

YUM CHINA HOLDINGS INC

(Ticker: YUMC-N) \$47.78

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The financial model of YUMC can be found here:

[HAO-LIN/YUMC FSM and DCF.xlsx at master • linhao142857/HAO-LIN \(github.com\)](#)

Business Assessment

Yum China Holdings, Inc. is a restaurant company. The Company owns, franchises or has ownership in entities that own and operate restaurants. Its segments include KFC, Pizza Hut Casual Dining, and other segments, including Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY, Taco Bell, East Dawning, Daojia and its e-commerce business. KFC is the quick-service restaurant (QSR) brand in China. KFC operate approximately 8,100 restaurants in more than 1,600 cities across China. Pizza Hut is the casual dining restaurant (CDR) brand in China. Pizza Hut operates approximately 2,500 restaurants in over 600 cities. Huang Ji Huang is a Chinese-style casual dining franchise restaurant brand with over 600 restaurants in China and international markets. Little Sheep is a hot pot restaurant in China having over 222 units in both China and international markets. Taco Bell is a QSR brand specializing in Mexican-style food. COFFii & JOY brand features specialty hand-dripped coffee.

Market Data (C\$)	
Current Price	47.78
52-Week Range	33.55-61.29
Market Cap (\$mm)	2,005
Current Dividend	0.48
Avg Daily Trading Vol (\$mm)	1.7
Fiscal Y-E	Dec 31
Source: BBG	

Absolute Valuation

Revenue: The resurgence of COVID-19 cases has again put the Chinese restaurant sector under pressure, and several cities have returned to city-wide quarantines. Therefore, placing pressure on the company's near-term results. Given the Q2 result, I used a 2.9% revenue growth rate for the year 2022. Upon a return of international tourism/traffic, YUMC should be well-positioned to leverage its high-margin, expanded system sales growth. I expect a similar revenue growth as the year 2021 (16.2%) for F2023.

Gross margin: Despite a lower margin during 2021 (about 21.5%), I expected its margin will stay at the same level during 2022, and gradually convert back to its prior COVID level (about 24%).

SG&A is projected as a percentage of revenue, and **D&A** expense grows with PP&E. **Tax rate** was the average of the past 3 years.

Based on the above analysis, YUMC is valued at \$48.56 under FCFF methods.

USmm, except per share	F2022E	F2023E
KFC	7411.28	8841.87
Pizza Hut	2112.05	2394.77
Other Brands	596.32	654.72
Total Revenue	10138.5	11776.83
EPS	1.08	1.88
Source: BBG, Analyst estimates		

Relative Valuation

YUMC is currently trading at 44.08x forecast EPS. This compares with the average of its restaurant peers of 26.89x. Given the forecast EPS, the target price of YUMC is \$47.61. Similarly, the firm's EV/EBITDA ratio gives us a target price of \$49.69. I see limited upside given the near-term headwinds that present risk to the execution of Zero-Covid policy.

I assigned equal weights to absolute and relative valuation. This gives the target share price of YUMC is at **\$48.62**.

Valuations	F2022E
Absolute	
FCFF	48.56
Relative	
P/E	47.61
EV/EBITDA	49.69
Target Price	48.62
Source: Analyst estimates	

	EV/EBITDA	P/E
RESTAURANT BRANDS INTERN	15.62	50.32
MCDONALD'S CORP	18.67	23.75
WENDY'S CO/THE	15.61	23.87
YUM! BRANDS INC	18.23	25.32
JACK IN THE BOX INC	15.62	13.55
DOMINO'S PIZZA INC	19.07	24.14
STARBUCKS CORP	19.84	27.29
Peer Average	17.52	26.89
YUM China	14.17	44.08
Source: BBG, Analyst estimates		

In my opinion, the risk/reward profile of YUMC shares has improved since the company reported in early-November 2021. The current valuation and potential growth opportunity support my **HOLD** recommendation.

The key risks to our target price (and to the firm) include the following: a deterioration in the general health; success in expanding its business in new and existing markets; unseasonable weather; foreign currency; and operational disruptions from COVID-19.

