

Yum China (YUMC US / 9987HK)

Margin profile to remain resilient

- Further expansion of store network would offset the negative impacts from the normalization of consumer market and the potential decline in ticket average on growth momentum
- Resilient margin profile is a result of the flexible store model and disciplined cost saving
- Maintain **BUY**; TP implies 23.6x/21.7x 24E/25E P/E, or 3.5x/3.1x 24E/25E P/B

Growth momentum suppressed by cautious customer spending. 1Q24 revenue growth slowed to 1.4% YoY, much lower than the previous quarters. The high-base impact from 1Q23, which saw a revenue growth of 9.3% YoY, affected growth momentum in 1Q24. The Group continued to expand its restaurant network by adding 378 net new stores by end-1Q24, aligning with the Group's commitment of store network expansion. The Group remains flexible in store formats, such as adopting even smaller store formats that require less CapEx in lower-tier cities. In addition, transportation hub and tourist spots also saw robust trading on reviving travel-related consumption, according to the Group. Overall same-store traffic growth for KFC and Pizza Hut were 4% YoY and 8% YoY, but ticket average declined by 6% YoY and 12% YoY, showing cautious spending amid the current macro condition and intensifying competition. Our projected store network expansion remains unchanged. We expect by end-FY24E total number of stores would reach ~ 16.3k and by end-FY26E total number of stores would reach ~20.0k. However, we expect the potential decline of ticket average would weigh on growth momentum, resulting in lower FY24E revenue growth and FY23-26E revenue CAGR of 8.1% YoY and 8.6% vs. 11.2% YoY and 10.3% in previous report.

Strong margin profile showed effective cost management. In 1Q24, on a YoY basis, the Group's restaurant margin declined by 2.7ppt, while OPM and NPM⁽¹⁾ dropped at lower rate of 1.6ppt and 0.2ppt due to cost savings in G&A expenses. The Group's core OPM, which is adjusted for special item, F/X impact, and non-recurring income/expenses, only saw decline of 0.8ppt. We believe the Group's cost management discipline and flexible store formats would continue to generate cost savings, which would provide the Group room for promotion or value-for-money offerings to draw more store traffic. We expect margin profile to fluctuate in the coming quarters. Nonetheless, in FY24E, restaurant margin, OPM, and NPM⁽¹⁾ are expected to reach 16.5%, 10.8%, and 7.7%.

Maintain BUY; TP at US\$ 53.7/HK\$ 420.0. Maintain **BUY** on the leading position supported by expanding store network and resilient margin profile. We lowered our DCF-derived TP as our profit projections in FY24E & FY25E were revised down base on our updated outlook. Current TP represents 23.6x/21.7x 24E/25E P/E, or 3.5x/3.1x 24E/25E P/B.

Risk factors: 1) Macroeconomic risk; 2) Regulatory/policy risk; 3) Operational risk; 4) Inflation risk; 5) Business concentration risk; 6) Seasonality risk; 7) Non-GAAP financial metrics; 8) Fluctuations in EPS growth; 9) Changing customer behavior.

Results and Valuation

FY ended Dec 31	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue (US\$ mn)	9,569	10,978	11,870	12,929	14,053
Chg (% YoY)	(2.9)	14.7	8.1	8.9	8.7
Net profit (US\$ mn) ⁽¹⁾	442	827	915	993	1,166
Chg (% YoY)	(55.4)	87.1	10.6	8.6	17.4
EPS (US\$)	1.05	1.99	2.28	2.47	2.90
Chg (% YoY)	(55.1)	89.3	14.5	8.6	17.4
BVPS (US\$)	15.40	15.40	15.23	17.06	19.27
Chg (% YoY)	(7.9)	0.0	(1.1)	12.1	13.0
P/E (x) – US	35.90	18.96	16.56	15.25	12.99
P/E (x) – HK	35.93	18.98	16.58	15.27	13.01
P/B (x)– US	2.45	2.45	2.48	2.21	1.96
P/B (x) – HK	2.45	2.45	2.48	2.21	1.96
ROAA (%)	3.8	7.6	8.1	8.4	9.1
ROAE (%)	6.5	12.8	14.6	15.3	16.0
DPS (US\$)	0.48	0.55	0.64	0.64	0.64
Yield (%) - US	1.3	1.5	1.7	1.7	1.7
Yield (%) - HK	1.3	1.5	1.7	1.7	1.7

