table, Milkground's actual growth rate exhibited significant volatility during the study period. In 2017, it peaked at 91.96%, only to plummet to 24.84% the following year. This drastic fluctuation can be attributed to substantial improvements in the company's revenue structure and product portfolio, which were offset by a decline in trade performance compared to the previous year, thereby dampening the actual growth rate. Subsequently, sales stabilized gradually. However, in 2022, like earlier trends, external environmental disruptions led to a contraction in operating revenue.

3.2. Sustainable Growth Rate

The Higgins Model defines sustainable growth rate (SGR) as:

$$\text{SGR} = \text{Net Profit Margin} \times \text{Total Asset Turnover} \times \text{Equity Multiplier} \times \text{Retention Ratio}$$

Using this formula, the annual reports of Milkground from 2016 to 2022 were organized:

Table 6. Milkground's Sustainable Growth Rate (SGR)

Year	Net Profit Margin	Total Asset Turnover	Equity Multiplier	Retention Ratio	SGR (%)
2016	6.17%	0.27	1.87	1.00	3.12
2017	0.44%	0.41	2.25	1.00	0.41
2018	0.87%	0.46	2.21	1.00	0.88
2019	1.10%	0.68	1.93	1.00	1.44
2020	2.60%	1.03	1.69	1.00	4.53
2021	4.33%	0.91	1.36	1.00	5.36
2022	3.54%	0.68	1.53	1.00	3.68

The sustainable growth rate of Milkground, consistent with previous data, shows a sharp decline from 2016 to 2017, followed by a hopeful upward trend from 2017 to 2021, reaching its peak in 2021, and then declining in 2022. The reasons for this trend are the same as mentioned earlier: excessive investment in marketing to capture market share led to a decline in the growth rate in 2017.

3.3. Deviation in Enterprise Growth Capability

Both a company's actual growth rate and the sustainable

growth rate based on the Higgins model are indicators used to measure corporate growth, but they reflect different aspects of this growth. The key difference between the two is that the actual growth rate is calculated based on the company's short-term operational performance, reflecting external factors such as market environment and competitive conditions. In contrast, the sustainable growth rate (SGR) derived from the Higgins model is based on the internal conditions necessary for sustainable growth, reflecting the company's internal ability and potential for sustainable development.

Table 7. Growth Deviation Calculation

Year	Sustainable Growth Rate (SGR)	Actual Growth Rate (g)	Deviation ($\Delta = g - \text{SGR}$)
2016	3.12%	41.76%	38.64%
2017	0.41%	91.96%	91.55%
2018	0.88%	24.82%	23.94%
2019	1.44%	42.32%	40.88%
2020	4.53%	63.20%	58.67%
2021	5.36%	57.31%	51.95%
2022	3.68%	7.84%	4.16%

Table 8. Operating Efficiency

Year	Net Profit Margin	Total Asset Turnover
2016	6.17%	0.27
2017	0.44%	0.41
2018	0.87%	0.46
2019	1.10%	0.68
2020	2.60%	1.03
2021	4.33%	0.91
2022	3.54%	0.68

Table 8. Financial Policy

Year	Retention Ratio	Equity Ratio	Asset-Liability Ratio
2016	1	87.15%	46.57%
2017	1	125%	55.64%
2018	1	121%	54.71%
2019	1	93.03%	48.19%
2020	1	84.79%	40.73%
2021	1	39.69%	26.74%
2022	1	57.58%	34.43%

Calculating the deviation between a company's actual growth rate and its Higgins model sustainable growth rate helps provide a better understanding of the company's growth status and development potential, offering critical decision-making support for managers. First, the deviation can reveal the company's growth potential. Second, it can guide corporate decision-making. Finally, it can be used to assess the company's value.

Milkground's actual growth rate (g) is significantly higher than its sustainable growth rate (SGR), indicating that the company's current growth model is unsustainable. This may be due to over-reliance on certain products or markets. The company should adjust its strategy to achieve more stable and sustainable growth.

From two operational efficiency indicators—net profit margin and total asset turnover—it is evident that Milkground's operational efficiency remains low. A low net

profit margin indicates poor cost control, while a low total asset turnover ratio suggests that the company's asset utilization efficiency needs improvement. Therefore, the company must strengthen cost management, optimize asset structure, and enhance operational efficiency.

