

A Financial Analysis on Kweichow Moutai

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Abstract. Baijiu has always been a beloved and enduringly popular beverage in China, with Kweichow Moutai standing as a leader in the Chinese Baijiu industry. To assess the company comprehensively, an in-depth financial analysis is warranted. This study delved into three critical aspects disclosed in Kweichow Moutai's annual report - revenue recognition, fixed assets, and construction in progress - to evaluate the reasonableness of the company's accounting practices. Moreover, an exploration of the company's market performance was conducted by calculating the key financial indicators within four domains: liquidity, solvency, profitability, and investment analysis. While Kweichow Moutai exhibits some slight accounting deficiencies, the overall accounting practices remain clear and compliant with international standards. Furthermore, the company's market performance is highly favorable. Combined with insights from leading research institutions, the study concludes that Kweichow Moutai stands as an attractive investment option, supported by its impressive market performance and compliance with established accounting norms.

Keywords: Financial analysis, Kweichow Moutai, Baijiu industry.

1. Introduction

The company is a landmark of the domestic liquor industry, focusing primarily on the production and sale of Moutai along with producing and selling beverages, foodstuffs and packaging materials. The company is most famous for its production of Moutai, a premium brand of baijiu, which is a strong Chinese distilled spirit made from sorghum and is often considered one of the most prestigious and sought-after baijiu brands both in China and internationally. In addition to its iconic Moutai brand, Kweichow Moutai also produces other series of wines and alcoholic beverages. The company's financial performance and its impact on the Chinese and global spirits market are of great interest to investors and enthusiasts alike. Moreover, the company also concentrates on the development of anti-counterfeiting technology and the R&D of products relevant to the IT industry. Currently, the company's annual productivity of Moutai has surpassed 10,000 tonnes, creating a pioneering chronological ladder-type development mode of products in the domestic market. The company's products have formed three series of more than 70 specifications of varieties, enabling a comprehensive approach to the market. As a result, the company has taken the lead in the liquor market, and has dominated China's superior liquor market.

From 2023-02-13 to 2023-06-26, China Kweichow Moutai Distillery (Group) Co., Ltd has increased its shareholding by a total of 771.3 thousand shares of the company. As of 2023-06-28, the number of shares held was 679 million outstanding shares, accounting for 54.07% of the total number of outstanding shares. From 2023-02-13 to 2023-06-26, Guizhou Moutai Distillery (Group) Technology Development Co., Ltd has increased its holdings by 31.4 thousand shares of the Company. As of 2023-06-28, the number of shares held was 27,849,700, accounting for 2.22% of the total number of shares in circulation [1].

On Sep. 4th, the "sauce-flavored latte" co-branded by Moutai and Luckin Coffee was officially launched to greet the consumers. The sauce-flavored latte has broken the record of Luckin Coffee's single product sales, with sales exceeding 5.42 million cups on the first day and total revenue exceeding 100 million yuan [2]. The cross-border cooperation of Moutai serves as an essential method to break the boundary of the enterprise, expand the consumer group and to revitalize the brand image, which can promote the relationship with young consumers. Such awareness of the young consumers also complies with the long-term interest of the enterprise.

2. Accounting Analysis

2.1. Revenue Recognition

Kweichow Moutai, with its predominantly homogeneous operations, focused on the sale of Moutai and other wine series, follows a revenue recognition policy that aligns with international accounting standards. Such alignment is a crucial positive attribute, as it reflects a dedication to maintaining transparency and upholding industry-accepted best practices in recognizing revenue from the sale of their products. It also indicates a willingness to provide a clear and accurate picture of the company's financial performance, reinforcing trust in its reported figures.

According to the regulation disclosed in its annual report, the company recognizes revenue when control of goods transfers to the customer, which may reduce the risk of premature revenue recognition before the fulfillment of the company's obligations to the customer, which can be particularly important in industries where customer satisfaction, reputation, and quality are paramount. The revenue recognition policy is a critical aspect of financial reporting, as it significantly influences the financial statements as well as indicators most commonly used by investors, such as ROE, ROI, net profit margin and so on. The timing of control transfer herein in particular plays a crucial role in evaluating reported revenues and profitability.

Moutai's accounting policy for revenue recognition seems reasonable, yet a notable concern lies in the absence of specific criteria for determining when control of the merchandise has been transferred. The company does not provide clear guidelines on this matter as what its rival, Wuliangye Yibin Co., Ltd., has included in its annual report, which may lead to inconsistencies in revenue recognition [3].