Source(s): The Group, ABCI Securities estimates

Company Report

May 7, 2024

Rating(US/HK): BUY/BUY
TP(US/HK):US\$ 53.7/HK\$ 420.0

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Price (US/HK)	US\$ 37.69/HK\$ 295
Est. price return (US/HK)	42.5%/42.4%
Est. dividend yield (US/HK)	1.7%/1.7%
Est. total return (US/HK)	44.2%/44.1%
Previous Rating &	BUY;
TP (US/HK)	US\$ 53.7/HK\$ 420.0
Previous Report Date	Feb 20, 2024

Source(s): Bloomberg, ABCI Securities estimate

Key Data

52Wk H/L (US\$) (US shr)	62.56/33.55
52Wk H/L (HK\$) (HK shr)	494.6/260.2
Total issued shares (mn)	404
Issued US shr (mn)	329
Issued HK shr(mn)	75
US-shr market cap (US\$ mn)	12,411
H-shr market cap (HK\$ mn)	22,103
3-mth avg daily turnover (US\$ mn) (US shr)	130.8
3-mth avg daily turnover (HK\$ mn) (HK shr)	193.3
Major shareholder(s) (%):	
JP Morgan	14.9

Source(s): Bloomberg, ABCI Securities

Price performance – US (%)

	Absolute	Relative*
1-mth	(2.5)	(2.1)
3-mth	4.9	0.1
6-mth	(16.9)	(35.8)

*Relative to S&P 500 Index

Source(s): Bloomberg, ABCI Securities

Price performance – HK (%)

	Absolute	Relative*
1-mth	(3.7)	(14.8)
3-mth	6.0	(13.7)
6-mth	(20.0)	(25.1)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Note:

- refers to net profit to shareholders of the Company ;
- US\$/HK\$= 7.8184; 3) Market data as of May 6, 2024

Exhibit 1: Changes in assumptions and valuations

As of Dec 31	Current report		Previous report		Rationale
	FY24E	FY25E	FY24E	FY25E	
Assumptions					
D/E (%)	2.2	1.8	2.2	1.8	Adjusted based on 1Q24 figures
D/A (%)	1.2	1.0	1.2	1.0	
Tax rate (%)	27.0	27.0	25.8	25.8	
Valuations					
TP (US\$)	53.7		58.8		TP is lower due to the lower profit projection in FY24E & FY25E
TP (HK\$)	420.0		460.0		
P/E (x)	23.6	21.7	26.7	24.6	
P/B (x)	3.5	3.1	4.0	3.6	

Note: for previous report publication date please refer to the first page of this company report
 Source(s): ABCI Securities estimates

Exhibit 2: Changes in major forecasts

As of Dec 31	Current report			Previous report			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Net revenue (US\$ mn)	11,870	12,929	14,053	12,202	13,453	14,785	(2.7)	(3.9)	(5.0)
Net profit (to shareholders of the Company) (US\$ mn)	915	993	1,166	916	994	1,161	(0.2)	(0.1)	0.4
EPS (US\$)	2.28	2.47	2.90	2.25	2.44	2.85	1.1	1.2	1.7

