Tricon Restaurants International: Globalization Re-examined

The Malaysians go to Kentucky Fried and the Qataris go to Taco Bell for the same reason Americans go to Universal Studios—to see the source of their fantasies. Today, for better or worse, globalization is a means for spreading the fantasy of America around the World.[1]

—Thomas Friedman

Tricon Global Restaurants, headquartered in Louisville, Kentucky, operated and franchised the world's largest ensemble of fast food restaurants: Taco Bell, Pizza Hut, and KFC. The company, spun off from PepsiCo in October 1997, had been reorganized into four divisions, three domestic ones built around each of its three brands plus one to manage all of its international operations. Andrall Pearson—a class of 1947 HBS MBA and a former McKinsey partner, PepsiCo president, and HBS professor—had been appointed Tricon's chairman and CEO, and David Novak, its vice-chairman and president. As president of Tricon Restaurants International (TRI), Peter Bassi was in charge of Tricon's international operations.

Pearson and Novak set out to change Tricon's culture, improve unit economics, and refranchise some of the units the company owned. One of their immediate objectives was to reduce the $4.6 billion debt with which the spinoff had left Tricon. Meanwhile, Bassi worked on consolidating and standardizing Tricon's operations worldwide and focusing company efforts on a few key markets.

The Fast Food Industry

The revenues of the fast food industry worldwide were estimated at $160 billion in 1998. In 1997, 27 of the top 30 fast food chains worldwide were headquartered in the United States and accounted for over 60% of global fast food sales. They generated the bulk of their sales in the United States, which accounted for more than half the world market. But they were increasingly looking abroad for growth since sales were increasing at only about 5% annually in the United States: a bit slower than in Europe, and significantly slower than in other regions, where competition also tended to be more fragmented. China and Mexico, for example, were expected to grow in excess of 20%

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annually. While local chains had so far managed to retain leadership over U.S.-based competitors in a number of individual markets, their level of internationalization was still quite limited.

The Supply Side

Fast food chains typically attempted to offer the same experience at every outlet in the chain. They achieved uniformity in their offerings through standardization of the menu, production processes, raw material quality, appearance of outlets, and service levels. In broad terms, the cost of raw materials might account for 20-40% of store revenues, labor for 20%, and rent and utilities for about 25-30%. But these averages masked broad variations by food category (as **Exhibit 1** illustrates), as well as by country. In value-conscious developing markets, food and packaging accounted for a larger share of revenues and costs because of lower sales prices and labor costs, which were also often held down by lower turnover rates. In addition, the absolute level of food costs also varied across countries for more idiosyncratic reasons. Thus, in the case of pizza, cheese prices (approximately 50% of total food cost, on average) were much lower in New Zealand, which supplied countries as far away as Korea, than in North Atlantic countries where protection kept the prices of dairy products high. And in the case of chicken, while the United States benefited from some of the world's lowest feed costs (about 60% of the price of chicken), the Far East was a less expensive place to cut and prepare chicken because of lower labor costs (about 15% of the price of chicken). Demand-side differences also played a role: white meat sold at a premium in Europe and the United States, while the reverse was true in the Far and Middle East.

Rental costs also varied considerably. The availability and price of land was one obvious cost driver, while another related to the mix between on-premise and off-premise business (with the latter encompassing delivery, drive-through, and take-out). Generally younger Asian consumers tended to eat on-premise, while consumers in Canada, Australia, and the U.S. were more likely to eat off-premise. The rental and capital costs for off-premise establishments were significantly lower than for on-premise establishments. More-developed markets tended to have higher concentrations of off-premise establishments and, in fact, the sophistication of a market was sometimes gauged by the amount of off-premise business it could support.

Significant semivariable and fixed costs (including marketing, as well as the cost components discussed above) made volume a key to profitability. Thus, locations capable of generating adequate traffic were essential. Locational decisions were related to the mix of on-premise/off-premise business. On-premise stores were ideally located near or at traffic generators, such as shopping malls, movie theaters, stadiums, and airports. Take-out business did better in residential neighborhoods.

Franchising was prominent in fast foods, and vice versa. In the United States, franchised establishments accounted for 43% of fast food outlets by 1995, up from 15% in 1970. Franchised percentages exceeded this average for most of the large fast food chains, which accounted for 15 of the 20 largest franchised business format chains in the United States. Franchisees shouldered some or all of the capital costs (if they owned the land as well as the restaurant premises). In addition to paying a royalty and a share of the franchisor's local advertising costs, they also had to operate the business in accordance with the franchisor's standards of quality, service, cleanliness, and value. In return, the franchisor offered use of its trademarks, restaurant decor designs, signage, and equipment layout, its formulas and specifications for menu items, and its methods of operating, controlling inventory, accounting, and marketing as well as access to economies of scale in procurement and advertising. Franchisors sometimes bought out particularly profitable or (less typically) unprofitable franchises. They also helped broker the resale of the latter to other franchisees and, on occasion, wrested control away from franchisees with service or cleanliness problems (e.g., McDonald's repossessing its previously franchised restaurant on the Champs Elysée in Paris).

The largest fast food chains typically relied on a mix of franchised and company-owned units for their operations. This "plural" form of organization had been studied in depth in the United States for five successful chains, including KFC and Pizza Hut.[2] The research revealed significant complementarities between franchised and company-owned units. Franchising helped the chains to grow without capital investment. However, franchisees enabled the chains to increase local responsiveness and inject, through voluntarism, some reality checks into their decisionmaking processes. Company-owned units, in contrast, could be used to control development pace, and supplied a basis for building franchisee confidence (e.g., rapid roll out of new concepts). Also, mutual learning between the franchised and company-owned units seemed to depend on mechanisms such as cross-cutting career paths and ratcheting (the use of one type of operation to set standards for the other).

The Demand Side

Consumer spending on fast food was increasing more rapidly than total expenditures on food, for a variety of reasons. In some developed markets such as the United States, a primary reason for high fast food consumption was that many households had two working adults, who therefore cooked fewer and fewer meals at home. But in other developed markets such as France and Italy, fast food penetration remained quite limited. And in some less-developed markets, such as China, many of the relatively upscale customers were attracted more by the American "style" and experience afforded by U.S. fast food chains than by their food.[3] As a result, some KFC outlets in China, for example, did 10,000 transactions per week rather than the 2,500 that was the average for the United States.

In virtually all countries, however, some degree of local customization of product lines was essential given variations in local tastes. For religious reasons, pork could not be served in Muslim countries, and Hindus had to be offered lamburgers instead of hamburgers. White South Africans, used to large barbecues, preferred more beef on their burgers than customers elsewhere; black South Africans had more "global" tastes and preferred a spicy, Portuguese-style chicken. Chicken served in Asia was crispier, spicier, and less salty than that served in the West. Pizza was a bit more similar across countries, with changes in trimmings usually sufficing to localize it (although, even here, the preferred thickness of crusts was of considerable importance). Demand also sometimes shifted within countries because of events such as local health scares (e.g., mad cow disease in the United Kingdom). Additionally, some countries had their own fast foods: fish and chips in the U.K., tapas in Spain, sushi and bento in Japan, and dosas and samosas in India. And in countries such as Italy, fast food had made only limited headway against entrenched local culinary traditions (despite the fact that McDonald's, for example, offered pasta and espresso there). Italians had even established a society officially dedicated to "slow food"!

Although international chains attempted to adapt their products to local variations, considerations of standardization and consistency with their basic formats limited their ability to do so. They spent larger amounts of money attempting to create products with appeal that might transcend national boundaries. For example, in the mid-1990s, McDonald's spent more than $100 million developing and introducing the Arch Deluxe, a better-tasting premium burger targeted at adult consumers. The new product was, however, a dismal failure.

International chains pulled on several other marketing levers as well. They searched for ways to increase the average size of the order by bundling high-margin items, such as soft drinks and french fries, in value meal or "combo" packages. They began to target previously untapped segments, such as breakfast and dinner. But perhaps most importantly, they spent large amounts of money on advertising and promotions that involved expensive tie-ins with media icons or events (e.g., Tricon and "Star Wars").

International fast food chains were among the leading advertisers in most countries: Tricon and McDonald's, for example, ranked eighth and tenth respectively among all U.S. commercial advertisers in 1998. Advertising varied in content and quality across countries because of legislation, as well as more fundamental cultural differences, but many campaigns targeted children with catchy characters. Thus, one researcher characterized McDonald's as having a "childhood buddy" relationship with U.S. customers.[4] The same was probably true of some other leading fast food brands. New entrants and niche players were especially dependent on advertising to create trial and market awareness. Differences in advertising expenditure and effectiveness could also induce significant shifts in competitive position among larger players. For instance, Papa John's feisty comparative advertising campaign looked set to help it displace Little Caesar, which had cut back on media outlays in 1997 and 1998, as the third-largest U.S. pizza chain.