2.2. Fixed Asset

Fixed assets are tangible assets with a useful life of more than one year and a high unit value that are held for use in the production of goods, provision of services, rental or business management. Kweichow Moutai classifies fixed assets into four main categories, namely buildings and structures, machinery equipment, electronic equipment, and transport equipment, and depreciates them uniformly using the straight-line method with a consistent residual value rate of 5%. Of these four categories, buildings and structures have the longest depreciable life (20 years), followed by machinery and equipment (10 years). Electronic equipment and transport equipment have both depreciated over five years. Such categorization allows for effective tracking and management of different types of assets. The uniform usage of the straight-line method, which is a conventional and straightforward approach to allocating the cost of assets over their useful lives, and the identical residual value rate of 5%, simplifies the depreciation process and ensures consistency in estimating an asset's value over time.

Taking Jan. 1st, 2014 as the cut-off date, machines and equipment dedicated only to research and development are depreciated over two years for electronic equipment and six years for machinery equipment once they exceed \$1 million thereafter. At the end of the period or year, fixed assets are examined on an item-by-item basis. If the recoverable amount of a fixed asset is less than its carrying amount due to a sustained decline in market value or because of technological obsolescence, damage, or prolonged inactivity, a provision for impairment of fixed assets is made based on the difference between the recoverable amount and its carrying amount. Provision for impairment of fixed assets is made on an individual asset basis. Such thorough evaluation ensures that the company remains aware of the condition, usefulness, and market value of its assets. The item-by-item examination is a prudent approach to asset management, as it allows for the identification of assets that may require special attention due to specific issues, such as technological obsolescence, damage, or inactivity.

In summary, Kweichow Moutai's fixed asset regulation provides a structured and systematic approach to managing and evaluating fixed assets. By classifying assets, uniformly depreciating them, conducting annual item-by-item examinations, and making provisions for impairment on an individual asset basis, the company ensures transparency, accuracy, and prudence in its financial

reporting. This approach helps in maintaining the reliability and trustworthiness of the company's financial statements.

2.3. Construction in Progress

In the annual report, Kweichow Moutai explicitly and thoroughly stipulates the accounting method of construction in progress and establishes the circumstances under which the construction in progress can be transferred to fixed assets, together with the main considerations for the provision for impairment of the construction in progress, which ensures that the recognition of assets aligns with the completion and readiness for use of the constructed assets and prevents premature recognition and accurately represents the economic reality of the company's fixed asset base. The fact that Kweichow Moutai outlines the main considerations for the provision for impairment of construction in progress is also an essential element of their financial reporting, as this shows the company's commitment to prudence and accuracy in accounting for projects that may face difficulties or delays. The provision for impairment ensures that the balance sheet reflects a more conservative valuation when projects are at risk of not achieving their expected outcomes.

There are currently a total of nine projects under construction with budgets exceeding one billion yuan, of which the Sauce-flavored Series Wine Production Technical Improvement and Ancillary Facilities Project, the Huanshan Wine Depot Project, the first phase of the Moutai Wine Technical Improvement and Ancillary Facilities Project in China Zone, and the "Twelfth Five-Year Plan" Expansion and Technical Improvement Project have already been completed. The most budgeted (155,160,000,000 yuan) construction project for the "14th Five-Year Plan" of Moutai Wine has just started in 2022 [4, 5]. Such disclosure provides valuable information to stakeholders since it indicates the company's significant investments in expansion and development, which can impact future revenue and profitability.

In summary, Kweichow Moutai's comprehensive regulation of construction in progress in its annual report signifies a strong commitment to transparent and prudent financial reporting. This approach ensures that construction projects are accounted for accurately, taking into consideration their readiness for use and potential impairment risks. Additionally, the disclosure of large-scale projects highlights the company's ambitious growth initiatives. These practices contribute to the reliability and integrity of the company's financial statements and enhance stakeholder confidence.

3. Performance

3.1. Liquidity Ratios

Kweichow Moutai's liquidity performance, as reflected by its current ratio, quick ratio, NWC to total assets, and cash ratio, appears robust and superior to its competitors in the alcoholic beverage industry.

Kweichow Moutai's current ratio of 6.35% as of 2023H1 suggests that the company has ample short-term assets to cover its current liabilities. The current ratio exceeding that of competitors is a positive sign as it implies a greater ability to meet its short-term obligations. However, an excessively high current ratio may also suggest that a company needs to be more efficiently utilizing its assets.