Source(s): ABCI Securities estimates

Exhibit 3: Quarterly performance

As of Dec 31	2Q22	3Q22	4Q22	1Q23	2Q23	3Q23	4Q23	1Q24
Revenue growth (YoY %)								
Total	(13.2)	5.1	(8.9)	9.3	24.7	8.5	19.4	1.4
KFC	(8.1)	12.0	(2.8)	9.0	24.5	8.4	17.7	1.5
Pizza Hut	(16.7)	1.8	(15.7)	9.1	23.7	6.8	22.8	(0.3)
Margins (%)								
<i>Restaurant margin</i>	<u>12.1</u>	<u>18.8</u>	<u>10.4</u>	<u>20.3</u>	<u>16.1</u>	<u>17.0</u>	<u>10.7</u>	<u>17.6</u>
KFC	13.4	20.6	12.7	22.2	17.3	18.6	12.0	19.3
Pizza Hut	8.6	13.4	1.9	14.2	12.4	12.7	7.3	12.5
<i>OPM</i>	<u>4.0</u>	<u>12.3</u>	<u>2.1</u>	<u>15.0</u>	<u>10.2</u>	<u>11.7</u>	<u>4.7</u>	<u>13.4</u>
KFC	7.7	16.5	7.4	19.4	14.0	15.9	9.1	17.0
Pizza Hut	2.5	8.8	(5.0)	9.3	6.4	8.0	1.1	8.0
<i>NPM (to shareholders of the Company)</i>	<u>3.9</u>	<u>8.5</u>	<u>1.1</u>	<u>9.9</u>	<u>7.4</u>	<u>8.4</u>	<u>3.9</u>	<u>9.7</u>

Source(s): the Group, ABCI Securities

Financial statements

Consolidated income statement

FY ended Dec 31 (US\$ mn, except per share data)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue	9,569	10,978	11,870	12,929	14,053
- Company sales	9,110	10,391	11,317	12,556	13,721
- Others	459	587	553	373	331
Company restaurant expenses	(7,829)	(8,701)	(9,446)	(10,427)	(11,352)
Restaurant profit	1,281	1,690	1,871	2,128	2,369
General and administrative expenses	(594)	(638)	(646)	(623)	(656)
Franchise expenses	(34)	(36)	(39)	(44)	(48)
Expenses for transactions with franchisees and unconsolidated affiliates	(279)	(356)	(362)	(373)	(382)
Other operating costs and expenses	(78)	(112)	(117)	(95)	(90)
Closures and impairment expenses, net	(32)	(29)	(31)	(30)	(33)
Other income, net	(94)	0	(2)	(3)	(2)
Operating profit	629	1,106	1,226	1,334	1,490
Others	58	120	138	148	250
Profit before taxes and equity in net earnings (losses) from equity method investments	687	1,226	1,365	1,482	1,740
Tax	(207)	(329)	(368)	(400)	(469)
Equity in net earnings (losses) from equity method investments	(2)	4	0	0	0
Net profit	478	901	997	1,082	1,271
- Owners	442	827	915	993	1,166
- MI	36	74	82	89	104
Cash Dividend	202	229	257	257	257
EPS (US\$)					
- Basic	1.05	1.99	2.28	2.47	2.90
- Diluted	1.04	1.97	2.26	2.45	2.88
Cash DPS (US\$)	0.48	0.55	0.64	0.64	0.64

Note: Items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Key operating figures

FY ended Dec 31 (US\$ mn, except store figures)	FY22A	FY23A	FY24E	FY25E	FY26E
Revenue					
- KFC	7,219	8,240	8,939	9,887	10,773
- Pizza Hut	1,960	2,246	2,464	2,722	2,979
Company sales					
- KFC	7,120	8,116	8,802	9,753	10,628
- Pizza Hut	1,939	2,214	2,431	2,693	2,949
Restaurant profit					
- KFC	1,121	1,440	1,573	1,756	1,952
- Pizza Hut	178	263	290	325	357
Operating profit					
- KFC	787	1,202	1,198	1,342	1,499
- Pizza Hut	70	142	129	148	170
Number of stores (units, as of end of FY)					
- Total	12,947	14,644	16,338	18,175	20,007
- KFC	9,094	10,296	11,503	12,778	14,021
- Pizza Hut	2,903	3,312	3,721	4,147	4,590