Milkground's retention ratio remains at 1, indicating that the company is not distributing all its profits as dividends or reinvesting them entirely but is maintaining a certain level of retained earnings for future expansion and investment. This prudent financial policy supports the company's long-term sustainable development.

From the perspectives of equity ratio and asset-liability ratio, Milkground's financial risk is relatively low. A high equity ratio indicates that the company's assets are primarily financed by its own funds, while a low asset-liability ratio suggests a low level of debt. This is favorable for the company's financial stability and sustainability.

3.4. Analysis of Deviation Causes

3.4.1. Analysis of Enterprise Operational Efficiency

The analysis of enterprise operational efficiency is of great significance for investors in evaluating a company's financial performance and business strategies. It helps investors gain a better understanding of the company's operations, management, and strategic direction, enabling them to make more accurate assessments of the company's investment value.

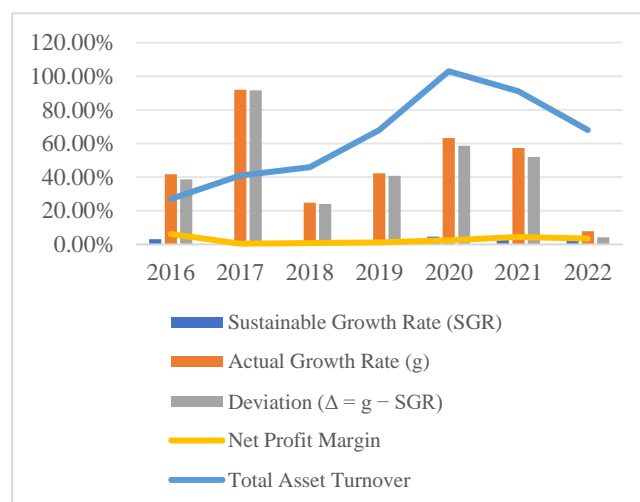


Figure 1. Trend Chart of Operational Efficiency Indicators

Milkground's growth rate deviation has been significantly high, improving only in 2022. The actual growth rate consistently exceeded the sustainable growth rate, indicating reliance on external factors rather than intrinsic sustainable growth. Declines in 2018, 2021, and 2022 suggest fluctuations in operational stability. While net profit margin had little impact on deviation, total asset turnover showed a strong correlation with it, except in 2017.

Total asset turnover, a key financial indicator, reflects a company's efficiency in utilizing assets. Declines in 2021 and 2022 were due to lower current asset turnover and external market changes. The unique 2017–2018 trend resulted from asset restructuring and the shift away from trade business post-listing.

Despite a low net profit margin, Milkground's sustainable growth rate followed a similar trend, indicating that managerial efforts and investment influence both growth and efficiency. However, actual growth rate variations suggest external factors like market demand, competition, and economic shifts play a significant role. Companies may boost

revenue through short-term strategies, such as price reductions or aggressive marketing, which can temporarily increase growth at the expense of operational efficiency.

Milkground's high marketing expenditures to enhance brand recognition explain why its actual growth rate surpassed operational efficiency, highlighting the impact of strategic investments on business performance.

3.4.2. Analysis of Enterprise Operational Efficiency

Analyzing a company's financial policies helps investors, creditors, analysts, and managers understand financial decision-making, risk management, and financial health, enabling them to assess and predict the company's financial performance and outlook.