The quick ratio of 5.07% demonstrates that Kweichow Moutai has a substantial reserve of highly liquid assets to cover its current liabilities, excluding inventory. A quick ratio much higher than competitors indicates a strong ability to meet short-term obligations even without relying on inventory sales.

Unlike Wuliangye's over 3%, which indicates that the company may not have made every use of its assets, and Shanxi Fenjiu's average of less than 1%, which suggests that the company may have retained excessively low levels of cash, a cash ratio of 2% is generally considered acceptable. It shows that Kweichow Moutai holds a reasonable level of cash reserves relative to its current liabilities, as shown in Table 1.

Table 1. Liquidity Ratios of Kweichow Moutai and its Competitors

Company	20H1	20H2	21H1	21H2	22H1	22H2	23H1
Current Ratio							
Kweichow Moutai	4.89	4.06	4.05	3.81	4.95	4.41	6.35
Wuliangye	5.32	3.96	3.42	3.63	4.77	3.85	4.42
Luzhou Laojiao	2.52	2.57	2.48	2.43	2.42	3.15	3.26
Shanxi Fenjiu	1.70	1.64	1.97	1.77	2.10	1.97	2.23
Yanghe	3.37	2.54	2.56	2.01	3.41	2.58	4.28
Quick Ratio							
Kweichow Moutai	4.00	3.43	3.37	3.24	4.10	3.62	5.07
Wuliangye	4.49	3.44	3.02	3.22	4.18	3.40	3.89
Luzhou Laojiao	1.99	1.96	1.81	1.76	1.70	2.23	2.47
Shanxi Fenjiu	0.91	0.98	1.31	1.20	1.42	1.32	1.49
Yanghe	1.79	1.53	1.60	1.33	2.09	1.70	2.65
Cash Ratio							
Kweichow Moutai	0.90	0.82	1.24	0.89	1.41	1.19	2.21
Wuliangye	4.28	3.35	2.90	3.16	4.13	2.59	3.04
Luzhou Laojiao	1.51	1.50	1.53	1.30	1.53	1.77	2.24
Shanxi Fenjiu	0.61	0.48	0.69	0.85	1.20	0.83	0.54
Yanghe	1.74	1.51	1.59	1.32	2.07	1.65	2.61
NWC to Total Assets							
Kweichow Moutai	66.92	65.60	64.35	63.82	67.70	65.87	70.81
Wuliangye	72.71	67.15	63.55	65.27	70.50	66.66	69.11
Luzhou Laojiao	34.58	34.68	35.09	36.17	37.68	44.56	50.09
Shanxi Fenjiu	32.10	31.24	40.75	36.79	44.22	39.13	42.53
Yanghe	44.77	41.92	42.79	36.92	49.86	46.47	55.09

3.2. Solvency

Kweichow Moutai's solvency position, as indicated by its debt ratios, stands out as exceptionally strong and conservative compared to its competitors in the liquor industry. Kweichow Moutai consistently maintained the lowest debt ratio among China's leading liquor companies over the past three years. A low debt ratio signifies that the company relies less on external borrowing to finance its operations and expansion. This conservative approach to leverage reduces financial risk and enhances long-term stability.

Kweichow Moutai's long-term debt ratio remaining below 0.5% is remarkable. In contrast, competitor Luzhou Laojiao averages more than 15% over the same period. This significant disparity indicates that Kweichow Moutai prefers to finance its operations with equity and short-term debt rather than taking on long-term debt obligations [6]. This approach minimizes interest costs and long-term financial risks.

Kweichow Moutai's current debt-to-equity ratio being small in comparison to its competitors further illustrates its conservative financial strategy. This ratio is an indicator of short-term debt obligations relative to shareholders' equity. A lower current debt-to-equity ratio signifies that the company relies less on short-term debt to meet its financial obligations, reducing the risk associated with fluctuating interest rates and repayment pressures, as shown in Table 2.