Key Concepts and Competitors

The fast food industry could be divided into at least twelve categories (see **Exhibit 2**). In addition, the array of choices available to consumers was also widened by theme park food services (e.g., Disneyland), contract food service (e.g., Marriott), and supermarket deli take-out arrangements (e.g., Boston Market), as well as ubiquitous "mom and pop" stores. This section focuses on the four categories that accounted for the bulk of the market—burgers, pizzas, chicken, and Mexican Food—and the leading competitor within each.

Burgers[5]

Burgers comprised the biggest single category in the fast food industry—probably more than one-third of the total—but had recently grown at below-average rates because of saturation, health concerns about red meats, and the outbreak of mad cow disease in the United Kingdom. Despite its size, the burger category was relatively concentrated. Reasons included its relative standardization and the $1 million-plus capital investment required for a state-of-the-art burger store. McDonald's, the category leader, was the largest and most profitable fast food company in the world. And the number two competitor in burgers, Burger King, only one-third McDonald's size, was, nevertheless, the second-largest single fast food chain in the world (although Tricon's three chains were collectively considerably larger).

The leader in burgers, McDonald's Corporation, was founded by Ray Kroc in 1955. In 1998, it generated systemwide sales of $36 billion from almost 25,000 units spread across 115 countries. Company revenues totaled $12.4 billion that year, and operating income totaled $2.8 billion. According to Interbrand, McDonald's was the second best-known brand in the world. McDonald's capital expenditures for 1998 were $1.9 billion, but, by its own account, the company enjoyed substantial free cash flow. During 1998, McDonald's bought back about $1.2 billion of its own stock as part of a $3.5 billion stock repurchase program to be completed by the end of 2001 (see **Exhibit 3** for selected financial data).

Approximately $1.5 billion or 80% of McDonald's total capital expenditures in 1998 were earmarked for outside the United States. McDonald's international operations accounted for 49% of the company's revenues and 57% of its profits. Even more important, that was where McDonald's future growth was expected to come from. Within the United States, saturation seemed to have set in: net additions of units there were negligible since there was already one McDonald's outlet there for every 23,000 people. But the $1.5 billion invested overseas allowed McDonald's to add about 1,600 units to its system there, bringing the total number to 12,300. In 1998, McDonald's International generated systemwide sales of $18 billion, company revenues of $7.7 billion, and operating profits of $1.8 billion. Overall, about 86% of systemwide sales (and greater than 100% of company profits, some observers guessed) were accounted for by just 11 of the countries in the McDonald's system: Australia, Brazil, Canada, England, France, Germany, Hong Kong, Japan, the Netherlands, Taiwan, and the United States. Europe (44% of international units) had been the major growth driver in 1998, as both Asia Pacific (33% of international units) and Latin America (10% of international units) were affected by regional economic crises (see **Exhibit 4** for some additional geographic data).

McDonald's basic strategy was well known and had stayed fairly stable over time (see **Exhibit 5**). While the strategy had many features, its most distinctive one was the consistency that the company tried to achieve in key processes. For example, McDonald's operating manual had, over time, specified increasingly detailed procedures to be followed, raw materials to be used, the end-products to be produced, and the services to be provided. It specified, for example, that french fries have a sugar content of 21%, that a pound of cheese yield 32 slices, and so on. (The equipment used at each store was meant to make following such instructions easy for even an unskilled worker.) Other examples included the painstaking way in which McDonald's nurtured a small number of suppliers willing to work with stringent specifications, the deliberateness with which it approached foreign market entry decisions, and its carefully-developed skills at site selection. McDonald's heavy reliance on frozen food inputs (e.g., beef patties) had also helped impose some order by forcing investments to be made around a supply chain rather than helter-skelter.

Of course, McDonald's had needed innovation as well as consistency to build and sustain its market leadership. A major milestone was a franchisee's invention of the Big Mac in 1968. This product became such a cultural icon that the *Economist* eventually devised a Big Mac index for comparing the costs of living in various cities. Another franchisee invented the Egg McMuffin as a breakfast-menu item in 1973. The Egg McMuffin became the basis for a breakfast line that now accounted for about 15% of the company's sales. Chicken McNuggets were introduced in the 1980s, after a seven-year development program, and quickly came to account for 7.5% of domestic sales. But in the 1990s, instead of a comparable success, McDonald's experienced the large-scale failure of the Arch Deluxe. While the company remained focused on burgers as main dishes, particularly in the Unites States, chicken accounted for an increasing portion of sales, especially in Asia, where the company had begun offering not only sandwiches and nuggets, but also a chicken on the bone product (McCrispy) to cater to local preferences for dark meat. New CEO Jack Greenberg planned to leverage the "elasticity" of the McDonald's brand and provide "almost anything people will eat" as long as it was consistent with the company's mode of operation.[6] McDonald's had also entered into major alliances with the likes of Coca-Cola and Disney.

Despite such changes, McDonald's value chain remained geared towards consistency of experience rather than product taste or variety, and had been challenged on those bases. Burger King had mounted an aggressive marketing campaign claiming greater customization and better-tasting food. As part of its response, McDonald's had invested nearly $200 million in a new generation of kitchen technology called "Made for You" that it had started to roll out domestically. Overseas, local burger chains had managed to best McDonald's in a few countries. In the Philippines, for example, Jollibee had seized over 40% of the local market by tailoring its products to local tastes—sweet and spicy burgers, fried chicken, noodles and mango peach pie.[7] Apart from the product line and lower prices, virtually everything else—the operating systems, equipment, service offerings, and even the kid's mascot, Jolly Bee—appeared to be modeled on McDonald's. McDonald's responded with Burger McDo, a sweeter burger, and McSpaghetti (*not* offered in Italy), but with only limited success.

Pizza[8]

Pizzas were roughly tied with chicken as the second-largest fast food category after burgers—probably about 15% of the total. The pizza market was much less concentrated than the burger market, reflecting the proliferation of small, but entrenched independents. Capital requirements were low in the pizza business: about $300,000 for a state-of-the-art on-premise pizza parlor (not including land), or as little as $150,00-$200,000 for an establishment focused on delivery.

In addition, high "tickets" ($10-12 per pizza) and low order flows made the pizza business less complex. Whatever the reasons, small, neighborhood pizzerias were expected to grow faster than top pizza chains in the United States over the next five years.

The leader in pizzas, Pizza Hut, dated back to a pizza parlor opened by Dan and Frank Carney in 1958 in Wichita, Kansas. Franchising began early at Pizza Hut, so that it had almost 3,200 units, including more than 100 outside the United States, by the time PepsiCo acquired it in 1977 for $300 million. In 1998, Pizza Hut generated system-wide sales of $7.2 billion from 12,285 units. Pizza Hut's international activities, organized under Tricon Restaurants International, encompassed 3,814 units and accounted for 33% of the systemwide sales under the Pizza Hut brand. As of the end of 1998, 35% of units in the United States were company-owned, versus 26% overseas (where another 17% were accounted for by joint ventures). Further reductions in company-ownership on both fronts seemed likely as part of Tricon's refranchising strategy (described in the next section). Also, the number of U.S. units had dropped by 3% and that of international units by 1% during 1998 as part of a policy of closing unprofitable units that could not be refranchised.

Although Pizza Hut became the leading pizza chain worldwide in terms of both sales and units in 1971, it subsequently had to beat back several challenges to its leadership from varied number twos. The company's responses had included deep-dish pan pizzas, "personal" pizzas that boosted lunchtime traffic, and the launch of its own delivery business.

In 1998, Pizza Hut continued to face fresh challenges from the number two competitor, U.S.-based Domino's, which reported systemwide sales of $3.2 billion and company revenues of $1.2 billion from 6,250 units worldwide. At the end of 1998, a group of investors led by Bain Capital acquired Domino's, which described itself as the world's largest pizza delivery chain, from its founder for approximately $1 billion. During that year, Domino's had introduced an innovative heat-retaining delivery pouch. This was part of a $200-million multiyear re-imaging campaign that also included new flavored crusts, a new typeface and bolder logo, changes to store design, new pizza boxes, and new employee uniforms. Pizza Hut, in turn, spent tens of millions of dollars on a quality initiative dubbed "totally new pizzas," which featured fresh pizza toppings and a reformulated sauce, more consistent oven temperatures, and the installation of 2,500 phones to take new orders more quickly. Pizza Hut continued to seek a 15-25% price premium for itself and to refrain from selling pizza by the slice.

