

Yum China (YUMC US / 9987HK)

Short-term challenges remain

- FY21 revenue growth was 19.2% YoY on slower growth in 2H21 due to the COVID resurgence
- COVID-induced operational disruptions across the nation and rising costs of operation reduced margins, especially in 2H21
- Expect FY21E-24E revenue CAGR to reach 12.8% and restaurant count to reach ~15,000 by end-FY24E; lower FY22E restaurant margin, OPM, and NPM (to shareholders of the Company) to 14.1%, 10.9%, and 8.4%
- Maintain **BUY**; TP represents 27.18x/23.83x 22E/23E P/E, or 2.99x/2.91x 22E/23E P/B

Network expansion to support revenue growth. FY21 revenue growth reached 19.2% YoY, but 4Q21 revenue only edged up by 1.4% YoY. Overall growth slowed in 3Q/4Q due to COVID during the period, weighing down the FY21 performance. 4Q21 revenue growth of KFC and Pizza Hut was 2.3% YoY and 1.7% YoY, while FY21 revenue growth of the two brands was 20.3% YoY and 21.9% YoY. For FY22, we believe the risk of regional COVID-19 outbreaks remains high. Nonetheless, we believe the Group would leverage its expanding network to offer delivery or non-dine-in options to customers and deploy more sales initiatives in dealing with any operational disruption. We expect by end-FY22E, overall restaurant counts would increase by ~1,000 to ~12,800; by end-FY24E, the figure would reach ~15,000, representing a FY21-24E CAGR of 8.6%. The number of KFC and Pizza Hut restaurants would reach ~10,600 and ~3,100 by end-FY24E. We estimate a 15.4% YoY increase in overall FY22E revenue and a 12.8% FY21-FY24E revenue CAGR; FY22E revenue growth of KFCs and Pizza Hut would reach 16.6% YoY and 7.6% YoY; their FY21-FY24E revenue CAGR would be 14.0% and 8.4%, respectively.

Inflation and COVID-19 to complicate margin profile. Restaurant margin was impacted by regional COVID-19 outbreaks and rising costs of operation in 3Q/4Q. The Group's restaurant margin was 7.5% in 4Q21, compared to 12.2% in 3Q21; FY21 restaurant margin was 13.7% vs. 14.9% in FY20. However, OPM increased to 30.3% in 4Q21 vs. 7.7% in 3Q21 mainly due to non-cash gain from the fair value re-measurement of previously held equity interest held in Hangzhou KFC, in which the Group increased its investments in Dec 2021. We believe the rising global inflation and COVID-19 resurgence would complicate short-term margins. As a result, we expect restaurant margin, OPM, and NPM (to shareholders of the Company) to be 14.1%, 10.9%, and 8.4% in FY22E, down 2.0ppt, 1.2ppt, and 1.3ppt compared to our previous estimates.

Maintain BUY; TP at US\$ 61.7/HK\$ 481.6. Despite the short-term challenges, the Group's expanding network would solidify its leadership position in the restaurant industry and its proactive approaches in enhancing operational flexibility would help it deal with the pandemic uncertainty. Maintain **BUY**. We lower our DCF-derived TP, which represents 27.18x/23.83x 22E/23E P/E, or 2.99x/2.91x 22E/23E P/B, mainly due to the short-term pressure on margins.

Risk factors: 1) Macroeconomic risk; 2) Pandemic risk; 3) Regulatory/policy risk; 4) Operational risk; 5) Inflation risk; 6) Concentration risk; 7) Seasonality risk; 8) Non-GAAP financial metrics.

Results and Valuation

FY ended Dec 31	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (US\$ mn)	8,263	9,853	11,367	12,835	14,157
Chg (% YoY)	(5.8)	19.2	15.4	12.9	10.3
Net profit (US\$ mn) ⁽¹⁾	784	990	959	1,093	1,233
Chg (% YoY)	10.0	26.3	(3.2)	14.0	12.8
EPS (US\$)	2.01	2.34	2.27	2.59	2.92
Chg (% YoY)	6.3	16.4	(2.9)	14.0	12.8
BVPS (US\$)	15.91	16.72	20.62	21.25	23.98
Chg (% YoY)	95.0	5.1	23.3	3.0	12.8
P/E (x) – US	25.84	22.19	22.86	20.05	17.77
P/E (x) – HK	25.97	22.31	22.98	20.15	17.86
P/B (x) – US	3.26	3.11	2.52	2.44	2.17
P/B (x) – HK	3.28	3.12	2.53	2.46	2.18
ROAA (%)	9.1	8.5	6.7	6.5	6.5
ROAE (%)	16.9	14.9	12.2	12.4	12.9
DPS (US\$)	0.24	0.48	0.48	0.48	0.48
Yield (%) – US	0.5	0.9	0.9	0.9	0.9
Yield (%) – HK	0.5	0.9	0.9	0.9	0.9

