

Yum China (YUMC US / 9987HK) New expansion plan to promote growth

- The Group recently in its investor day event announced increasing its targeted net new store opening for FY23E to 1.4k – 1.6k; the Group will also raise total store count target to ~20k by FY26E
- Based on our updated store opening forecast, we project FY23E revenue growth to be 22.4% YoY; FY23E-25E revenue CAGR would be 17.8%
- Maintain BUY; current TP represents 32.89x/27.16x 23E/24E P/E, or 4.48x/3.91x 23E/24E P/B

Store network expansion plan shows room for growth. Enhancing penetration of the Chinese market to capture untapped markets and consumer groups continues to be the overarching growth strategy. In the investor day event, the Group raises FY23E annual net new store opening target to 1.4k-1.6k from the previous 1.1k-1.3k, while FY23E CapEx target is maintained at US\$ 700mn - US\$ 900mn, reflecting the higher cost efficiency in new store investment and the more flexible store formats to be adopted in the future. The Group also set the total store count target at 20k by FY26E, of which 15-20% will be accounted by franchising. The pace of store network expansion, in terms of net new store openings, would be much faster than previous years. Based on the total store count of 12,947 by end-FY22 and the planned net new store opening target in FY23E, we calculate that the annual net store opening would have to be above 1.8k in FY24E-26E vs. the FY20-22 average of ~1.25k to reach the ambitious target. The total CapEx budgeted for store network expansion in FY24E-26E would be US\$ 2.3 - US\$ 3bn, according to the Group. We believe the updated store expansion plan shows room for growth still exists despite the challenging consumer market at present.

Lifting our revenue projections to reflect accelerated store expansion pace. Based on the new guidance, we project the total store count to be ~14.5k in FY23E; of which KFC and Pizza Hut would take up ~10.1k and ~3.3k. Net new store opening for FY23E would be ~1.58k. By end-FY25E, the total store count would be ~18.1k, of which KFC and Pizza Hut would take up ~12.4k and ~4.1k. Average net new store opening for FY24E and FY25E would be ~1.8k. We raise our revenue growth forecast on the expanded store network. FY23E revenue growth would be 22.4% YoY, supported by the YoY revenue growth of KFC and Pizza Hut at 20.3% and 17.0%. FY22-25E revenue CAGR is projected at 17.8%.

Maintain BUY; TP at US\$ 76.2/HK\$ 596.0. The Group's ambitious store opening plan shows its confidence in China's consumer market and strengthening its strategic moat through supply chain development and digitalization infrastructure would further support revenue growth and profits, which supports the raised DCF-derived TP. Maintain BUY. Current TP represents 32.89x/27.16x 23E/24E P/E, or 4.48x/3.91x 23E/24E 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.

Results and Valuation

FY ended Dec 31	FY21A	FY22E	FY23E	FY24E	FY25E
Revenue (US\$ mn)	9,853	9,569	11,716	13,607	15,638
Chg (% YoY)	19.2	(2.9)	22.4	16.1	14.9
Net profit (US\$ mn) ⁽¹⁾	990	442	969	1,173	1,428
Chg (% YoY)	26.3	(55.4)	119.2	21.1	21.7
EPS (US\$)	2.34	1.05	2.32	2.81	3.42
Chg (% YoY)	16.4	(55.1)	120.7	21.1	21.7
BVPS (US\$)	16.72	15.40	17.02	19.48	22.36
Chg (% YoY)	5.1	(7.9)	10.6	14.4	14.8
P/E (x) – US	24.44	54.48	24.68	20.38	16.75
P/E (x) – HK	24.71	55.06	24.94	20.60	16.92
P/B (x)– US	3.42	3.72	3.36	2.94	2.56
P/B (x) – HK	3.46	3.75	3.40	2.97	2.59
ROAA (%)	8.5	3.8	8.1	8.8	9.6
ROAE (%)	14.9	6.5	14.2	15.4	16.3
DPS (US\$)	0.48	0.48	0.52	0.52	0.52
Yield (%) - US	0.8	0.8	0.9	0.9	0.9
Yield (%) - HK	0.8	0.8	0.9	0.9	0.9