Internationally, Pizza Hut also faced challenges from local competitors, including ones that were trying to go global. The most important example was Telepizza of Spain. Founded by a former Johnson & Johnson executive of Cuban origin in the late 1980s, Telepizza focused on the delivery business in Spain. Its IPO at the end of 1996 valued it at over $1.5 billion. Telepizza was considered instrumental in increasing the share of pizza in the fast food market in Spain to 38%, compared to 15-16% in the United States and the United Kingdom and 8-9% in France and Germany. Outside Spain, Telepizza had entered Portugal, Mexico, and Poland in 1992, Chile in 1993, and France in 1998, with the United Kingdom, Morocco, Germany, Brazil, and several other countries targeted for 1999-2000. At the end of 1997, Telepizza had 399 units in Spain and 68 overseas. By way of comparison, Pizza Hut had 150 units in Spain at the end of 1995, 122 at the end of 1996, and 123 at the end of 1997.[9]

Chicken[10]

Chicken was roughly tied with pizza as the second-largest fast food category after burgers, but was more internationalized (i.e., less U.S.-dominated). In the U.S., KFC accounted for 55% of the market, followed by Popeye's with 8%, and Church's with 6%. The market overseas, though more fragmented, was growing much more rapidly.

The leader in quick service chicken restaurants, KFC (formerly Kentucky Fried Chicken), could be traced back to a restaurant opened in Corbin, Kentucky in 1939 by Colonel Harland D.

Sanders. After he was forced out of business by the interstate highway system in 1952, the Colonel began to franchise his way of frying chicken with a blend of 11 herbs and spices and pressure-cooking. The company was listed on the New York Stock Exchange in 1969 and, after two other changes in ownership, was sold to PepsiCo for $840 million in 1986. At the time, the KFC system had more than 6,500 units, including more than 1500 outside the United States. Its acquisition made PepsiCo the largest fast food competitor in the world in terms of units and the second-largest in terms of sales.

In 1998, KFC generated system-wide sales of $8.3 billion from 10,423 units. KFC's international activities, organized under Tricon Restaurants International, encompassed 5,291 units and accounted for 49% of the systemwide sales under the KFC brand. As of the end of 1998, 32% of units in the United States were company-owned, versus 21% overseas (where another 9% were accounted for by joint ventures). Further reductions in company-ownership on both fronts seemed likely as part of Tricon's refranchising strategy (described in the next section). Also, the number of U.S. units had remained virtually flat, while international units increased by 3% during 1998.

KFC had largely invented its category and claimed a larger share of it than either McDonald's or Pizza Hut did of theirs. But growth in the U.S. had been limited in recent years—although Tricon professed to see significant expansion opportunities for all its chains domestically. Outside the United States, KFC accounted for 62% of Tricon Restaurants International's sales, compared to 36% for Pizza Hut and 2% for Taco Bell. The challenges of running KFC's international business were compounded by the fact that the chicken business seemed to vary more from country to country than did the pizza or burger business. One apparent reason was that local tastes for chicken tended to be more sharply defined than tastes for pizzas (under the toppings) or burgers. Other sources of cross-country variation included income and daypart positioning. In Australia, KFC was positioned for the mainstream middle class, while in the U.S. it was more blue collar. In the United Kingdom (outside London), KFC was mostly an evening meal concept, but in France and Spain, sales were mostly during lunchtime and, thus, competed directly with burger sales. In fact, KFC in the U.S., taking its cues from the French and Spanish markets, had announced plans to enter the chicken-sandwich business in direct competition with McDonald's and Burger King. Other new products included Popcorn Chicken and Crispy Strips, which quickly proved to be popular on-the-go. Overall, KFC was priced at a 15% premium to McDonald's and offered food quality similar to Burger King's. Early efforts at global advertising had proved very difficult until recent successes with an animated Colonel Sanders, who was easy to dub and otherwise localize. Same store sales grew 12% during the month after the Colonel's first Popcorn Chicken commercials.

KFC's indirect competitors had included not only the leaders in other traditional fast food categories, but also Boston Market. This chain, widely considered responsible for pioneering the chicken home-meal-replacement segment, had briefly been second in the chicken market in terms of unit share and unit growth, with annual sales per unit that amounted to $1 million in 1997, compared to $800,000 for KFC. But Boston Market's attempt to launch the Extreme Carver sandwich amidst great fanfare to compete with fast food restaurants for the lunch market proved to be a disaster. Despite widening discounts, the product was judged too expensive. Boston Market began 1998 with $800 million in long-term debt, a $312-million loss in the first quarter, and a system with significant numbers of new stores that were up to three years away from achieving profitability. It filed for bankruptcy in October 1998 and was subsequently acquired by McDonald's.

Mexican Food[11]

The Mexican quick-service restaurant industry was estimated to account for 5% of the worldwide fast food market, but was largely confined to the United States. Market concentration was high, with Taco Bell alone accounting for 73% of market share. The next largest players, Taco John's and Del Taco had shares of 3% each.

Taco Bell dated back to a Mexican restaurant started by Glen Bell in Downey, California in 1962. Taco Bell went public in 1969 and opened its first international restaurant in 1977. PepsiCo acquired Taco Bell at a time when it had 860 units, mostly concentrated in the West and Southwest. Twenty years later, Taco Bell generated system-wide sales of $5 billion from 7,055 units. Taco Bell's international activities, organized under Tricon Restaurants International, encompassed 75 units—concentrated in Canada, Puerto Rico, and Central and South America—and accounted for 3% of the systemwide sales under the Taco Bell brand. As of the end of 1998, 24% of units in the United States were company-owned. The total number of U.S. units had changed by 2% from the previous year, and the number of company-owned units was down by 25%, in line with refranchising efforts.

While Taco Bell remained domestically focused, it had also recently been the single most important driver of growth domestically. It had aggressively expanded access points in the 1990s, and was promoting a tiered menu strategy with which it could continue being a mid-tier, family food provider, while also selling cheaper fare focused on teens. Taco Bell had also recently entered the $20 billion "after-five" dinner category with the $9.99 12-item Grande Meal. In 1998, it launched an advertising campaign featuring a bilingual chihuahua, Gidget, which quickly became a cultural icon in the United States (see **Exhibit 6**). Gidget was not, however, universally employable. For example, dogs were taboo in some Asian countries and considered delicacies in others.

Tricon Global Restaurants and Tricon Restaurants International

PepsiCo spun off KFC, Pizza Hut, and Taco Bell into Tricon Global Restaurants in 1997. Across its three formats, Tricon operated or franchised more units than any other fast food chain in the world—29,000 in total, employing more than 500,000 people in 102 countries. In 1998, its system-wide sales (including franchisees' revenues) were $20.6 billion, its company revenues $8.5 billion, its operating profits $1,028 million, and its net income $445 million, up from a $111 million loss the previous year. The market value of Tricon's common stock amounted to $7.3 billion at the end of 1998, up from $4.3 billion at the end of 1997. The spinoff from PepsiCo had also left it with a debt load of $4.6 billion, seven times the 1998 cash flow from operating activities (see **Exhibit 7** for additional financial data).

History

Prior to the spinoff, PepsiCo's restaurant businesses had not been as successful as the company had hoped. For one thing, Coca-Cola had started an aggressive advertising campaign in the late 1980s to convince non-Pepsi fast food chains to buy Coca-Cola syrup rather than Pepsi-Cola syrup to avoid cross-subsidizing some of their toughest competitors in fast foods. Both Burger King and Wendy's switched from Pepsi-Cola syrup to Coca-Cola syrup in 1991, flattening Pepsi's sales growth for the year. On the restaurant side, PepsiCo initially invested substantially in disparate equity operations around the world, and then partially reversed course by beginning to refranchise company-owned restaurants. PepsiCo launched a restaurant services company with the objective of improving operational efficiency in all restaurants, and a restaurant supply company, founded in the early 1980s, was divested. In early 1995, the international arms of KFC and Pizza Hut were consolidated into PepsiCo Restaurants International. Peter Hearl, EVP of Tricon Restaurants International, commented that KFC and Pizza Hut were run in "flag planting mode" under PepsiCo. Potential franchisees were given tremendous leeway in structuring their operations, and there was minimal coordination across different countries. Hearl described the company at the time as an U.S. domestic company doing business overseas, rather than a multinational.

The Spin-off

In January 1997, PepsiCo announced plans to spin off its restaurant businesses as an independent, publicly traded company—Tricon Global Restaurants, Inc. (ticker symbol, YUM). Prior to the spin-off, PepsiCo disposed of several other restaurant chains, including California Pizza Kitchen, Chevys Mexican Restaurant, D'Angelo Sandwich Shop, East Side Mario's, and Hot `n Now. The spinoff, completed on October 6, 1997, initially valued Tricon's common stock at $4.6 billion.