ESG factors and/or issues

Environment: Environmental issues such as climate change, deforestation, and pollution are growing challenges associated with social development. As the largest restaurant company in China, Yum China needs to focus on climate action, water conservation, green building, and waste management.

Food: Customers and investors have higher expectations of disclosures and information transparency for food quality, safety, and nutrition.

People: Fulfilling the needs of key stakeholders, including its employees, customers, suppliers and the general public.

Appendix

Financial Statement Modeling

INCOME STATEMENT								
Fiscal year	2019A	2020A	2021A	2022P	2023P	2024P	2025P	2026P
Fiscal year end date	12-31-19	12-31-20	12-31-21	12-31-22	12-31-23	12-31-24	12-31-25	12-31-26
Revenue	8,776.0	8,263.0	9,853.0	10,138.7	11,781.2	12,370.3	12,741.4	12,996.2
Cost of sales (enter as -)	(6,659.0)	(6,298.0)	(7,734.0)	(7,958.9)	(9,189.3)	(9,525.1)	(9,683.4)	(9,877.1)
Gross Profit	2,117.0	1,965.0	2,119.0	2,179.8	2,591.9	2,845.2	3,057.9	3,119.1
Other operating cost (enter as -)	(729.0)	(525.0)	(169.0)	(202.8)	(66.4)	(78.1)	(89.9)	(101.7)
Selling, general & administrative (enter as -)	(487.0)	(479.0)	(564.0)	(557.6)	(648.0)	(680.4)	(700.8)	(714.8)
Operating profit (EBIT)	901.0	961.0	1,386.0	1,419.4	1,877.5	2,086.7	2,267.3	2,302.6
Interest income, net	39.0	43.0	60.0					
Other expense, net (enter as -)	63.0	104.0	(54.0)					
Net interest, finance and other costs	102.0	147.0	6.0	100.0	100.0	100.0	100.0	100.0
Pretax profit	1,003.0	1,108.0	1,392.0	1,519.4	1,977.5	2,186.7	2,367.3	2,402.6
Taxes (enter expense as -)	(290.0)	(324.0)	(402.0)	(440.8)	(573.7)	(634.4)	(686.8)	(697.0)
Net income	713.0	784.0	990.0	1,078.6	1,403.8	1,552.3	1,680.5	1,705.6

BALANCE SHEET								
Fiscal year	2019A	2020A	2021A	2022P	2023P	2024P	2025P	2026P
Fiscal year end date	12-31-19	12-31-20	12-31-21	12-31-22	12-31-23	12-31-24	12-31-25	12-31-26
Cash & equivalents, ST and LT marketable securities	4,263.0	3,996.0	4,105.4	4,679.7	4,898.1	4,928.4	4,711.1	
Accounts receivable (Trade receivables)	99.0	67.0	68.9	80.1	84.1	88.6	88.4	
Inventories	398.0	432.0	444.6	513.3	532.0	540.9	551.7	
Prepaid expenses and other current assets	176.0	221.0	227.4	264.2	277.5	285.8	291.5	
Operating lease right-of-use assets	2,164.0	2,612.0	3,173.6	3,871.8	4,762.3	5,905.2	7,322.5	
Deferred income taxes	98.0	106.0	109.1	126.7	133.1	137.1	139.8	
Property, plant & equipment, net	1,765.0	2,251.0	2,751.1	3,320.2	3,905.2	4,494.8	5,083.0	
Intangible assets, net	246.0	272.0	279.9	325.2	341.5	351.7	358.8	
Investments in unconsolidated affiliates	85.0	292.0	300.5	349.1	366.6	377.6	385.2	
Goodwill	832.0	2,142.0	2,142.0	2,142.0	2,142.0	2,142.0	2,142.0	
Other non current assets (other long-term assets)	749.0	832.0	856.1	994.8	1,044.6	1,075.9	1,097.4	
Total assets	10,875.0	13,223.0	14,458.5	16,667.3	18,487.0	20,326.0	22,171.3	
Accounts payable and accrued liabilities	1,995.0	2,332.0	2,399.8	2,770.8	2,872.1	2,919.8	2,978.2	
Income taxes payable	72.0	51.0	52.5	61.0	64.0	66.0	67.3	
Total current liabilities	2,067.0	2,383.0	2,452.3	2,831.8	2,936.1	2,985.8	3,045.5	
Non-current operating lease liabilities	1,915.0	2,286.0	2,352.3	2,733.4	2,870.0	2,956.1	3,015.3	
Non-current finance Lease Liabilities	28.0	40.0	40.0	40.0	40.0	40.0	40.0	
Deferred income taxes liabilities	227.0	425.0	425.0	425.0	425.0	425.0	425.0	
Other non current liabilities	167.0	167.0	171.8	199.7	209.7	216.0	220.3	
Total liabilities	4,404.0	5,301.0	5,401.4	6,189.9	6,440.8	6,582.9	6,706.0	
Common stock	4.0	4.0	4.0	4.0	4.0	4.0	4.0	
Treasury stock	(728.0)	(803.0)	(763.0)	(763.0)	(763.0)	(763.0)	(763.0)	
Additional paid-in capital	4,658.0	4,695.0	4,695.0	4,695.0	4,695.0	4,695.0	4,695.0	
Retained earnings	2,105.0	2,892.0	3,987.1	5,407.4	6,976.2	8,673.2	10,395.3	
Other comprehensive income	167.0	268.0	268.0	268.0	268.0	268.0	268.0	
Noncontrolling interests	265.0	866.0	866.0	866.0	866.0	866.0	866.0	
Total equity	6,471.0	7,922.0	9,057.1	10,477.4	12,046.2	13,743.2	15,465.3	
Balance check	0.0	0.0	0.0	0.0	0.0	0.0	0.0	