Table 2. Solvency of Kweichow Moutai and its Competitors

Company	20H1	20H2	21H1	21H2	22H1	22H2	23H1
Debt Ratio							
Kweichow Moutai	17.24	21.40	21.28	22.81	17.26	19.42	13.39
Wuliangye	17.09	22.95	27.17	25.24	19.05	23.59	20.44
Luzhou Laojiao	35.62	33.78	34.78	34.89	35.57	33.19	42.72
Shanxi Fenjiu	46.39	49.11	42.55	47.97	40.36	40.73	37.72
Yanghe	20.30	28.58	28.85	37.34	21.76	30.07	17.64
Long-term Debt Ratio							
Kweichow Moutai	0.05	0.00	0.26	0.16	0.14	0.17	0.20
Wuliangye	0.34	0.30	1.29	0.62	0.44	0.24	0.27
Luzhou Laojiao	16.71	15.02	14.54	12.83	12.44	15.77	26.52
Shanxi Fenjiu	0.65	0.85	0.63	0.67	0.53	0.44	4.79
Yanghe	1.78	1.89	1.88	1.36	1.29	1.07	1.00
Current Debt to Equity							
Kweichow Moutai	21.57	28.31	27.75	30.56	21.41	24.84	15.90
Wuliangye	20.72	30.20	36.77	33.93	23.80	31.36	26.18
Luzhou Laojiao	35.65	33.58	36.66	39.04	41.28	31.14	38.82
Shanxi Fenjiu	87.83	98.49	75.26	93.71	68.67	69.63	56.64
Yanghe	23.64	38.09	38.62	58.21	26.51	41.98	20.45

3.3. Profitability

Kweichow Moutai's profitability, as demonstrated by its net profit margin and gross profit margin, is outstanding compared to other leading liquor companies in China.

The company's gross profit margin consistently averaging over 90% is an impressive achievement, as it indicates that the company generates a substantial profit from its core operations, primarily the production and sale of alcoholic beverages. Such a high gross profit margin is often associated with premium brands and efficient production processes. It reflects the company's ability to manage its production costs effectively while commanding premium prices for its products.

The net profit margin, averaging over 50%, signifies that Kweichow Moutai efficiently manages not only its production costs but also its operating expenses and taxes. This is a key indicator of strong profitability, as it measures the proportion of sales revenue that translates into net income after all expenses have been accounted for. A net profit margin of this magnitude demonstrates the company's ability to maintain a healthy bottom line.

Kweichow Moutai's lower inventory turnover compared to competitors suggests that the company may maintain higher inventory levels. While high inventory turnover is generally a positive sign, a lower inventory turnover may be acceptable for premium brands or products with limited supply. The observation that inventory turnover is higher at year-end compared to mid-year suggests that the company may stockpile inventory for peak demand or to ensure product availability, as shown in Table 3.

Table 3. Profitability of Kweichow Moutai and its Competitors

Company	20H1	20H2	21H1	21H2	22H1	22H2	23H1
Net Profit Margin							
Kweichow Moutai	54.44	52.18	53.39	52.47	53.99	52.68	53.66
Wuliangye	36.96	36.48	37.67	37.02	38.45	37.81	39.10
Luzhou Laojiao	42.24	35.78	45.79	38.45	47.79	41.44	48.80
Shanxi Fenjiu	23.42	22.27	29.53	26.99	32.97	31.12	35.73
Yanghe	40.23	35.47	36.45	29.64	36.49	31.19	36.00
Gross Profit Margin							
Kweichow Moutai	91.46	91.41	91.38	91.54	92.11	91.87	91.80
Wuliangye	74.54	74.16	74.96	75.35	76.92	75.42	76.78
Luzhou Laojiao	81.84	83.05	85.67	85.70	85.92	86.59	88.35
Shanxi Fenjiu	71.70	72.15	74.99	74.91	75.89	75.36	76.30
Yanghe	73.22	72.27	74.43	75.32	73.94	74.60	76.12
Inventory Turnover							
Kweichow Moutai	0.15	0.30	0.14	0.29	0.13	0.28	0.14
Wuliangye	0.58	1.10	0.70	1.20	0.67	1.21	0.66
Luzhou Laojiao	0.37	0.68	0.25	0.49	0.21	0.39	0.16
Shanxi Fenjiu	0.36	0.67	0.47	0.69	0.44	0.72	0.46
Yanghe	0.25	0.40	0.27	0.40	0.30	0.44	0.30

3.4. Investment

Kweichow Moutai's relatively high PB ratio over the past three years suggests that the market values the company at a premium relative to its book value. This premium may reflect the market's confidence in the company's brand, future growth potential, and sustainable competitive advantage. However, potential investors should be cautious about overpaying for shares, and the PB ratio should be considered in conjunction with other financial metrics.

Secondly, Kweichow Moutai's ROE being on par with competitors and not particularly impressive indicates that the company's profitability relative to its equity base is in line with industry standards. It's noteworthy that Shanxi Fenjiu stands out with a much higher ROE, which suggests it may be more effective in generating returns for its shareholders. Investors should consider Kweichow Moutai's ROE within the context of the industry and assess the reasons behind Shanxi Fenjiu's exceptional performance.