PepsiCo also announced plans to sell its food distribution company in order to focus on its core beverage and snack food businesses and become more competitive with its soft drinks arch-rival, Coca-Cola. The retention of the snack food division, FritoLay, which led in many markets around the world and commanded high margins, was supposed to help support this strategy, not least because of opportunities to sell sodas and snack food together. And the restaurant businesses would get the attention they needed in order to grow. Some analysts disagreed with this logic, however, claiming that, by divesting the restaurant businesses, PepsiCo had "thrown away the company's best chance for growth."[12]

After the spinoff, Tricon's CEO, Andrall Pearson, and its President, David Novak, retained, in many respects, the pre-spinoff organizational structure (see **Exhibit 8**), but outlined a series of new goals for the company (see **Exhibit 9**). KFC, Pizza Hut, and Taco Bell would continue to run their own operations domestically, but Tricon would make more attempts to achieve economies across the three brands by setting up combo units, launching multibrand promotions, creating a unified food service purchasing cooperative (with U.S. franchisees), and leveraging general and administrative expenses (approximately 10% of company revenues) across them. Economies were still expected from such sharing at the scales at which the Tricon chains operated. And company ownership of the Tricon system was supposed to be reduced from 38% in 1997 to 20-25% in the long run by selling company-owned restaurants to franchisees, relying on franchisees for the bulk of system expansion, and shutting down company-owned restaurants with marginal economics that could not be refranchised. By the end of 1998, company-ownership had been reduced to 32% of the units in the Tricon system.

While the three domestic operating companies were kept separate, their international operations were combined into a separate operating company known as Tricon Restaurants International (TRI). In 1998, TRI's system-wide sales (including franchisees' revenues) were $6.7 billion (32% of the Tricon total, but down 5% from the previous year), its company revenues $2 billion (24% of the total, and down 16% from the previous year as a result of the Asian crisis and refranchising). Its operating profits amounted to $191 million (21% of the total, and up 11% from the previous year). At the end of 1998, the TRI system encompassed 9,336 units (approximately 35% of which were operated by the company or by joint ventures), up 178 from the end of 1997, and its capital expenditures for the year totaled $161 million (down 13% from the previous year). TRI aimed to grow at 20% per year. Bassi professed optimism about meeting this target: "I'm very optimistic about our ability to go global largely based on McDonald's experience."

TRI was organized into 17 separate geographic business units that corresponded to either large countries or regional agglomerations of smaller operations. See **Exhibit 10** for additional geographic information. Four of the largest units (Greater China, Mexico, Canada, and the United Kingdom) reported directly to TRI President Peter Bassi, with TRI EVP and General Manager Peter Hearl taking responsibility for the rest. In addition, senior vice-presidents assumed worldwide responsibility for each of the functional areas (Human Resources, Marketing, Finance, Development, Operations, R&D and Quality Assurance, and Legal) and also reported to Bassi. Functional area heads in each geography reported not only to the general manager of the business in question, but also to their respective senior vice-presidents in Dallas. Bassi and his team had put in place eight "how we work together" principles to stitch together the resultant matrix: customer purpose, belief in people, recognition, coaching and support, accountability, positive energy, and teamwork.

In 1998,TRI decided to concentrate its equity investments in the handful of countries that either generated significant profits, or had the potential to do so. (Roughly two-thirds of TRI's sales were accounted for by just seven countries, and their share of international operating profits was thought to be even higher). The goal was to reduce the number of primary equity markets incrementally from 27 in 1998 to 16 by the end of 1999 and, ultimately, to nine or ten. With a smaller number of core markets reporting directly to Bassi and Hearl in Dallas, the need for a regional infrastructure might be overcome. Of course, equity ownership would still be emphasized in the course of market entry as a way of giving franchisees examples to follow. The remaining 90+ markets would be operated by franchisees. **Exhibit 11** assembles some data about TRI's "top 20" markets. In addition, existing human resource capabilities were fundamental in Bassi's decisions about whether to retain significant equity interests in a country or not.

The focus on a manageable set of countries was supposed to help stitch together a multinational from what had been an ad hoc series of fiefdoms. Bassi's team had begun to emphasize the idea of "one-system" across their various business units. (See **Exhibit 12** for a composite value chain.) Bassi had articulated an 80:20 rule, in which headquarters would drive 80% of what customers saw and felt in the 10,000 restaurants outside the U.S., and local options 20%. Bassi thought that the balance at McDonald's was more like 95:5. Hearl added that the transition of the past two years had been difficult for both the field managers and the franchisees. People didn't want to change just to accommodate the new TRI when the old system had been successful for them.

Operations

The cornerstone of operational improvement at Tricon was a program called CHAMPS, which stood for Cleanliness, Hospitality, Accuracy, Maintenance, Product Quality, and Speed of Service. CHAMPS began as a simple quality control check, but quickly developed into the standard for a common operating platform among all franchisees, whether U.S. or international. It focused on defining and measuring excellence, training and supporting employees, and recognizing and rewarding those who achieved excellence. An important component of CHAMPS was the mystery shopper program, which began in 1996, but took two years to gather steam. A "mystery guest," who simulated a customer visiting a restaurant, evaluated how well the restaurant delivered its core products. Mark Seals, senior vice-president for operations, explained:

> The biggest barrier was creating a common mystery guest form, which the guest had to fill out, that everyone would agree to. For example, we had debates about whether or not it made sense to evaluate whether the server made eye contact and smiled. But the Asians objected, saying that smiling doesn't mean hospitality, and we don't make eye contact. So we ended up with wording which could be interpreted differently in different situations, but which captured the core idea: 'Were you greeted in a friendly manner with appropriate eye contact?'

The mystery shopper program was accompanied by a monthly CHAMPS excellence review, a back-of-house and front-of-house detailed self-administered audit done by each restaurant manager.

CHAMPS also covered the creation of a standard library of operating manuals to replace the assortment of old, photocopied manuals from one country that might have guided operations in another. This four-volume set (one each for management, service, product, and equipment) was created first in Dallas and then amended with input from managers across the world. Customizing the manuals and translating them into more than a hundred local languages was a gargantuan task. Menu and ingredient differences posed particular challenges. For example, some countries used frozen dough, while others used pre-mixed dough to which they had to add a certain amount of water at a particular temperature, and still others used yeast additives to condition the dough, etc.

Allowances also had to be made for taste differences. Thus, while the core menu items were similar, there were variations in the form they took. For example, the "chicken-on-the-bone" product varied from country to country. Several Asian countries, for example, developed a hotter and spicier version. Countries like Malaysia, which preferred crispier chicken, had to adapt the standard manual's prescribed "heat-pressure" variations to suit this need. To accommodate these different tastes, headquarters in Dallas established the "gold standard" for every core item and insisted that variations from this standard be justified through rigorous statistical testing. However, policing the standard was not always easy.

Seals' other major responsibilities as the SVP in charge of operations concerned procurement and inbound logistics. Availability, economics of shipping, and regulatory differences dictated procurement patterns. Chicken and produce, for example, were purchased locally for freshness and because of regulatory barriers to transporting live birds across national borders. Cheese, in contrast, could be purchased globally. Packaging materials, which were vital to the take-out business, were generally sourced locally though the amounts needed varied drastically from country to country, depending, for instance, on the amount of off-premise business.

Marketing

Before the spin-off, there had been a lack of standardization and shared best practices between the brands, or even regionally within a brand. To ensure that the brand communicated the same message throughout TRI's worldwide operations, the marketing group in Dallas set standards and determined best practices. The starting point of any brand was the brand "white paper." Bill Cobb, senior vice-president for marketing, explained:

> We try to get to the essence of KFC, Pizza Hut, and Taco Bell, from the way the building looks to the pricing approach to the menu. Then we set gold standards on products from the white paper. Everyone, of course, feels that they have local conditions that justify exemption, but we try to hold very firmly to the testing protocol.

Cobb believed that KFC had the image of a direct competitor to McDonald's across the world: like McDonald's, it offered quick service, emphasized kids' playgrounds, and even had a kids' mascot called "Chicky." Pizza Hut's image was that of a pizza *restaurant* that served "the best pizzas under one roof," while staying away from the "slice" business. Unlike competitors such as Papa John's in the U.S. and Telepizza in Spain which were mostly off-premise, Pizza Hut emphasized on-premise eating in addition to the "delta" business ("del" for delivery, and "ta" for take-away).