Source(s): The Group, ABCI Securities estimates

Company Report

Feb 18, 2022

Rating (US): BUY
Rating (HK): BUY
TP (US): US\$ 61.7
TP (HK): HK\$ 481.6

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Price (US/HK)	US\$ 51.93/HK\$ 407.2
Est. price return (US/HK)	18.89%/18.27%
Est. dividend yield (US/HK)	0.92%/0.92%
Est. total return (US/HK)	19.81%/19.19%
Previous Rating&	BUY;
TP (US/HK)	US\$ 74.2/HK\$ 577.4
Previous Report Date	Aug 6, 2021

Source(s): Bloomberg, ABCI Securities estimate

Key Data

52Wk H/L (US\$) (US shr)	69.67/43.91
52Wk H/L (HK\$) (HK shr)	544/341.2
Total issued shares (mn)	422
Issued US shr (mn)	380
Issued HK shr(mn)	42
US-shr market cap (US\$ mn)	19,738
H-shr market cap (HK\$ mn)	17,066
3-mth avg daily turnover (US\$ mn) (US shr)	120.04
3-mth avg daily turnover (HK\$ mn) (HK shr)	74.40
Major shareholder(s) (%):	
Invesco	9.52

Source(s): Bloomberg, ABCI Securities

Price performance – US (%)

	Absolute	Relative*
1-mth	11.63	17.56
3-mth	(4.60)	1.65
6-mth	(13.49)	(12.65)

*Relative to S&P 500 Index

Source(s): Bloomberg, ABCI Securities

Price performance – HK (%)

	Absolute	Relative*
1-mth	12.49	9.67
3-mth	(3.38)	(1.37)
6-mth	(13.73)	(10.26)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Note:

1) refers to net profit to shareholders of the Company;
2) US\$/HK\$= 7.8002; 3) Market data as of Feb 17, 2022



Exhibit 1: Changes in assumptions and valuations

Exhibit 1: Changes in assumptions and valuations					
As of Dec 31	Current report		Previous report		Rationale
	FY22E	FY23E	FY22E	FY23E	
Assumptions					
D/E (%)	0	0	0	0	N/A
D/A (%)	0	0	0	0	
Tax rate (%)	26.5	26.5	26.5	26.5	N/A
Valuations					
TP (US\$)	61.7		74.2		Lower TP mainly due to lower margin forecasts
TP (HK\$)	481.6		577.4		
P/E (x)	27.18	23.83	26.22	23.21	
P/B (x)	2.99	2.91	3.70	3.30	

Note: Previous report was published on Apr 16, 2021

Source(s): ABCI Securities estimates

Exhibit 2: Changes in major forecasts

As of Dec 31	Current report			Previous report			Change (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Net revenue (US\$ mn)	11,367	12,835	14,157	11,364	12,877	N/A	0.0	(0.3)	N/A
Net profit (to shareholders of the Company) (US\$ mn)	959	1,093	1,233	1,104	1,247	N/A	(13.2)	(12.4)	N/A
EPS (US\$)	2.27	2.59	2.92	2.62	2.96	N/A	(13.4)	(12.6)	N/A

Source(s): ABCI Securities estimates



Financial statements

Consolidated income statement

FY ended Dec 31 (US\$ mn, except per share data)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	8,263	9,853	11,367	12,835	14,157
- Company sales	7,396	8,961	10,265	11,570	12,846
- Others	867	892	1,102	1,264	1,310
Company restaurant expenses	(6,298)	(7,734)	(8,817)	(9,950)	(10,966)
Restaurant profit	1,098	1,227	1,448	1,621	1,880
General and administrative expenses	(479)	(564)	(634)	(727)	(791)
Franchise expenses	(65)	(64)	(76)	(91)	(107)
Expenses for transactions with franchisees and unconsolidated affiliates	(633)	(649)	(868)	(975)	(1,052)
Other operating costs and expenses	(57)	(65)	(59)	(72)	(79)
Closures and impairment expenses, net	(55)	(34)	(42)	(44)	(51)
Other income, net	285	643	372	468	582
Operating profit	961	1,386	1,243	1,444	1,691
Others	147	6	118	100	51
Pretax profit	1,108	1,392	1,361	1,545	1,742
Tax	(295)	(369)	(361)	(409)	(460)
Net profit	813	1,023	1,000	1,136	1,281
- Owners	784	990	959	1,093	1,233
- MI	29	33	42	43	48
Cash Dividend	94	203	203	203	203
EPS (US\$)					
- Basic	2.01	2.34	2.27	2.59	2.92
- Diluted	1.95	2.28	2.21	2.52	2.84
Cash DPS (US\$)	0.24	0.48	0.48	0.48	0.48