Source(s): The Group, ABCI Securities estimates

Company Report Sep 19, 2023

Rating (US): BUY
Rating (HK): BUY
TP (US): US\$ 76.2
TP (HK): HK\$ 596.0

Analyst : Paul Pan
Tel: (852) 2147 8829
paulpan@abci.com.hk

Price (US/HK)	US\$ 57.2/HK\$ 452
Est. price return (US/HK)	33.3%/31.9%
Est. dividend yield (US/HK)	0.9%/0.9%
Est. total return (US/HK)	34.2%/32.8%
Previous Rating &	BUY;
TP (US/HK)	US\$ 73.3/HK\$ 571.5
Previous Report Date	Aug 2, 2023

Source(s): Bloomberg, ABCI Securities estimate

Key Data

52Wk H/L (US\$) (US shr)	64.7/38.58
52Wk H/L (HK\$) (HK shr)	514.5/300
Total issued shares (mn)	418
Issued US shr (mn)	377
Issued HK shr(mn)	42
US-shr market cap (US\$ mn)	21,537
H-shr market cap (HK\$ mn)	18,944
3-mth avg daily turnover (US\$ mn) (US shr)	96.2
3-mth avg daily turnover (HK\$ mn) (HK shr)	118.3
Major shareholder(s) (%):	
Invesco	8.0

Source(s): Bloomberg, ABCI Securities

Price performance – US (%)

	Absolute	Relative*
1-mth	5.2	3.3
3-mth	(3.7)	(4.7)
6-mth	(5.8)	(19.5)

*Relative to S&P 500 Index

Source(s): Bloomberg, ABCI Securities

Price performance – HK (%)

	Absolute	Relative*
1-mth	5.4	7.6
3-mth	(5.0)	5.5
6-mth	(8.4)	(0.3)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Note:

- 1) refers to net profit to shareholders of the Company ;
- 2) US\$/HK\$= 7.8183; 3) Market data as of Sep 18, 2023

Development of supply chain and infrastructure to enhance strategic moat. Supply chain development continues to be emphasized as a key part of building its strategic moat. The concept entails the following key components: 1) The Group aims to integrate upstream to complete its farm to table strategy, which would help ensure the safety and quality of its products, optimize the cost efficiency in raw material sourcing, and innovate product offerings with better raw material utilization; 2) To complete construction of one self-owned logistics center in Nanxiang in 2024 and to expand the number of cities and towns covered by its logistics network from more than 3k to more than 5k; 3) Investment in automation and intelligent network to optimize cost and service quality, enhance efficiency, and increase operational excellence would further complement the development of the logistics system. Total CapEx budgeted for supply chain and infrastructure development in FY24E-26E would be US\$ 700mn - US\$ 1bn, according to the Group.

Digitization strategy to further support growth. The Group has been investing heavily in digitization in consumer experience and behind-the-scene operation. During the event, the Group indicated that following its completion of the first two phases of digitization, the third phase would incorporate more AI technology. The Group's in-house digitization capabilities would be supported by AI algorithm, end-to-end digitization, data integration, cyber security, and YUMC Cloud. Further development of digitization will help curate a seamless customer experience, and consolidates management duties in areas such as physical stores monitoring, human resources, and inventory control. Total CapEx budgeted for digitization development in FY24E-26E would be US\$ 500mn - US\$ 1bn, according to the Group.

US\$ 3bn budgeted for dividend payment and share repurchase in FY24E-26E. The Group announced that US\$ 3bn is budgeted for dividends and share repurchase in FY24E-26E during the inventor day event. As of end-1H23, the Group had US\$ 1bn remaining for share repurchase. The additional budget for dividend and share repurchase reflects strong confidence in prospects.

Margin profile to improve. As the Group continues to optimize its cost structure with the business initiatives proposed, we believe restaurant operations, specifically, raw material costs, would benefit from the upstream integration synergy offered by the self-owned supply chain, and digitization infrastructure would raise efficiency in the management system. Overall, inflationary pressure arisen from raw material costs and staff costs would be partially offset, supporting a better margin profile. We project restaurant margin, OPM, and NPM (to shareholders of the Company) to rise to 17.1%, 12.5%, and 8.3% in FY23E and 17.5%, 13.7%, and 9.1% in FY25E.