Note: Items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Consolidated balance sheet

FY ended Dec 31 (US\$ mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash and cash equivalents	1,130	1,128	836	846	2,153
Accounts receivable	64	68	67	109	81
Inventories	417	424	543	567	594
Others	2,329	1,811	1,753	1,855	1,816
Current assets	3,940	3,431	3,199	3,377	4,644
PP&E	2,118	2,310	2,422	2,548	2,699
Operating lease right-of-use assets	2,219	2,217	2,431	2,502	2,680
Intangible assets & goodwill	2,147	2,082	2,077	2,081	2,089
Others	1,402	1,991	2,483	2,592	2,837
Non-current assets	7,886	8,600	9,412	9,723	10,305
Total assets	11,826	12,031	12,612	13,100	14,949
Accounts payable and other current liabilities	2,096	2,164	2,620	2,283	2,978
Short-term borrowing	2	168	151	136	122
Income taxes payable	68	90	108	102	163
Current liabilities	2,166	2,422	2,880	2,521	3,263
Non-current operating lease liabilities	1,906	1,899	2,210	2,238	2,351
Non-current finance lease obligations	42	44	42	43	43
Others	552	547	564	554	555
Non-current liabilities	2,500	2,490	2,815	2,835	2,949
Shareholders' capital	6,482	6,405	6,121	6,860	7,749
MI	666	701	783	872	976
Total equity	7,148	7,106	6,904	7,732	8,725
Redeemable non-controlling interest	12	13	13	13	13
Total liabilities and equity	11,826	12,031	12,612	13,100	14,949

Note: Items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Consolidated cash flow statement

FY ended Dec 31 (US\$ mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Net profit	478	901	997	1,082	1,271
Depreciation and amortization	602	453	721	901	986
Change in working capital	203	24	168	(505)	734
Others	130	95	161	140	277
Cash flow from operating activities	1,413	1,473	2,047	1,618	3,269
Capital spending	(679)	(710)	(802)	(870)	(851)
Others	157	(33)	5	5	5
Cash flow from investing activities	(522)	(743)	(797)	(865)	(846)
Cash dividend	(202)	(216)	(257)	(257)	(257)
Others	(642)	(500)	(1,300)	(485)	(801)
Cash flow from financing activities	(844)	(716)	(1,558)	(743)	(1,056)
Effect of foreign exchange rate changes	(53)	(16)	15	(0)	(60)
Net change in cash, cash equivalent, and restricted cash	(6)	(2)	(292)	10	1,307
Cash, cash equivalent, and restricted cash - end	1,130	1,128	836	846	2,153