Getting to worldwide brand uniformity to adequately communicate these images, however, was a difficult task. Other than music and sports, it was hard to find themes that struck a genuinely global chord. As a result, Tricon's previous attempts, and PepsiCo's before that, to come up with global advertising campaigns had failed. Animated cartoon characters, such as the "animated colonel" were the best prospect since they could be used in different countries with voice-overs although even here, local content requirements sometimes limited this strategy. In addition, the quality of advertising agencies around the world varied greatly, even those affiliated with global advertising houses. Furthermore, it was still hard to buy media globally. Tricon pooled advertising budgets in the Middle East, where satellite TV was popular, but this was more the exception than the rule. Generally, local budgets supported local marketing campaigns. Thematic advertising campaigns lent themselves to broader geographies, but, for most promotional ads, it was too difficult to coordinate marketing schedules across countries. Also, the reality of the asset base was quite different from the vision implied by a uniform brand image. Cobb could tell how old a restaurant was simply by looking at its oven. Finally and perhaps most importantly, global advertising was complicated by the need to communicate an experience—which could vary greatly, depending on market—instead of just information about a product. As Bassi put it, "Even if you can globalize a product, it is very difficult to globalize an experience."

Cobb paid significant attention to facilitating the sharing of best practices. Formal mechanisms in place included a quarterly brand board meeting attended by all marketing managers worldwide—"back in the kitchen, trying to figure out how to make stew," as Cobb described the process. In addition, the franchise advisory council met three times a year to discuss franchising issues, including marketing. And perhaps most important was personal contact: "We parachute into various countries and get marketing updates. Two days in a country gives you a very good feel for how they approach their marketing strategy."

Organizationally, each of Tricon's 17 geographic business units had a marketing manager who reported to the unit general manager. The marketing manager of a unit of company-owned stores would control everything from media placement and the local ad agency to point-of-sale marketing and menu offerings. In markets with a mix of company-owned and franchised units, marketing was undertaken cooperatively, with both franchisees and the company contributing to the general fund. A committee decided how to spend the fund, and the marketing manager would lead it in collaboration with and subject to the approval of franchisees. "Franchisees improve things," said one senior vice-president. "We don't generally have fist fights with them." In units that were 100% franchised, the marketing manager played a consulting role.

"The nature of our business is 29,000 factories around the world making our product with unskilled labor. Marketing is doubly important because it is controllable," explained Cobb.

Human Resources

Senior Vice-President for Human Resources Dave Pace tried to define what it meant to work at TRI. Like Tricon, TRI subscribed, first and foremost, to a restaurant-focused culture, which meant that the head office and any regional infrastructure were to be seen as restaurant support centers, and the restaurant general manager had the most important role in the system. Pace described the barriers to the creation of this culture within the four walls of the individual restaurant, as well as across the restaurant system. "We had so many fiefdoms in the field. We had to figure out how to break these up." Regional and local managers were moved around on the theory that this allowed them to discard historical baggage and sign on to the new program being developed.

Second, Tricon emphasized ownership and recognition to a greater extent than its arch-rival, McDonald's, encouraging even middle management to own company stock. David Novak, currently Tricon President, had begun to emphasize recognition while he was President of KFC, making it a practice of giving rubber chicken awards in recognition of exceptional performance. Despite many predictions that local cultures in places like the U.K. and Asia would reject the seemingly worthless award, the recognition culture quickly took hold. "People are so appreciative of getting recognition," explained Pace. "As long as it's sincere, people just want to be told 'thank you.'" Other countries came up with their own awards—the Flying Pig award in Australia recognized those who had found a way to make pigs fly! An initially reluctant managing director in China later created his own Golden Dragon award, with similarly positive results.

Pace spent much of his time wrestling with recruiting and turnover in every country. He commented that developing countries generally had lower turnover than in the U.S., where it could approach 300% per annum for some chains, implying a cost of $800-900 per job. TRI had also found that keeping a restaurant manager in place for more than one year greatly increased restaurant profitability. However, with explosive growth, as in China, restaurant managers had to be moved frequently to help start up new restaurants. Pace commented that "we've been fairly successful in growing a pipeline of talent in each market." Of 15,000 Tricon employees in China, all but 30 were Chinese nationals, and TRI had one of the most respected management teams in China. Generally, management positions in each country tended to be filled from within the country. TRI succeeded in filling its positions from within its ranks about 80-90% of the time and otherwise looked at related industries in the same country. This was in contrast to McDonald's, which had placed an extreme emphasis on growing executives from within, with operations often serving as the steppingstone to leadership positions.

The emphasis on local management depth made it more difficult to move talent across borders. Most cross-border managerial mobility was limited to the highest levels of management. There were exceptions, such as a cadre of managers who moved from Singapore to Sydney to Hong Kong, a cadre who moved between Latin America and Spain, and a small handful of U.S.-born career expatriates who had been outside the U.S. for very long time periods. Overall, however, there were only 110-120 expatriates within the organization, of whom perhaps 100 were U.S. nationals. Expatriates typically cost three to four times as much as locals. A senior executive commented on some of the other constraints:

> You can't take someone who has success in Eastern Europe and put them in South America. You have to be aware of cultural background and financial realities. [We look at] someone's desire to live in a different part of the world—whether the person has proper cultural, linguistic, economic, historic appreciation of where they are going. What is the chance of success in the business environment where person is going? Is it complete startup from zero, or is it a failed situation, or is it a strong business which needs to be grown? Some people want turnaround situations or startup opportunities, while others are more risk averse.

Compensation and quality of life challenges further complicated cross-border mobility. Tricon followed the practice of being in the 75th percentile of compensation within each country. "We try to make the base salary and options consistent across countries, but what changes is the living allowance." In a move between London and the U.S., the expatriate could expect a similar life style. However, managers heading from, say, the U.S. to Sao Paulo or Mexico City or Shanghai had a more difficult time recreating the lifestyle they led in the advanced economies.

Finance

Chief Financial Officer David Deno spent the majority of his time deciding how to allocate funds across the myriad demands on them.

> Everyone has a passion for some part of the world and impartial decision making is tough. I try to figure out the risk-reward profile of a country. What's our history been in the country? What does competition look like? What's our capability to pull this off in terms of having the right human resources in place for particular projects? Brazil is an example where the risk-reward tradeoff seems favorable, but we have had such a bad recent history that we have decided not to make it a priority. In contrast, we have had a great history in China, and so would be willing to do different kinds of projects there.

Each country unit was evaluated formally every two years, but Deno admitted that "not a week goes by without discussion on one country or another."

Some aspects of the financing function were quite standardized across countries—the ways in which its books were maintained, the information technology systems it used for reporting purposes, and the planning cycles. Others varied by country. For example, investment models used for projects in the U.K. were quite different from those used in Mexico. Factors like foreign exchange and political volatility, as well as crime and corruption, had to be considered in countries like Mexico, and projects in Europe had to be particularly careful about the social costs of doing business.

Two of the toughest challenges were how to deal with currency fluctuations and determine country risk premia. TRI rarely hedged for foreign currency risks since the calls for which way the currency would move were just as often wrong as they were right, and hedging had sometimes proved more expensive than doing nothing. Deno also thought that there was no scientific model to deal with country risk premia.

Another striking difference between countries was the level of sophistication of their financial intermediaries, which greatly affected ways in which mergers and acquisition activity took place. The transaction costs in acquiring a company in Turkey, for instance, might be five times greater than that for a comparable transaction in the U.S., while the opportunity cost of delays and false starts might be ten times greater. It was harder to find buyers for restaurants, tougher to close deals, and tougher to deal with regulatory bodies in such countries. In places like mainland China, TRI preferred, when possible, to deal with the local arms of U.S.-based financial institutions, such as Chase Manhattan, rather than the local financial institutions.

Finally, taxation issues were quite non-standard across countries. Deno was especially concerned with how to repatriate money from a country:

> Once cash flow became positive, we have to work extensively with tax authorities to ensure a legal, yet oftentimes 'crazy,' scheme to repatriate the funds. This happens even in developed countries like Australia, where we have to jump through hoops to get money out legally.

A finance manager in each geographic business unit reported to the general manager of that unit, and had "dotted line" responsibility to Deno. "In Dallas, we take care of capital investment and treasury matters, financial management and control, tax, information technology, and acquisitions and divestitures." The finance manager could, and sometimes did, initiate discussions with Dallas about these topics. Deno spent a considerable amount of time trying to ensure that there was adequate human capital in the finance function of each major business unit.

Capital was raised primarily in the U.S., with domestic banks in different countries approached for cash management and lines of credit only. Capital for new projects was treated like high-risk or venture capital. TRI had historically found that it was stretched too thin over many countries, resulting in low profitability when there was an insufficient number of restaurants. At the restaurant level, the store would break even within a year or two, but the initial investment for real estate, operations, training, etc. took up to five years to recoup. Deno noted that TRI had a financing cost advantage in the chicken business, relative to local players, since this was a relatively capital-intensive business. He did not perceive any cost advantage in pizza, however.