CASH FLOW STATEMENT								
Fiscal year				2022P	2023P	2024P	2025P	2026P
Fiscal year end date				12-31-22	12-31-23	12-31-24	12-31-25	12-31-26
Net income				1,078.6	1,403.8	1,552.3	1,680.5	1,705.6
Depreciation and amortization				531.0	629.0	673.0	706.1	733.5
Stock based compensation				0.0	0.0	0.0	0.0	0.0
Decreases / (Increases) in working capital assets				(20.9)	(116.7)	(36.0)	(19.7)	(18.3)
Increases / (Decreases) in working capital liabilities				69.3	379.5	104.3	49.7	59.7
Other non current assets				(24.1)	(138.7)	(49.7)	(31.3)	(21.5)
Other non current liabilities				4.8	27.8	10.0	6.3	4.3
Cash from operating activities				1,638.7	2,184.7	2,253.9	2,391.5	2,463.3
Capital expenditures				(1,031.1)	(1,198.1)	(1,258.0)	(1,295.7)	(1,321.6)
Other assets				(581.0)	(809.9)	(930.6)	(1,168.2)	(1,434.6)
Cash from investing activities				(1,612.1)	(2,008.0)	(2,188.6)	(2,463.9)	(2,756.2)
Long term debt				66	381	137	86	59
Exercise of stock options				3.7	3.7	3.7	3.7	3.7
New shares issued (repurchase)				12.8	12.8	12.8	12.8	12.8
Cash from financing activities				82.8	397.6	153.2	102.6	75.6
Net change in cash during period				109	574	218	30	-217

Sensitivity analysis for the first forecast year net income

Revenue growth rate						
	\$1,079	9.0%	7.0%	5.0%	3.0%	1.0%
	24.0%	1,329	1,306	1,283	1,260	1,237
Gross	23.0%	1,253	1,231	1,209	1,188	1,166
Profit	22.0%	1,176	1,156	1,136	1,116	1,095
Margin:	21.0%	1,100	1,081	1,062	1,044	1,025
	20.0%	1,024	1,007	989	972	954
	19.0%	948	932	916	899	883
Revenue growth rate						
	\$1,079	9.0%	7.0%	5.0%	3.0%	1.0%
	7.0%	1,024	1,007	989	972	954
SG&A %	6.5%	1,062	1,044	1,026	1,008	989
of sales:	6.0%	1,100	1,081	1,062	1,044	1,025
	5.5%	1,138	1,119	1,099	1,080	1,060
	5.0%	1,176	1,156	1,136	1,116	1,095
	4.5%	1,215	1,194	1,173	1,152	1,131