



Yum China Holdings, Inc. (YUMC)

Updated November 28th, 2023, by Yiannis Zourmpanos

Key Metrics

Current Price:	\$45	5 Year CAGR Estimate:	23.0%	Market Cap:	\$18.96 B
Fair Value Price:	\$62	5 Year Growth Estimate:	15.0%	Ex-Dividend Date:	11/27/2023
% Fair Value:	73%	5 Year Valuation Multiple Estimate:	6.5%	Dividend Payment Date:	12/19/2023
Dividend Yield:	1.2%	5 Year Price Target	\$124	Years Of Dividend Growth:	1
Dividend Risk Score:	C	Retirement Suitability Score:	F	Rating:	Buy

Overview & Current Events

Yum China Holdings, Inc. (YUMC) is China's largest restaurant company, with over 14,000 restaurants in over 1,900 cities. Yum China separated from Yum! Brands in October 2016.

On October 31st, 2023, Yum China announced Q3 2023 results reporting non-GAAP diluted EPS of \$0.59, missing market estimates by \$0.03. The revenue for the quarter was reported at \$2.91 billion, up 9.0% as compared to last year.

The company's total system sales also saw an impressive 15% year-over-year growth, primarily driven by a 15% increase at KFC and a 13% increase at Pizza Hut when evaluated in constant currency. This growth can be attributed mainly to the contributions from new units, improved same-store sales, and the comparison to a prior year impacted by temporary closures. Regarding same-store sales, YUMC experienced a 4% year-over-year increase, with KFC and Pizza Hut recording 4% and 2% growth, respectively, in constant currency. This improvement in same-store sales further underscores the company's strong operational execution and market resilience. A critical operational highlight was the addition of 500 net new stores during the quarter, bringing the total store count to 14,102 as of September 30, 2023. This expansion is a testament to YUMC's aggressive growth strategy and its confidence in the market.

Furthermore, the company's operating profit witnessed a 2% year-over-year increase, climbing to \$323 million from \$316 million. In constant currency terms, this represents a 9% increase, primarily fueled by sales leveraging. This improvement in operating profit reflects YUMC's efficient cost management and ability to capitalize on increased sales volumes. Overall, YUMC's third quarter results demonstrate robust revenue and sales growth, successful store expansion, and improved operational efficiency, positioning the company well for sustained growth in the competitive fast-food market.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	-	-	-	\$1.36	\$1.01	\$1.53	\$1.84	\$1.51	\$1.22	\$1.20	\$2.06	\$4.13
DPS	-	-	-	-	\$0.10	\$0.42	\$0.48	\$0.24	\$0.48	\$0.48	\$0.52	\$0.62
Shares	-	-	-	383.3	384.7	379.0	376.0	420.0	428.0	423.0	421.4	416.0

Yum China has grappled with COVID-19-related challenges with intermittent lockdowns from 2020 to the current year, which has affected its earnings in recent years. However, we believe the company is well-positioned for growth in the coming years with a favorable industry outlook. The fast-food restaurant industry still has a lot of room for growth, constituting only about 17% of restaurant spending compared with 61% in the US. We believe the trend will change in the coming years, driven by secular trends and Yum China.

The company would be the biggest beneficiary gaining substantial brand value and market size as macro headwinds subside. However, we maintain our EPS growth rate to 15.0%, which we believe is a fair reflection of the company's growth prospects as China economy is recovering. The company is continuing to expand its store count, which will be a catalyst for EPS growth in the next five years. In addition, we believe the company will be able to grow its dividends at a healthy pace in the future and have assumed a dividend growth rate of 20.0% for the next five years.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Avg. P/E	-	-	-	20.0	35.1	25.4	23.9	33.2	48.6	50.8	21.9	30.0
Avg. Yld.	-	-	-	-	0.3%	1.1%	1.1%	0.5%	0.8%	1.0%	1.2%	0.5%

Yum China is trading at a forward P/E of 21.9, significantly lower than the five-year average of 37.6. The stock is trading at a discount due to the uncertain economic outlook of the Chinese economy. We expect the P/E to normalize as earnings grow and have assumed a conservative P/E of 30.0 by 2028, leading to our 5-year price target of \$124.