Exhibit 1: Changes in assumptions and valuations

As of Dec 31	Current report		Previous report		Rationale
	FY23E	FY24E	FY23E	FY24E	
Assumptions					
D/E (%)	0	0	0	0	
D/A (%)	0	0	0	0	N/A
Tax rate (%)	30.9	30.9	30.9	30.9	
Valuations					
TP (US\$)	76.2		73.3		
TP (HK\$)	596.0		571.5		
P/E (x)	32.89	27.16	32.05	28.31	Higher TP on improved growth outlook
P/B (x)	4.48	3.91	4.31	3.80	

Note: Previous report was published on Aug 2, 2023

Source(s): ABCI Securities estimates

Exhibit 2: Changes in major forecasts

As of Dec 31	Current report			Previous report			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Net revenue (US\$ mn)	11,716	13,607	15,638	11,605	13,007	14,495	0.95	4.61	7.88
Net profit (to shareholders of the Company) (US\$ mn)	969	1,173	1,428	956	1,083	1,229	1.30	8.38	16.14
EPS (US\$)	2.32	2.81	3.42	2.29	2.59	2.94	1.30	8.38	16.14

Source(s): ABCI Securities estimates

Exhibit 3: Quarterly figures

As of Dec 31	2Q21	3Q21	4Q21	1Q22	2Q22	3Q22	4Q22	1Q23	2Q23
Revenue growth (YoY %)									
Total	28.9	8.8	1.4	4.3	(13.2)	5.1	(8.9)	9.3	24.7
KFC	32.7	9.4	2.3	10.1	(8.1)	12.0	(2.8)	9.0	24.5
Pizza Hut	26.9	7.8	1.7	1.1	(16.7)	1.8	(15.7)	9.1	23.7
Margins (%)									
<i>Restaurant margin</i>	<u>15.8</u>	<u>12.2</u>	<u>7.5</u>	<u>13.8</u>	<u>12.1</u>	<u>18.8</u>	<u>10.4</u>	<u>20.3</u>	<u>16.1</u>
KFC	16.8	13.6	8.6	15.2	13.4	20.6	12.7	22.2	17.3
Pizza Hut	13.1	8.2	5.9	10.7	8.6	13.4	1.8	14.2	12.4
<i>OPM</i>	<u>10.4</u>	<u>7.7</u>	<u>30.3</u>	<u>7.5</u>	<u>4.0</u>	<u>12.3</u>	<u>2.1</u>	<u>15.0</u>	<u>10.2</u>
KFC	14.2	11.2	4.1	11.1	7.7	16.5	7.5	19.4	14.0
Pizza Hut	7.2	3.5	(1.4)	5.5	2.5	8.8	(5.0)	9.3	6.4
<i>NPM (to shareholders of the Company)</i>	<u>7.4</u>	<u>4.1</u>	<u>20.7</u>	<u>3.7</u>	<u>3.9</u>	<u>8.5</u>	<u>1.1</u>	<u>9.9</u>	<u>7.4</u>

Source(s): the Group, ABCI Securities

Financial statements

Consolidated income statement

FY ended Dec 31 (US\$ mn, except per share data)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue	9,853	9,569	11,716	13,607	15,638
- Company sales	8,961	9,110	10,873	12,578	14,392
- Others	892	459	843	1,029	1,246
Company restaurant expenses	(7,734)	(7,829)	(9,016)	(10,411)	(11,878)
Restaurant profit	1,227	1,281	1,857	2,167	2,514
General and administrative expenses	(564)	(594)	(649)	(771)	(907)
Franchise expenses	(64)	(34)	(48)	(70)	(105)
Expenses for transactions with franchisees and unconsolidated affiliates	(649)	(279)	(531)	(590)	(630)
Other operating costs and expenses	(65)	(78)	(55)	(68)	(81)
Closures and impairment expenses, net	(34)	(32)	(37)	(42)	(47)
Other income, net	643	(94)	(18)	(18)	(23)
Operating profit	1,386	629	1,362	1,638	1,967
Others	6	58	104	138	194
Pretax profit	1,392	687	1,466	1,776	2,161
Tax	(369)	(207)	(453)	(548)	(667)
Net profit	1,023	478	1,014	1,228	1,494
- Owners	990	442	969	1,173	1,428
- MI	33	36	45	54	66
Cash Dividend	203	202	217	217	217
EPS (US\$)					
- Basic	2.34	1.05	2.32	2.81	3.42
- Diluted	2.28	1.04	2.29	2.77	3.38
Cash DPS (US\$)	0.48	0.48	0.52	0.52	0.52

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)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue					
- KFC	7,003	7,219	8,687	10,029	11,454
- Pizza Hut	2,109	1,960	2,293	2,683	3,111
Company sales					
- KFC	6,816	7,120	8,544	9,839	11,199
- Pizza Hut	2,092	1,939	2,255	2,635	3,048
Restaurant profit					
- KFC	1,013	1,121	1,586	1,819	2,083
- Pizza Hut	224	178	250	315	366
Operating profit					
- KFC	827	787	1,125	1,267	1,427
- Pizza Hut	111	70	109	143	160
Number of stores (units, as of end of FY)					
- Total	11,788	12,947	14,507	16,312	18,119
- KFC	8,168	9,094	10,101	11,278	12,446
- Pizza Hut	2,590	2,903	3,252	3,663	4,097