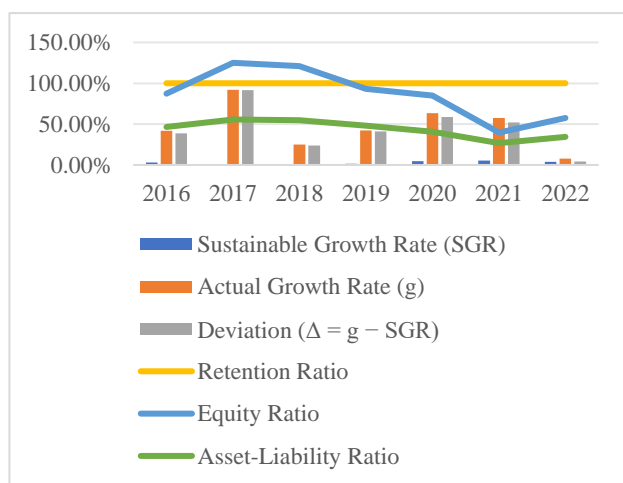


Figure 2. Financial Policy Indicator Trend Chart

As a company grows, its primary means of expanding total assets is by increasing shareholder equity. As shown in the figure, the retention ratio remains constant at 1. Since Milkground was listed only in 2016 and has had a continuously increasing need for capital, it did not distribute dividends during the study period and reinvested all its profits into development. Consequently, it is difficult to determine any correlation between the retention ratio and growth deviation. In contrast, the equity ratio and asset-liability ratio, except for the anomalous year of 2017 (caused by asset restructuring and changes in trade business), appear to exhibit trends that are exactly opposite to those of the three growth rate indicators. The results indicate that as the equity ratio and asset-liability ratio increase, the deviation between the sustainable growth rate, actual growth rate, and overall growth rate gradually decreases—and vice versa. This suggests that when a company relies more on debt financing (i.e., an increased asset-liability ratio), its financial risk rises, leading to lower sustainable and actual growth rates. Conversely, when a company uses more equity financing (i.e., an increased equity ratio), its financial risk diminishes, thereby facilitating higher sustainable and actual growth rates. Therefore, when deciding on financing methods, the company's financial health and future needs must be carefully considered to ensure sustainable growth.

From 2017 to 2021, both the equity ratio and asset-liability ratio showed a declining trend. Although this shift increased the proportion of company-owned assets—resulting in greater free cash flow and improved debt repayment capacity, which enhanced stability and flexibility—it also led to underutilized funds. Consequently, the company missed many opportunity costs, such as the chance to expand operations through borrowing, which could adversely affect its

sustainable growth potential. In 2021, to accelerate expansion and development, Milkground conducted targeted fundraising from Mengniu Dairy. Following this, the company gradually increased its financial leverage, leading to an upward trend in these two indicators in 2022. This adjustment played a significant role in balancing the two growth rates and enhancing the company's sustainable growth capacity.

4. Challenges and Causes

4.1. Problems in the Process of Achieving Sustainable Growth

4.1.1. Profitability and Capital Utilization Issues

Table 9. Milkground's Profit Quality

Year	ROE (%)	ROIC (%)	Net Profit Margin (%)
2016	1.68	1.95	6.17
2017	0.37	0.20	0.44
2018	0.89	0.46	0.87
2019	1.54	0.88	1.10
2020	4.55	2.80	2.60
2021	4.97	4.31	4.33
2022	3.05	2.49	3.54

According to the table data, Milkground's return on net assets (ROE), return on invested capital (ROIC), and net profit margin are all relatively low, indicating weak profitability.

Firstly, ROE measures the company's profitability in utilizing its assets. From 2016 to 2022, Milkground's ROE fluctuated significantly, with a maximum of 4.97% and a minimum of 0.37%, averaging around 2.58%. This suggests that the company has not generated sufficient returns on its assets.

Secondly, ROIC assesses the return a company earns on its invested capital. Between 2016 and 2022, Milkground's ROIC ranged from 0.20% to 4.31%, with an average of approximately 2.21%. While slightly higher than ROE, it remains below expectations.

Lastly, the net profit margin measures the proportion of profit in total revenue. From 2016 to 2022, Milkground's net profit margin fluctuated between 0.44% and 4.33%, with an average of about 2.08%. This is significantly lower than the industry average, indicating the need for measures to enhance profitability, such as improving marketing strategies to boost sales volume or reducing costs to increase profit margins.

Table 10. Revenue and Profit Indicators

Year	Sales Revenue (Billion CNY)	Net Profit (Billion CNY)	Net Profit Excluding Non-Recurring Gains and Losses (Billion CNY)
2016	5.12	0.32	-0.15
2017	9.82	0.04	0.01
2018	12.26	0.11	-0.14
2019	17.44	0.19	-0.12
2020	28.47	0.59	0.45
2021	44.78	1.54	1.22
2022	48.3	1.71	0.67

The data suggests a preliminary conclusion: the company experiences revenue growth without a corresponding increase

in profitability. Specifically, while its revenue has shown a stable upward trend in recent years, net profit and non-recurring profit have exhibited fluctuations and reversals. This indicates a decline in operational efficiency, which has not translated into improved profitability. Since non-recurring profit excludes one-time gains or losses, it provides a more accurate reflection of the company's true earning capacity.