Source(s): The Group, ABCI Securities estimates

Consolidated balance sheet

FY ended Dec 31 (US\$ mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Cash and cash equivalents	1,158	1,136	1,889	981	700
Accounts receivable	99	67	155	97	167
Inventories	398	432	553	639	669
Others	3,281	3,081	2,899	2,472	1,986
Current assets	4,936	4,716	5,496	4,189	3,523
PP&E	1,765	2,251	3,134	4,275	5,693
Operating lease right-of-use assets	2,164	2,612	3,740	4,930	6,679
Intangible assets & goodwill	1,078	2,414	2,540	2,667	2,832
Others	932	1,230	1,666	2,058	2,562
Non-current assets	5,939	8,507	11,080	13,930	17,765
Total assets	10,875	13,223	16,576	18,119	21,288
Accounts payable and other current liabilities	1,995	2,332	2,810	2,993	3,348
Income taxes payable	72	51	91	69	115
Current liabilities	2,067	2,383	2,900	3,062	3,463
Non-current operating lease liabilities	1,915	2,286	3,635	4,646	6,191
Non-current finance lease obligations	28	40	31	33	35
Others	394	592	399	462	484
Non-current liabilities	2,337	2,918	4,065	5,141	6,710
Shareholders' capital	6,206	7,056	8,702	8,966	10,118
MI	253	852	894	936	984
Total equity	6,459	7,908	9,596	9,902	11,102
Redeemable noncontrolling interest	12	14	14	14	14
Total liabilities and equity	10,875	13,223	16,576	18,119	21,288

Source(s): The Group, ABCI Securities estimates



Consolidated cash flow statement

FY ended Dec 31 (US\$ mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Net profit	813	1,023	1,000	1,136	1,281
Depreciation and amortization	818	940	1,302	1,661	2,153
Change in working capital	52	69	337	32	301
Others	(569)	(901)	31	2	107
Cash flow from operating activities	1,114	1,131	2,670	2,831	3,843
Capital spending	(419)	(689)	(927)	(1,193)	(1,313)
Others	(2,690)	(166)	140	578	459
Cash flow from investing activities	(3,109)	(855)	(788)	(616)	(854)
Share issuance - HK	2,195	0	0	0	0
Cash dividend	(95)	(203)	(203)	(203)	(203)
Others	(42)	(110)	(907)	(2,962)	(3,082)
Cash flow from financing activities	2,058	(313)	(1,110)	(3,165)	(3,285)
Effect of foreign exchange rate changes	40	15	(20)	40	15
Net change in cash, cash equivalent, and restricted cash	103	(22)	753	(909)	(281)
Cash, cash equivalent, and restricted cash - end	1,158	1,136	1,889	981	700

Source(s): The Group, ABCI Securities estimates

Key operating and financial ratios

FY ended Dec 31	FY20A	FY21A	FY22E	FY23E	FY24E
Growth (YoY %)					
Net revenue	(5.8)	19.2	15.4	12.9	10.3
Restaurant profit	(13.3)	11.7	18.0	11.9	16.0
Operating profit	6.7	44.2	(10.3)	16.2	17.1
Net profit (to shareholders of the Company)	10.0	26.3	(3.2)	14.0	12.8
Non-GAAP operating profit	(19.7)	4.6	25.9	4.3	13.5
Non-GAAP net profit	(15.6)	(14.6)	89.1	14.5	10.9
Profitability ratios (%)					
Restaurant margin	14.8	13.7	14.1	14.0	14.6
OPM	11.6	14.1	10.9	11.3	11.9
NPM (to shareholders of the Company)	9.5	10.0	8.4	8.5	8.7
Non-GAAP OPM	8.9	7.8	8.5	7.8	8.1
Non-GAAP NPM	7.4	5.3	8.7	8.9	8.9
Return ratios (%)					
ROAA	9.1	8.5	6.7	6.5	6.5
ROAE	16.9	14.9	12.2	12.4	12.9
Liquidity ratio (x)					
Current ratio	2.4	2.0	1.9	1.4	1.0
Quick ratio	2.2	1.8	1.7	1.2	0.8
Cash ratio	0.6	0.5	0.7	0.3	0.2
Working capital (days)					
Receivable turnover	4.1	3.1	3.6	3.6	3.4
Inventory turnover	49.1	44.1	45.7	48.9	48.8
Payable turnover	42.8	43.3	45.0	44.2	45.0
CCC	10.4	3.8	4.2	8.3	7.2
Leverage ratios (%)					
Total debt to Equity	0.0	0.0	0.0	0.0	0.0
Total debt to Total assets	0.0	0.0	0.0	0.0	0.0
Net debt/(cash) to Equity	(17.9)	(14.4)	(19.7)	(9.9)	(6.3)
Net debt/(cash) to Total assets	(10.6)	(8.6)	(11.4)	(5.4)	(3.3)

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) Non-GAAP measures exclude the impact of share-based compensation expenses on operating costs and expenses; 5) 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; 6) 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; 7) 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, multiplied by the number of day

Source(s): The Group, ABCI Securities estimates

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Rating	Definition
Buy	Stock return \geq Market return rate ($\sim 10\%$)
Hold	- Market return ($\sim 10\%$) \leq Stock return $<$ Market return rate ($+ \sim 10\%$)
Sell	Stock return $<$ - Market return ($\sim 10\%$)

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 2008 (HSI total return index 2008-20 CAGR at 9.2%)

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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