Safety, Quality, Competitive Advantage, & Recession Resiliency

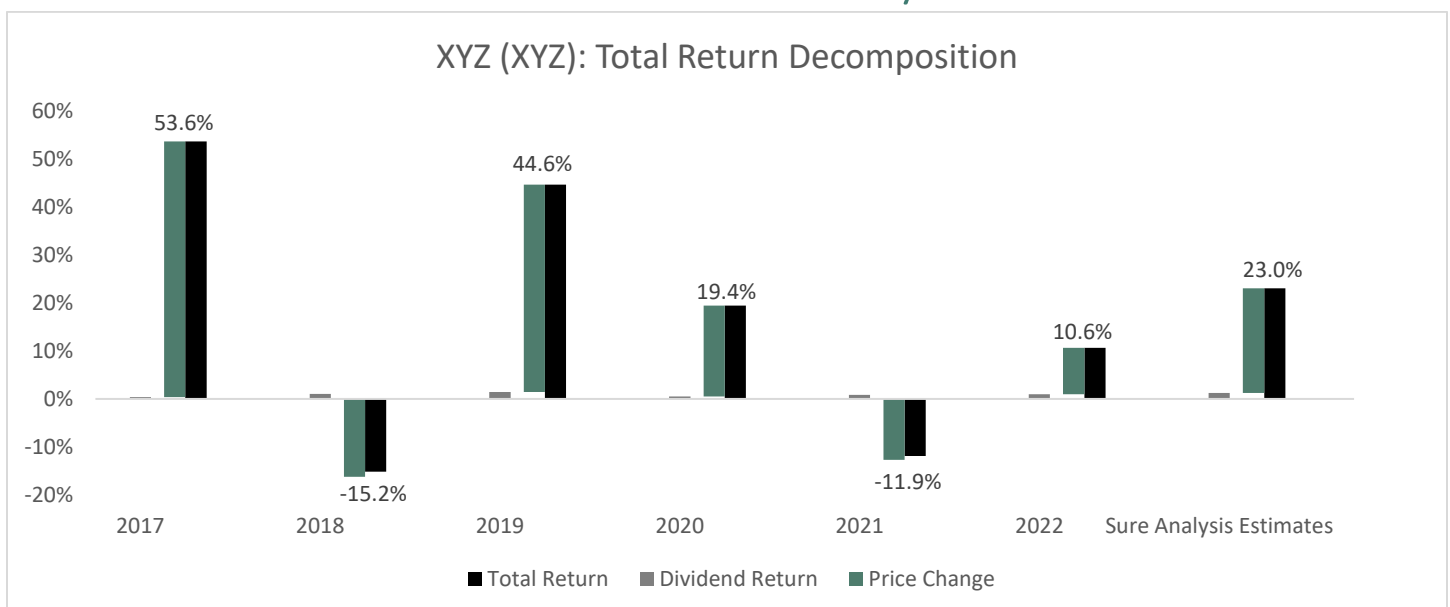
Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	-	-	-	0%	10%	27%	26%	16%	39%	40%	25%	15%

Yum China has a good payout ratio and has increased the dividends at a CAGR of 48.0% from 2017 to 2022. Yum China's most important competitive advantage is its high brand value. Moreover, focusing on menu innovations and efficient supply chain infrastructure, which results in cost advantages compared to smaller brands, gives Yum China an edge over other fast-food restaurant businesses. In addition, Yum China, as the largest restaurant chain, benefits from economies of scale, which allows it to exert significant influence over suppliers and guarantee access to food and other raw materials at stable, reasonable pricing. The business also operates in a recession-proof industry since everyone still requires food and drink to survive, no matter the macroeconomic situation. Recently, the company announced that it is increasing the total amount of its share repurchase authorization to \$3.4 billion by \$1 billion, and from 2017 to November 1, 2023, the company paid \$1.6 billion to repurchase approximately 36 million shares of common stock.

Final Thoughts & Recommendation

The company's fundamental business model is solid and will continue to thrive. The company has a solid balance sheet with \$3.1 billion available in cash and short-term investments as of the last quarter, which it can utilize to continue to expand and pay dividends to shareholders. Following the recent plunge in YUMC stock price, we maintain our buy rating premised upon the 23.0% annualized total returns for the medium-term, driven by forecasted earnings-per-share growth of 15.0%, a starting yield of 1.2%, and a valuation tailwind.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	6,905	6,934	6,909	7,075	7,769	8,415	8,776	8,263	9,853	9,569
Gross Profit	880	841	908	1,096	1,284	1,315	1,401	1,267	1,406	1,427
Gross Margin	12.7%	12.1%	13.1%	15.5%	16.5%	15.6%	16.0%	15.3%	14.3%	14.9%
SG&A Exp.	356	389	395	429	495	456	487	479	564	594
D&A Exp.	394	411	425	402	409	445	428	450	516	602
Operating Profit	529	469	511	652	761	830	863	709	734	658
Op. Margin	7.7%	6.8%	7.4%	9.2%	9.8%	9.9%	9.8%	8.6%	7.4%	6.9%
Net Profit	126	(7)	323	498	398	708	713	784	990	442
Net Margin	1.8%	-0.1%	4.7%	7.0%	5.1%	8.4%	8.1%	9.5%	10.0%	4.6%
Free Cash Flow	782	775	913	866	884	1,333	1,185	1,114	1,131	734
Income Tax	135	54	168	156	379	214	260	295	369	207

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets		3,257	3,201	3,727	4,287	4,610	6,950	10,875	13,223	11,830
Cash & Equivalents		238	425	885	1,059	1,266	1,046	1,158	1,136	1,130
Acc. Receivable		60	33	74	79	80	88	99	67	64
Inventories		260	189	268	297	307	380	398	432	417
Goodwill & Int.		216	192	167	340	520	481	1,218	2,552	2,270
Total Liabilities		1,303	1,216	1,284	1,440	1,633	3,775	4,404	5,301	4,666
Accounts Payable		501	438	480	420	619	623	708	830	727
Long-Term Debt		-	-	-	-	-	-	-	-	-
Total Equity		1,888	1,921	2,377	2,765	2,873	3,077	6,206	7,056	6,482
LTD/E Ratio		-	-	-	-	-	-	-	-	-

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets			10.0%	14.4%	9.9%	15.9%	12.3%	8.8%	8.2%	3.5%
Return on Equity			17.0%	23.2%	15.5%	25.1%	24.0%	16.9%	14.9%	6.5%
ROIC			16.4%	22.5%	15.0%	24.3%	23.2%	16.3%	13.8%	5.9%
Shares Out.	-	-	-	383.3	384.7	379.0	376.0	420.0	428.0	425.0
Revenue/Share	17.71	17.78	17.72	19.17	19.52	21.30	22.62	20.55	22.70	22.52
FCF/Share	2.01	1.99	2.34	2.35	2.22	3.37	3.05	2.77	2.61	1.73

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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