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)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash and cash equivalents	1,136	1,130	1,809	2,798	3,908
Accounts receivable	67	64	144	163	231
Inventories	432	417	555	567	798
Others	3,081	2,329	2,166	2,432	2,289
Current assets	4,716	3,940	4,674	5,960	7,225
PP&E	2,251	2,118	2,320	2,412	2,537
Operating lease right-of-use assets	2,612	2,219	2,305	2,462	2,555
Intangible assets & goodwill	2,414	2,147	2,194	2,218	2,217
Others	1,230	1,402	1,713	1,788	1,807
Non-current assets	8,507	7,886	8,531	8,880	9,117
Total assets	13,223	11,826	13,205	14,840	16,342
Accounts payable and other current liabilities	2,332	2,098	2,592	2,914	3,076
Income taxes payable	51	68	138	150	183
Current liabilities	2,383	2,166	2,729	3,064	3,259
Non-current operating lease liabilities	2,286	1,906	2,088	2,264	2,316
Non-current finance lease obligations	40	42	37	40	39
Others	592	552	513	552	539
Non-current liabilities	2,918	2,500	2,637	2,856	2,894
Shareholders' capital	7,056	6,482	7,115	8,142	9,345
MI	852	666	711	765	832
Total equity	7,908	7,148	7,826	8,907	10,176
Redeemable non-controlling interest	14	12	12	12	12
Total liabilities and equity	13,223	11,826	13,205	14,840	16,342

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)	FY21A	FY22A	FY23E	FY24E	FY25E
Net profit	1,023	478	1,014	1,228	1,494
Depreciation and amortization	516	602	647	738	916
Change in working capital	25	203	439	(136)	7
Others	(433)	130	82	131	140
Cash flow from operating activities	1,131	1,413	2,182	1,961	2,557
Capital spending	(689)	(679)	(742)	(1,127)	(1,347)
Others	(166)	157	22	10	12
Cash flow from investing activities	(855)	(522)	(720)	(1,117)	(1,335)
Cash dividend	(203)	(202)	(217)	(217)	(217)
Others	(110)	(642)	(535)	414	151
Cash flow from financing activities	(313)	(844)	(753)	197	(67)
Effect of foreign exchange rate changes	15	(53)	(30)	(52)	(45)
Net change in cash, cash equivalent, and restricted cash	(22)	(6)	679	989	1,110
Cash, cash equivalent, and restricted cash - end	1,136	1,130	1,809	2,798	3,908

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	FY21A	FY22A	FY23E	FY24E	FY25E
Growth (YoY %)					
Net revenue	19.2	(2.9)	22.4	16.1	14.9
- KFC	20.3	3.1	20.3	15.5	14.2
- Pizza Hut	21.9	(7.1)	17.0	17.0	15.9
Restaurant profit	11.7	4.4	45.0	16.7	16.0
- KFC	10.1	10.7	41.5	14.7	14.5
- Pizza Hut	23.8	(20.5)	40.6	25.9	16.2
Operating profit	44.2	(54.6)	116.6	20.2	20.1
- KFC	3.2	(4.8)	43.0	12.6	12.7
- Pizza Hut	79.0	(36.9)	55.5	31.0	12.1
Net profit (to shareholders of the Company)	26.3	(55.4)	119.2	21.1	21.7
Non-GAAP operating profit	4.6	(17.4)	115.2	20.2	20.1
Non-GAAP net profit	(14.6)	(15.0)	117.2	21.1	21.7
Profitability ratios (%)					
Restaurant margin	13.7	14.1	17.1	17.2	17.5
- KFC	14.9	15.7	18.6	18.5	18.6
- Pizza Hut	10.7	9.2	11.1	12.0	12.0
OPM	15.5	6.9	12.5	13.0	13.7
- KFC	12.1	11.0	13.2	12.9	12.7
- Pizza Hut	5.3	3.6	4.8	5.4	5.2
NPM (to shareholders of the Company)	10.0	4.6	8.3	8.6	9.1
Non-GAAP OPM	7.8	6.6	11.6	12.0	12.6
Non-GAAP NPM	5.3	4.7	8.3	8.6	9.1
Return ratios (%)					
ROAA	8.5	3.8	8.1	8.8	9.6
ROAE	14.9	6.5	14.2	15.4	16.3
Liquidity ratio (x)					
Current ratio	2.0	1.8	1.7	1.9	2.2
Quick ratio	1.8	1.6	1.5	1.8	2.0
Cash ratio	0.5	0.5	0.7	0.9	1.2
Working capital (days)					
Receivable turnover	3.1	2.5	3.2	4.1	4.6
Inventory turnover	45.6	47.6	46.0	47.0	50.6
Payable turnover	54.2	61.5	59.0	61.2	65.5
CCC	(5.5)	(11.4)	(9.7)	(10.1)	(10.2)
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	(14.4)	(15.8)	(23.1)	(31.4)	(38.4)
Net debt/(cash) to Total assets	(8.6)	(9.6)	(13.7)	(18.9)	(23.9)