Though Tricon had not contemplated a foreign listing, large franchisees sometimes were listed on their domestic stock exchanges. TRI generally did not finance franchisee businesses, but did try to arrange favorable terms for franchisees with its lending partners. TRI would sometimes try to broker the sale of a troubled franchise to another franchisee, although it typically avoided buying out the troubled operation itself. Sometimes, franchise operations in one country might be bought by a successful franchisee in a neighboring country, as was the case in central Europe recently. The associated "firefighting" generally took up a moderate amount of Deno's time. But significant firefighting had recently been necessary in Asia, in the wake of the regional financial crisis.

Franchising

According to Peter Hearl, "Our record on franchising was very spotty." We had pockets of excellence and mediocrity, so we started to galvanize ourselves around real success factors for being a good franchisor. This is still an ongoing process." Getting franchising "right" was increasingly important, since larger sections of the globe were going to be served through the franchise business model, as TRI increasingly concentrated its equity operations in fewer countries.

As part of the ongoing process, TRI had opened franchise support centers in Dallas, London, and Singapore. These centers had to deal with substantial international heterogeneity in franchising arrangement. For example, until recently, Asia had lacked a U.S.-style middle-class whose "sweat equity" could be used to support a business model involving hundreds or even thousands of individual franchisees. Combined with the fact that companies like Tricon had historically lacked systems for dealing with markets such as Asia, this led to reliance on a very small number of franchisees, each of whom often had responsibility for an entire country. These franchisees were often publicly-traded local entities that concentrated on retail businesses and sometimes had operations that crossed national boundaries.

The support that the franchisor provided internationally could also be quite different from that in the United States. Large Asian franchisees did not require as much "policing" for quality, especially if they were publicly traded. Thus, Art Rautio, regional manager for Southeast Asia and HBS graduate, said that he had built a team around the same functional lines as the large Asian franchisees, with each team member having to build relationships with counterparts in the franchisees. Furthermore, the Asian franchisees had typically been even more independent than the smaller ones in the United States, so that selling them on the new Tricon way had proven particularly challenging.

That said, Bassi still emphasized the standardization of the franchise contract around the world as a way of imposing discipline on the franchisees. The TRI franchise contract involved a per-store fee of $35,000, royalties of 6% of sales, an advertising contribution of 5-6% of sales, and a term of 10 years, with an additional ten year renewal option.

Product Development

Product development had been bundled into the "R&D and Quality Assurance" department at TRI, reflecting the fact that it was no longer enough to come up with new products: they also had to pass the gold standards. Overall, Tricon reported spending approximately $20 million per year on R&D at facilities in Louisville, Kentucky, in Dallas, Texas, and in Irvine, California. However, this figure probably did not capture all the resources and time actually spent on product development, while including some expenditures on process development.

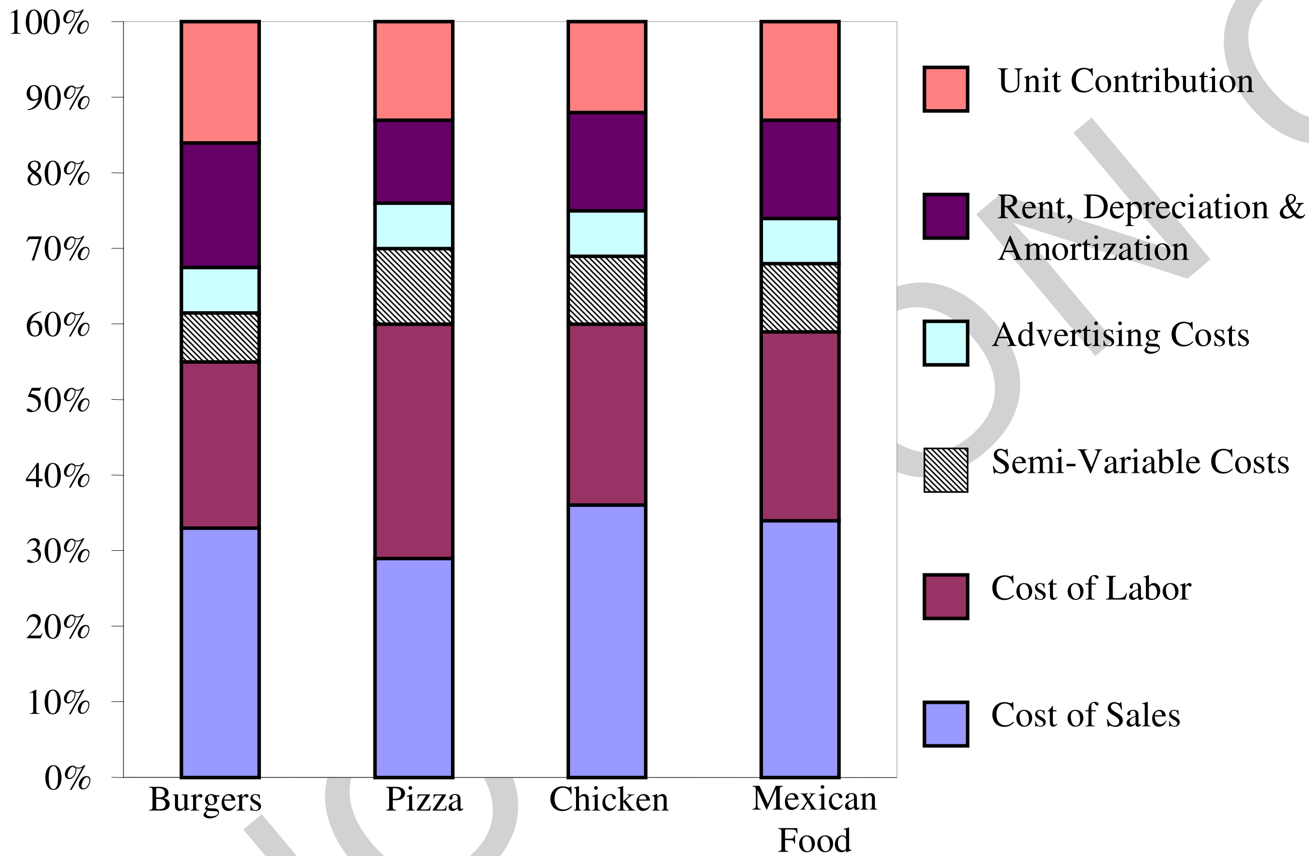
The resources that Tricon did spend on product development were earmarked mostly for the United States. Tricon believed that, unlike McDonald's, it had substantial room to grow in the United States, particularly in 4,900 locations that had a McDonald's, but only one or none of Tricon's three brands. In addition, significant expenditures on product—and process—development were required to expand into new dayparts (e.g., dinner for Taco Bell and lunch sandwiches for KFC), as well as into new channels (e.g., chicken delivery and multibrand stores). According to President David Novak, however, the existing brands were unlikely to support expansion into breakfast (even though some of Taco Bell's competitors had breakfast businesses). "We don't think the world is waiting for a breakfast pizza or a KFC breakfast. When we enter the breakfast business, which will be down the road, the likely way will be to acquire a breakfast brand."[13]

Product development outside the U.S. was comparatively limited. Country markets had some application resources to customize products for local health and safety standards, local suppliers, and customer sentiment (e.g., the backlash in Europe against genetically engineered food). In addition, TRI made some attempts to tap into franchisees' ideas about product innovations (e.g., Crispy Chicken in Malaysia), although cross-country transplantation was typically limited by the purely local appeal of innovations that beat the gold standard in a particular country (e.g., low salt content in Korea). Resources for international development and adaptation in the chicken business were particularly sought after, given its greater variation from country to country. TRI product development for KFC had been centralized in Asia due to the large Asian business and availability of technical resources. But from the perspective of Graham Allan, managing director of KFC in the U.K., this arrangement addressed only some of the product development issues that KFC faced.

Afterword

Peter Bassi, President of Tricon Restaurants International, read the Harvard Business School case study on TRI as he got into the plane to visit class the first time that the case would be taught. While he felt very confident about the international strategy that his organization had devised, he nonetheless anticipated a lively discussion.