Thirdly, Kweichow Moutai's higher ROA, second only to Shanxi Fenjiu, indicates that the company is efficient in generating returns from its total assets. This is a positive sign, suggesting that the company effectively utilizes its assets to generate profits. A higher ROA can be an attractive feature for potential investors.

In summary, investing in Kweichow Moutai offers potential benefits and considerations, yet it's essential to monitor the competitive landscape, as shown in Table 4.

Table 4. Investment Analysis Indicators of Kweichow Moutai and its Competitors

Company	20H1	20H2	21H1	21H2	22H1	22H2	23H1
PB							
Kweichow Moutai	14.39	16.91	17.11	14.77	14.31	12.11	11.44
Wuliangye	9.04	14.11	12.17	9.29	7.99	6.54	5.67
Luzhou Laojiao	6.33	15.13	13.70	14.11	11.72	10.37	8.14
Shanxi Fenjiu	16.01	35.77	32.63	26.44	23.66	17.21	10.22
Yanghe	4.46	9.31	7.37	5.89	6.42	5.13	4.16
ROE							
Kweichow Moutai	16.54	31.41	15.26	29.90	15.61	32.41	18.06
Wuliangye	14.39	24.94	15.12	25.30	14.99	25.05	14.79
Luzhou Laojiao	16.22	28.27	17.84	31.13	19.40	33.30	20.46
Shanxi Fenjiu	20.41	35.76	30.85	42.51	30.09	44.31	29.81
Yanghe	14.75	19.95	14.49	18.54	15.77	20.85	16.17
ROA							
Kweichow Moutai	18.00	33.40	16.45	31.41	16.82	33.85	20.13
Wuliangye	14.94	25.13	14.61	26.01	15.83	25.74	14.79
Luzhou Laojiao	14.04	24.84	15.48	26.98	16.42	29.29	16.84
Shanxi Fenjiu	13.59	23.64	22.11	28.51	22.19	32.64	24.05
Yanghe	14.41	18.41	13.68	16.35	14.21	17.48	16.24

4. Strategic Forecast

4.1. Industry Pattern and Trend

Firstly, in terms of macroeconomics, China's long-standing favorable fundamentals has remained unchanged, and the per capita disposable income of the residents has continued to grow, which indicates that the demand for liquor consumption would be on an upward trend [7]. Secondly, from the perspective of industry development, China is facing a new trend of industry development with the superposition of the three phases of "new order reshaping period, new pattern forming period and new consumption upgrading period", in which the market consumption demand will be more concentrated and tilted to the advantageous production areas, head enterprises and excellent brands, making the industry's "Matthew effect" more obvious [8].

4.2. Profit Forecast

Kweichow Moutai took the initiative to regulate the delivery rhythm and price system in 23Q3 to ensure long-term healthy development. In addition, the current Maotai wine demand tenacity is still highlighted, in that the performance of the company has continued steady increase under external pressure, highlighting the company's brand barriers [9]. The company's full-year goal of total revenue growth of about 15% over the previous year is expected to be achieved successfully. Moreover, the effectiveness of the company's deepening marketing reform is likely to emerge in the future, enabling the company to continue the high-quality development of earnings with strong brand barriers, deepening marketing reform, high-quality quantity and price operations [10]. The major research institutes are now upholding their forecasts that the company will be profitable.

5. Conclusion

Kweichow Moutai, a prominent player in the Chinese liquor industry, demonstrates several strengths in its financial and operational aspects. The company's adherence to international accounting standards for revenue recognition and a focus on control transfer ensure transparency in reporting revenues, and its regulation for handling fixed assets, including specific criteria for control transfer and provisions for impairment, reflects prudent financial management.

Judging from the market performance, Kweichow Moutai may also appear to be an attractive investment option. First of all, Kweichow Moutai's solvency position is remarkably strong given its low debt ratios compared to competitors, signifying a conservative approach to financial leverage. Secondly, the company's liquidity performance, as evidenced by high current and quick ratios, is robust, highlighting its ability to meet short-term obligations comfortably. Thirdly, Kweichow Moutai boasts impressive profitability, with outstandingly high gross and net profit margins. However, its relatively lower inventory turnover is also worth noticing.

Last but not least, while Kweichow Moutai's PB ratio is relatively high, it actually reflects market confidence in the company's brand and growth potential. Its ROE and ROA are solid, although not exceptional, with Shanxi Fenjiu's outperformance. In summary, Kweichow Moutai's financial stability, efficient management of assets, and strong profitability make it an attractive investment option.

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