Note: Items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

Key operating and financial ratios

FY ended Dec 31	FY22A	FY23A	FY24E	FY25E	FY26E
Growth (YoY %)					
Net revenue	(2.9)	14.7	8.1	8.9	8.7
- KFC	3.1	14.1	8.5	10.6	9.0
- Pizza Hut	(7.1)	14.6	9.7	10.5	9.4
Restaurant profit	4.4	31.9	10.7	13.8	11.3
- KFC	10.7	28.5	9.3	11.6	11.1
- Pizza Hut	(20.5)	47.8	10.1	12.2	9.9
Operating profit	(54.6)	75.8	10.9	8.8	11.7
- KFC	(4.8)	52.7	(0.3)	12.0	11.7
- Pizza Hut	(36.9)	102.9	(9.5)	15.3	14.9
Core OP	N/A	78.8	11.7	10.6	11.4
- KFC	N/A	50.2	2.9	13.5	12.9
- Pizza Hut	N/A	197.9	1.4	16.6	17.2
Net profit (to shareholders of the Company)	(55.4)	87.1	10.6	8.6	17.4
Non-GAAP operating profit	(17.4)	77.1	9.9	8.5	11.7
Non-GAAP net profit	(15.0)	88.8	9.3	8.2	17.5
Profitability ratios (%)					
Restaurant margin	14.1	16.3	16.5	17.0	17.3
- KFC	15.7	17.7	17.9	18.0	18.4
- Pizza Hut	9.2	11.8	11.9	12.1	12.1
OPM	6.9	10.6	10.8	10.6	10.9
- KFC	11.0	14.8	13.6	13.8	14.1
- Pizza Hut	3.6	6.4	5.3	5.5	5.8
Core OPM	6.9	10.8	11.1	11.0	11.2
- KFC	11.3	14.9	14.2	14.5	15.0
- Pizza Hut	2.5	6.5	6.0	6.3	6.7
NPM (to shareholders of the Company)	4.6	7.5	7.7	7.7	8.3
Non-GAAP OPM	6.6	10.2	10.4	10.3	10.6
Non-GAAP NPM	4.7	7.7	7.8	7.7	8.3
Return ratios (%)					
ROAA	3.8	7.6	8.1	8.4	9.1
ROAE	6.5	12.8	14.6	15.3	16.0
Liquidity ratio (x)					
Current ratio	1.8	1.4	1.1	1.3	1.4
Quick ratio	1.6	1.2	0.9	1.1	1.2
Cash ratio	0.5	0.5	0.3	0.3	0.7
Working capital (days)					
Receivable turnover	2.5	2.2	2.1	2.5	2.5
Inventory turnover	50.3	43.7	46.2	48.6	45.8
Payable turnover	74.2	71.4	70.1	71.4	65.2
CCC	(21.5)	(25.4)	(21.8)	(20.3)	(17.0)
Leverage ratios (%)					
Total debt to Equity	0.0	2.4	2.2	1.8	1.4
Total debt to Total assets	0.0	1.4	1.2	1.0	0.8
Net debt/(cash) to Equity	(15.8)	(13.5)	(9.9)	(9.2)	(23.3)
Net debt/(cash) to Total assets	(9.5)	(8.0)	(5.4)	(5.4)	(13.6)

Note: 1) Restaurant profit is defined as company sales less expenses incurred directly by company-owned restaurants in generating company sales; 2) Restaurant margin is defined as restaurant profit divided by company sales; 3) Company sales refers to revenues from Company-owned restaurants; 4) OPM is defined as operating profit divided by company sales; 5) Core operating profit is defined as excludes special Items, and further adjusted for items affecting comparability and the impact of F/X; 6) Core OPM is defined as core operating profit divided by company sales; 7) Non-GAAP measures exclude the impact of share-based compensation expenses on operating costs and expenses; 8) Receivable turnover days equals the average of the beginning and ending balances of net accounts receivable for that FY divided by total revenues for that FY, and multiplied by the number of days; 9) Inventory turnover days equals the average of the beginning and ending balances of net inventory (including inventory procured by the Company, which is subsequently supplied to stores of unconsolidated affiliates and franchisees) for that FY divided by total cost of food and paper for Company-owned stores and stores of unconsolidated affiliates and franchisees for that FY, and multiplied by the number of days; 10) Payable turnover days equals the average of the beginning and ending balances of accounts payable related to inventory purchase and distribution for that FY divided by total cost of food and paper for Company-owned stores and stores of unconsolidated affiliates and franchisees for that FY and, multiplied by the number of day; 11) Items may not sum up due to rounding.

Source(s): The Group, ABCI Securities estimates

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Rating	Definition
Buy	Stock return rate \geq Market return rate ($\sim 7\%$)
Hold	- Market return rate ($\sim 7\%$) \leq Stock return rate $<$ Market return rate ($\sim 7\%$)
Sell	Stock return $<$ - Market return ($\sim 7\%$)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months
Market return rate: average market return rate since 2005 (2005-23 HSI total return index averages at 7.4%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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