For Milkground, the issues of weak profitability and revenue growth without profit increase require serious attention. On one hand, the company must further optimize operations, enhance efficiency, and minimize waste and losses to improve profitability. On the other hand, it should explore new profit growth avenues by leveraging innovation and differentiation strategies to increase product value, strengthen market expansion, and develop new revenue streams. Addressing these issues with targeted and effective operational strategies is crucial for enhancing profitability, improving operational efficiency, and achieving sustainable development.

4.1.2. Low Capital Utilization Efficiency

Milkground's total asset turnover ratio and current asset turnover ratio gradually increased from 2016 to 2019, saw a sharp rise in 2020, and then experienced a significant decline in 2021. Regarding the asset-liability ratio, it decreased each year from 2016 to 2021, indicating an improving financial position. However, it slightly increased again in 2022. Additionally, the equity multiplier showed a downward trend

over the past few years, dropping from 1.87 to 1.36, suggesting that Milkground faced increased risks when using debt financing for investments. Meanwhile, both the current ratio and quick ratio surged sharply after 2021, indicating an improvement in Milkground's liquidity.

Overall, these data suggest that Milkground's capital utilization efficiency remains at a relatively low level. The low capital utilization rate may be attributed to the company's financial policy decisions, which have led to capital being tied up rather than fully utilized to generate value.

Table 11. Capital Utilization Quality Indicators

Year	Total Asset Turnover	Current Asset Turnover	Debt-to-Asset Ratio	Equity Multiplier
2016	0.27	0.62	46.57%	1.87
2017	0.41	0.93	55.64%	2.25
2018	0.46	1.07	54.71%	2.21
2019	0.68	1.69	48.19%	1.93
2020	1.03	2.77	40.73%	1.69
2021	0.91	1.77	26.74%	1.36
2022	0.68	1.17	34.43%	1.53

4.2. Problems in the Process of Achieving Sustainable Growth

4.2.1. Decline in Profit Margin

Table 12. Main Business Overview (thousand yuan)

Year	Category	Cheese	Trade Product	Liquid Milk	Total
2022	Revenue	386,872	59,997	34,889	481,759
	Proportion	80.30%	12.45%	7.24%	100.00%
	Gross Profit	157,579	3,661	3,003	164,244
	Proportion	95.94%	2.23%	1.83%	100.00%
	Gross Profit Margin	40.73%	6.10%	8.61%	34.09%
2021	Revenue	333,487	70,399	43,000	446,887
	Proportion	74.62%	15.75%	9.62%	100.00%
	Gross Profit	161,780	2,744	5,903	170,427
	Proportion	94.93%	1.61%	3.46%	100.00%
	Gross Profit Margin	48.51%	3.90%	13.73%	38.14%

Table 13. Main Business Changes

Category	Cheese	Trade Products	Liquid Milk	Total
Revenue Change	16.01%	-14.78%	-18.86%	7.80%
Gross Profit Margin Change	Decreased by 7.78%	Increased by 2.20%	Decreased by 5.12%	Decreased by 4.04%

Cheese products are the primary source of revenue for Milkground. However, in 2022, the gross profit margin of cheese products decreased by 7.78 percentage points year-on-year to 40.73%, significantly impacting Milkground's overall performance, particularly its net profit. Additionally, the gross profit margin of liquid milk also declined by 5.12 percentage points year-on-year to 8.61% in 2022. Although the gross profit margin of trade products increased by 2.2 percentage points year-on-year to 6.1%, its relatively small revenue scale was insufficient to offset the decline in the gross profit margins of cheese products and liquid milk. As a result, Milkground's overall gross profit margin decreased by 4.04 percentage points year-on-year to 34.09% in 2022.

As an emerging category in the dairy industry, the market demand for cheese is still in the growth and cultivation stage. Although Milkground has expanded its market through

marketing strategies, a stable consumption demand has yet to be established. Additionally, the negative impact of the pandemic on consumption further affected its profitability. However, the decline in profits is not yet a major concern. Nonetheless, the decrease in gross profit margin indicates a shrinking profit margin for products, which could negatively affect the company's long-term profitability.