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) Non-GAAP measures exclude the impact of share-based compensation expenses on operating costs and expenses; 6) 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; 7) 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; 8) 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; 9) Items may not sum up due to rounding.

Source(s): The Group, ABCI Securities estimates

Disclosures

Analyst Certification

The analyst, Paul PAN Hongxing, primarily responsible for the content of this research report, in whole or in part, hereby certify that all of the views expressed in this report accurately reflect my personal view about the subject company or companies and its or their securities. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or views expressed in this report. I and/or my associates have no financial interests in relation to the listed company(ies) covered in this report, and I and/or my associates do not serve as officer(s) of the listed company (ies) covered in this report.

Disclosures of Interests

ABCI Securities Company Limited and/or its affiliates may pursue financial interests to the companies mentioned in the report.

Definition of equity rating

Rating	Definition
Buy	Stock return rate \geq Market return rate ($\sim 9\%$)
Hold	- Market return rate ($\sim 9\%$) \leq Stock return rate $<$ Market return rate ($\sim 9\%$)
Sell	Stock return $<$ - Market return ($\sim 9\%$)

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 2006 (For reference: HSI total return index 2006-22 averaged at 8.4%)

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.

Disclaimers

This report is for our clients only and is for distribution only under such circumstances as may be permitted by applicable law. It has no regard to the specific investment objectives, financial situation or particular needs of any specific recipient. It is published solely for informational purposes and is not to be construed as a solicitation or an offer to buy or sell any securities or related financial instruments. No representation or warranty, either expresses or implied, is provided in relation to the accuracy, completeness or reliability of the information contained herein. This report would not be regarded by recipients as a substitute for the exercise of their own judgment. Any opinions expressed in this report are subject to change without notice and may differ or be contrary to opinions expressed by other business areas as a result of using different assumptions and criteria. The analysis contained herein is based on numerous assumptions. Different assumptions could result in materially different results. The analyst(s) responsible for the preparation of this report may interact with trading desk personnel, sales personnel and other constituencies for the purpose of gathering, synthesizing and interpreting market information. ABCI Securities Company Limited is under no obligation to update or keep current the information contained herein. ABCI Securities Company Limited relies on information barriers to control the flow of information contained in one or more areas within ABCI Securities Company Limited, into other areas, units, groups or affiliates of ABCI Securities Company Limited. The compensation of the analyst who prepared this report is determined exclusively by research management and senior management (not including investment banking). Analyst compensation is not based on investment banking revenues, however, compensation may relate to the revenues of ABCI Securities Company Limited as a whole, of which investment banking, sales and trading are a part. The securities described herein may not be eligible for sale in all jurisdictions or to certain categories of investors. The price and value of the investments referred to in this research and the income from them may fluctuate. Past performance is not necessarily indicative of future results. Foreign currency rates of exchange may adversely affect the value, price or income of any security or related instrument mentioned in this report. For investment advice, trade execution or other enquiries, clients would contact their local sales representative. Neither ABCI Securities Company Limited nor any of its affiliates, directors, employees or agents accepts any liability for any loss or damage arising out of the use of all or any part of this report. Additional information will be made available upon request.

Copyright 2023 ABCI Securities Company Limited

No part of this material may be (i) copied, photocopied or duplicated in any form by any means or (ii) redistributed without the prior written consent of ABCI Securities Company Limited.

Office address: ABCI Securities Company Limited, 13/F Fairmont House, 8 Cotton Tree Drive, Central, Hong Kong.

Tel: (852) 2868 2183