Exhibit 1 Comparative Cost Structures for Selected Fast Food Categories



Source: Tricon Global Restaurants, Inc

Exhibit 2 Market Niches in the Fast Food Industry

Market Niche	Example
Hamburger stores	McDonald's
Chicken stores	KFC
Pizza stores	Pizza Hut
Mexican food stores	Taco Bell
Dinner houses	Olive Garden
Family restaurants	Denny's
Steak houses	Bonanza
Seafood houses	Red Lobster
Snack restaurants	Dunkin' Donuts
Cafeterias	Morrison's
In-store restaurants	K-Mart
Hotel restaurants	Hilton Hotels

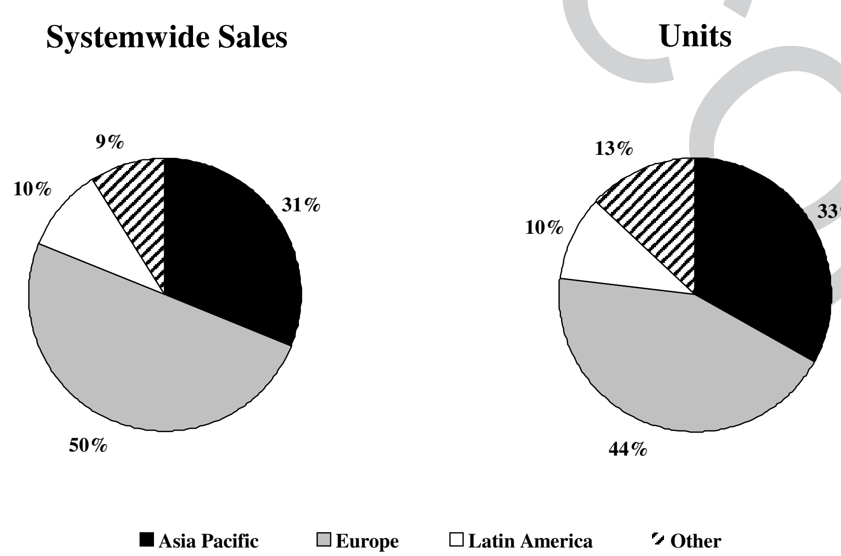
Source: Tricon Global Restaurants, Inc

Exhibit 3 McDonald's Selected Financial Data ($ millions)

	1998	1997	1996	1995
System Sales	35,979	33,638	31,812	29,914
Revenues	12,421	11,409	10,687	9,795
Operating Income	2,762	2,808	2,633	2,649
Net Income	1,550	1,643	1,573	1,427
Capital Expenditures	1,879	2,111	2,375	2,064
Total Assets	19,784	18,242	17,386	15,415
Current Liabilities	2,497	2,985	2,135	1,795
Long-term Debt	6,189	4,834	4,830	4,258
Shareholders Equity	9,465	8,852	8,718	7,861

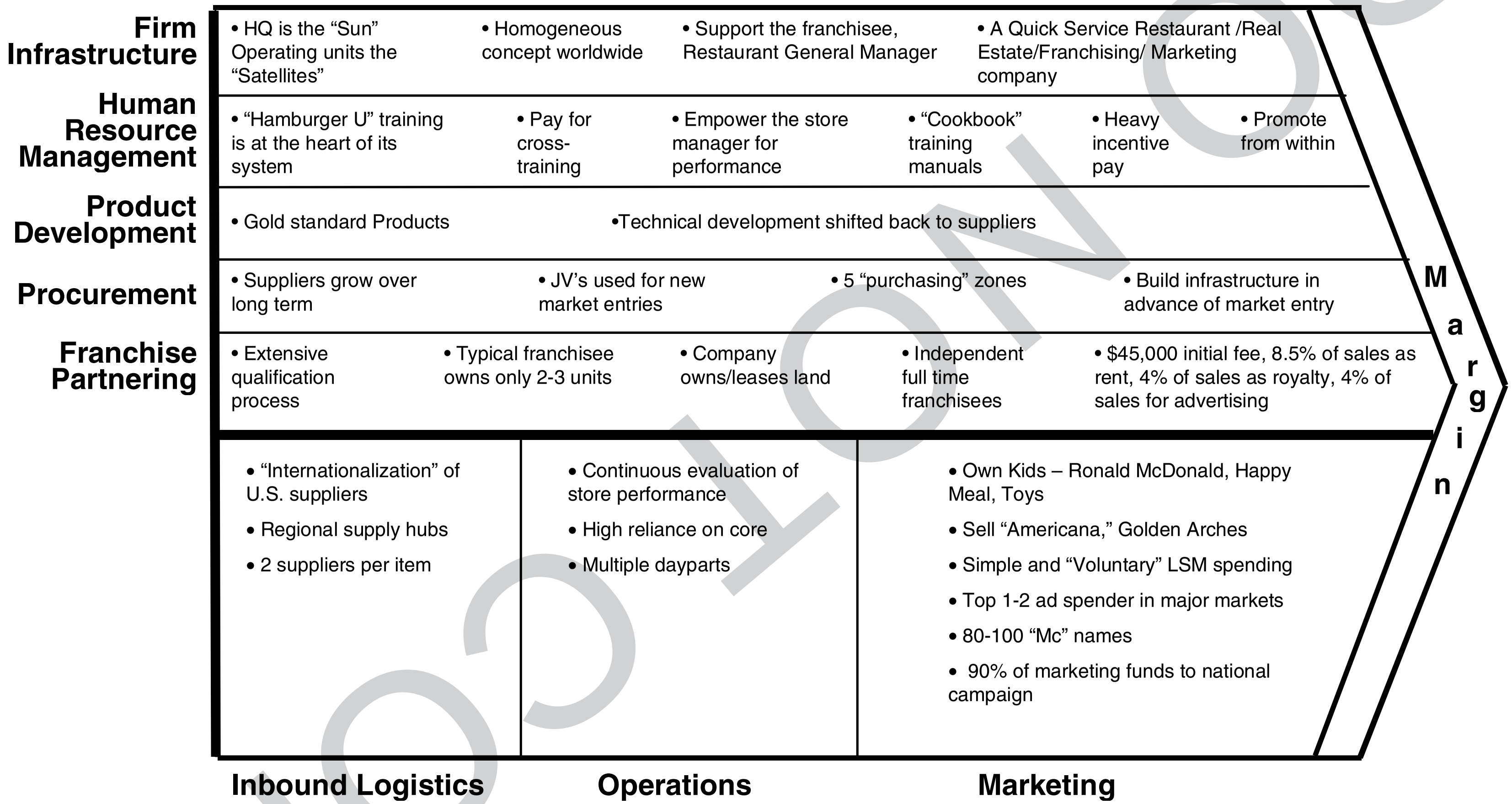
Source: Annual Reports

Exhibit 4 McDonald's International Information by Geographic Regions, 1998



Source: Annual Reports

Exhibit 5 Value Chain for McDonald's International



Source: Casewriter's analysis

Exhibit 6 Gidget

Source: Tricon Global Restaurants, Inc. 1998 Annual Report

Exhibit 7 Tricon Global Restaurants Selected Financial Data ($ millions)

	1998	1997	1996	1995
System Sales	20,620	20,465	20,280	19,700
Revenues	8,468	9,685	10,232	10,250
Operating Income	1,028	241	372	252
Net Income	445	-111	-53	-132
Capital Expenditures	460	541	620	701
Total Assets	4,531	5,114	6,520	6,908
Current Liabilities	1,473	1,582	1,416	1,478
Long-term Debt	3,436	4,551	231	260
Shareholders Equity	-1,163	-1,620	NA	NA

Exhibit 8 Tricon's Organizational Structure

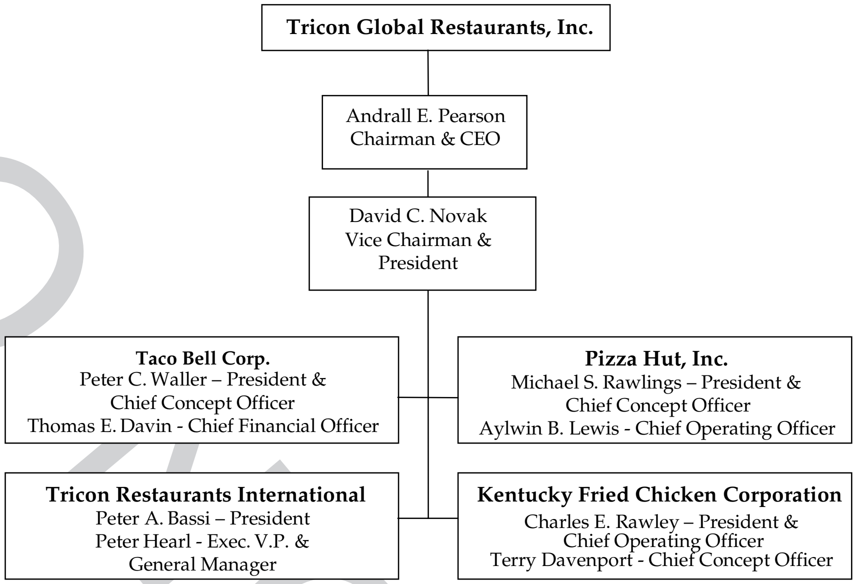


Exhibit 9

Tricon's Goals for the Future

1. Become renowned for an ownership and recognition culture that drives the best results in the industry.
2. Drive superior same store sales growth through differentiated brand positioning and innovation.
3. Improve the unit level economics enough to drive shareholder value.
4. Develop the most competitive, leveragable above-the-store cost structure in the industry.
5. Expand the system aggressively and profitably by becoming a superior franchise company.
6. Build a capital and asset structure that dramatically enhances shareholder value.