4.2.2. High marketing expenses

Before 2018, China's cheese market was dominated by foreign brands, and Milkground posed little competition. However, through aggressive marketing, the company quickly expanded its presence. By 2021, it held a 27.7% market share, ranking first among domestic cheese brands.

This growth was driven by soaring sales expenses, which rose from 1.255 billion yuan in 2017 (12.78% of revenue) to 11.59 billion yuan in 2021 (25.88%). Over five years, sales

expenses increased more than ninefold, totaling 24.34 billion yuan from 2018 to 2021, with annual growth exceeding 30% except in 2019.

From 2018 to 2021, Milkground’s revenue grew at a high rate, while net profit surged significantly. However, in 2022, sales expenses increased only 5.21% to 12.19 billion yuan, while revenue and net profit growth slowed to 7.84% and -12.32%, respectively.

The decline in sales investment directly impacted Milkground’s performance. High sales and operational costs have squeezed profit margins, reduced available funds, and lowered capital efficiency.

Table 14. Sales Expense Table

Year	Sales Expenses (Billion Yuan)	Sales Expense Ratio
2016	0.37	7.23%
2017	1.225	12.78%
2018	2.052	16.74%
2019	3.593	20.60%
2020	7.105	24.96%
2021	11.586	25.88%
2022	12.19	25.24%

5. Policy Recommendations

5.1. Secure Pricing and Procurement Volumes Through Advance Purchasing

As Milkground relies heavily on imported cheese raw materials, fluctuations in global commodity prices directly impact its profitability and cash flow. Geopolitical tensions, trade disputes, or supply chain disruptions could further exacerbate price volatility or shortages. To mitigate these risks, Milkground should:

(1) Establish long-term partnerships with key suppliers to lock in price ceilings and procurement volumes, ensuring stable costs and supply chain resilience.

(2) Diversify its supply chain by sourcing from multiple regions and investing in sustainable domestic dairy farms to enhance raw material security.

(3) Hedge against price volatility by aligning procurement cycles with sales contracts to reduce operational risks during production lead times.

5.2. Diversify Product Portfolio and Strengthen Market Leadership

While Milkground has built brand recognition as a leader in processed cheese (e.g., cheese sticks targeting children), excessive marketing expenses have strained capital efficiency. To consolidate its competitive edge:

(1) Expand Product Lines: Develop new categories such as natural cheeses (e.g., cheddar, parmesan), cheese slices, and cheese-based snacks (e.g., cheese crackers, cakes) to cater to broader demographics and consumption scenarios.

(2) Enhance R&D and Innovation: Leverage its R&D capabilities to create differentiated, high-value products that meet evolving consumer preferences, reducing reliance on costly marketing campaigns.

(3) Optimize Brand Positioning: Strengthen retail presence (e.g., shelf visibility in supermarkets) and emphasize its leadership in the cheese sector to boost customer loyalty and brand equity.

6. Conclusion

Despite Milkground’s rapid growth, its long-term competitiveness and sustainable growth capabilities remain limited. The company faces operational challenges, notably weak profitability where revenue expansion has not translated into proportional profit growth, posing risks to its development. Financially, while capital utilization efficiency has historically been low, gradual improvements were observed in 2022. These issues primarily stem from rising raw material costs and intensified market competition, which have compressed profit margins, as well as excessive marketing expenditures aimed at securing market share and brand dominance in the burgeoning cheese sector. To address these challenges, we recommend strengthening supply chain stability through long-term contracts with suppliers to lock in pricing and procurement volumes, alongside strategic investments in eco-friendly dairy farms to secure raw material supplies. Additionally, diversifying its product portfolio—such as expanding into natural cheeses and innovative formats—can solidify Milkground’s market leadership and cater to evolving consumer preferences.

A company’s financial health and balanced development hinge on its core operational, financial, strategic, and governance capabilities (Bai, 2019). Proactive identification of root causes and targeted interventions are essential for sustainable growth. By aligning cost management with strategic innovation, Milkground can mitigate risks, enhance profitability, and transition toward a more resilient and sustainable growth trajectory.

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