Exhibit 10 Tricon International Information by Geographic Regions, 1998

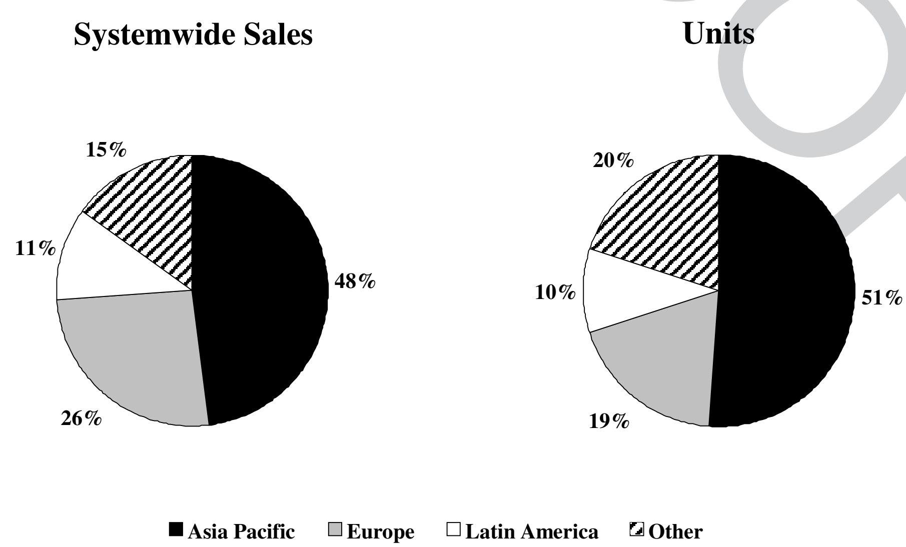


Exhibit 11 Top 20 Tricon Restaurants International Markets (plus the United States)

Country	Population (MM)	Geographic Distance[1]	Political Distance[2]	Linguistic Distance[3]	Per Capita Income PPP (USD)	Per Capita QSR Consumption (USD)	Total QSR Market Share %: McDonald's	Total QSR Market Share %: KFC	Total QSR Market Share %: Pizza Hut	Number of units: McDonald's	Number of units: KFC	Number of units: Pizza Hut	% Company Owned: KFC	% Company Owned: Pizza Hut
Puerto Rico	3.8	3453	1	1	--	317.2	15	8	7	109	69	57	100	100
Canada	30.3	2289	1	1	15,439	289.6	15	4	6	1,050	862	547	24	34
Australia	18.4	14048	2	1	13,920	211.8	34	13	10	642	445	393	46	48
New Zealand	3.6	12207	2	1	11,205	202.9	32	14	17	137	89	41	0	0
Germany	82	8391	2	2	15,229	140.2	35	1	9	850	14	150	0	49
UK	57.6	7657	2	1	15,490	124.8	28	9	8	825	384	458	37	0[4]
Japan	125.7	10418	2	2	15,554	110.5	31	10	1	2,437	1,050	220	69	0[5]
France	58.6	7948	2	2	15,756	81.3	34	1	6	629	7	129	100	0[6]
Singapore	3.4	15658	2	1	16,340	77.9	49	25	8	105	69	26	95	100
Taiwan	22	12427	2	2	--	50.2	48	18	6	233	64	85	27	0
Korea	45.9	10992	2	2	6,590	49.3	10	9	10	114	122	140	0	95
S. Africa	42.3	14667	2	1	--	30.1	5	25	1	137	350	41	5	0
Spain	39.1	7970	2	2	10,667	27.9	16	3	16	150	36	115	50	97
Malaysia	20.5	15582	2	1		21	20	55	9	110	239	64	0	0
Thailand	59.4	14531	2	2	3,162	19.1	17	47	20	61	194	104	42	0
Saudi Arabia	20	12583	2	2	--	14.1	8	13	15	27	43	71	0	0
Belgium	10.1	7966	2	2	15,579	10.3	25	--	28	60	0	72	0	52
Mexico	97.6	1496	1	2	--	7.3	24	26	12	131	157	99	80	88
China	1,221.5	11264	2	2	--	1.6	36	60	3	184	237	26	53	20
Poland	38.6	8800	2	2	5,087	25.0	35	1	16	95	4	46	0	76
U.S.	267				21,680	370.0	23	3	30	12,472	5,120	8,700	32	35

[1] From Dallas to Capital city (km)

[2] "1" indicates free trade agreement or other political linkages with the United States, "2" indicates absence of such linkages

[3] "1" indicates that English is an official court language, "2" indicates that it is not

[4] 91% of units owned through a joint venture

[5] 50% of units owned through a joint venture

[6] 90% of units owned through a joint venture

Exhibit 12 Value Chain for Tricon Restaurants International (there would be some differences to domestic)

Firm Infrastructure	• US RSC as process leaders, resource allocators	• No regional infrastructure	• Field / BMUs as operating centers	• Operate equity and franchise as one system
Human Resource Management	• "Restaurant General Manager is #1 Leader"	• YUM University to develop functional expertise	• Focus on building ownership at all levels	• Recognition culture driven deep in organization
Product Development	• Gold Standard core products		• Local R&D adapts to local preference for non-core	
Procurement	• Balance worldwide sourcing with local accessibility and cost			• Infrastructure developed to accelerate growth
Franchise Partnering	• Standardized franchise agreement	• Mixture of large (100+) and small (1) franchisees	• $35,000 initial fee, 6% of sales continuing fee, 5% of sales for advertising expenses	

	Inbound Logistics	**Operations**	**Marketing**
Pizza Hut	• Global sourcing of key ingredients (e.g., NZ cheese) • Backward integration of dough prep	• Assemble to order • Leverage scale opportunities → Call center → Ready-to-top dough • Product variety drives operating complexity	• "Best Pizzas Under One Roof, Our Place and Yours" • Distinctive Red Roof • Delivery emerging to drive accessibility
KFC	• Local sourcing • Minimal backward integration	• Assemble to forecast • Fresh chicken prepared in stores • Sandwiches drive operating complexity	• "Nobody Does Chicken Like KFC" • Well developed kids program (Chicky) • Plated meals increase value perception • Sandwiches drive 2 dayparts
Taco Bell	• "Kitchen Minus" -- Practically all items delivered ready to use • Relatively high U.S . export content	• Assemble to order • Multiple products can be made from limited number of ingredients • Low percent of combo meals • Premium on speed	• "Mexican-style Fast Food With Attitude" • Value for the money • Unique taste sensations

Margin

Endnotes

[1] Thomas Friedman, *The Lexus and the Olive Tree* (New York: Farrar Straus & Giroux, 1999), p. 235.

[2] Jeffrey L. Bradach, *Franchise Organizations* (Boston: Harvard Business School Press, 1998).

[3] Yunxing Yan, "McDonald's in Beijing: The Localization of Americana," Chapter 1, *Golden Arches East: McDonald's in East Asia*, Ed. James L. Watson (Stanford, Calif.: Stanford University Press, 1997).

[4] Steve Lohr, "Microsoft Losing Public's Affection," *International Herald Tribune*, August 3, 1999, p. 10.

[5] Information on McDonald's collected from public company reports.

[6] "A mission to buff up the golden arches," *Financial Times*, September 3, 1998.

[7] Information in this section from "Bee bites clown," *Forbes*, October 20, 1997.

[8] Some of the historical information on Pizza Hut based on "PepsiCo's Restaurants," HBS No. 794078.

[9] Some of the historical information on TelePizza based on "TelePizza," HBS No. 899080.

[10] Some of the historical information on KFC based on "PepsiCo's Restaurants," HBS No. 794078.

[11] Some of the historical information on Taco Bell based on "PepsiCo's Restaurants," HBS No. 794078.

[12] Subrata N. Chakravarty, John R. Hayes, "The pure-play syndrome," *Forbes*, October 20, 1997, p. 209.

[13] Duff McDonald, "McDonald's vs. Tricon," *Money*, August 1999, p. 49.