

Yum China (9987 HK)

Headwinds likely to stay after a weak 4Q21

Following a devastating 4Q21, we expect the headwinds (e.g. COVID-19 outbreaks, raw material and wages inflation) are likely to stay in 1Q22E. Hence we maintain HOLD and cut TP to HK\$ 343.43, based on 25x FY22E P/E (at par with industry average, down from 27x because of sector de-rating).

- 4Q21 results missed.** For FY21, YUMC sales grew by 19% YoY to RMB 9.85bn, inline with BBG/ CMBI est., while adjusted net profit (mainly for the non-cash gains from Hangzhou Catering and other mark-to-market investments like meituan) dropped by 15% YoY to RMB 525mn, missed BBG/ CMBI est. by 20%/ 25%. For 4Q21, adjusted net profit fell by 93% to RMB 11mn, missed BBG/ CMBI est. by 91%/ 94%. This is a negative surprise to us even though we already have a bearish view and HOLD rating. We attributed this to: 1) SSS decline and operating leverage, 2) weak GP margin, due to rising commodity prices and greater promotions and 3) staff costs inflations due to increases in min. wages. Restaurant level margin for KFC/ Pizza Hut fell to 8.6%/ 5.9%, far below its long-term blended margin target of ~17%.
- Pizza Hut, KFC dine-in and other off-premises sales took the hit.** 4Q21 SSS dropped by 11%, even worse than 7% drop in 3Q21 due to macro headwinds, despite outperforming Starbucks's 14% and 7% decline. Noted that KFC delivery sales still grew by 33% (vs 30% in 3Q21), but all other (Pizza Hut delivery, YUMC's dine-in and other off-premises) sales were weakening.
- Remain cautious about 1Q22E.** Management highlighted a sequential improvement in Jan 2022 (~500 stores closed temporarily), but sales should still be falling during CNY and we are suspecting a seasonal weakness in Feb 2022 due to an early CNY.
- Cost pressure is still on in FY22E.** Management believe cost inflation can still be from all fronts and expect double digits/ at least MSD (likely double-digits)/ MSD- HSD increases for energy/ commodity costs/ average wages in FY22E. Given our rather flattish SSSG assumptions in FY22E, operating leverage could still be in place in 1H22E.
- Targeting 1,000-1,200 net openings in FY22E.** Gross openings was 1,806 in FY21, beating guidance of ~1,700. Management is now guiding net openings of 1,000- 1,200 in FY22E, only similar to 1,282 in last year. We now forecast 840/ 240/ 45/ 35 net new stores for KFC/ Pizza Hut/ Lavazza/ others.
- Maintain HOLD and cut TP to HK\$ 343.43,** based on 25x FY22E P/E (revised down from 27x to factor in sector de-rating). We revised down FY22E/ 23E net profit by 15%/ 19%, to factor in: 1) lower SSSG, 2) lower GP and OP margins, but 3) slower store expansion. YUMC is trading at 25x FY22E P/E, not too attractive, given an 11% EBIT CAGR in FY20-24E.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (USD mn)	8,263	9,853	11,269	12,743	14,128
YoY growth (%)	(5.8)	19.2	14.4	13.1	10.9
Net income (USD mn)	784	990	781	960	1,147
Diluted EPS (USD)	1.89	2.26	1.77	2.17	2.58
YoY growth (%)	4.5	19.6	(21.6)	22.3	18.8
Consensus EPS (USD)	n/a	n/a	2.06	2.50	3.11
P/E (x)	23.7	19.8	25.3	20.7	17.4
P/B (x)	2.9	2.4	2.2	2.1	1.9
Yield (%)	0.5	1.1	1.0	1.2	1.4
ROE (%)	16.3	13.8	9.5	10.8	11.7
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIS estimates

HOLD (Maintain)

Target Price	HK\$343.43
(Previous TP)	HK\$438.86)
Up/Downside	-1.1%
Current Price	HK\$347.40

China Catering Sector

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Stock Data

Mkt Cap (HK\$ mn)	148,731
Avg 3 mths t/o (HK\$ mn)	43.01
52w High/Low (HK\$)	544.00/ 341.20
Total Issued Shares (mn)	428.1

Source: Bloomberg

Shareholding Structure

Primavera Capital	5.7%
BlackRock	7.1%
Invesco	9.0%
Management	0.2%
Free Float	78.0%

Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-5.6%	-8.9%
3-mth	-19.6%	-18.2%
6-mth	-24.4%	-18.7%
12-mth	-19.7%	-3.3%

Source: Bloomberg

12-mth Price Performance

Source: Bloomberg

Auditor: KPMG



Related Reports

- Yum China (9987 HK, HOLD) – Headwinds linger despite faster expansion – 29 Oct 2021
- Yum China (9987 HK, BUY) – Guidance was in-line but coffee will accelerate – 24 Sep 2021
- Yum China (9987 HK, BUY) – Another hit taken, but stay mid-term positive – 16 Sep 2021

Earnings revision

Figure 1: Earnings revision

US\$ mn	New			Old			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	11,269	12,743	14,128	11,545	13,258	14,714	-2.4%	-3.9%	-4.0%
Gross profit	8,004	9,079	10,075	8,210	9,456	10,506	-2.5%	-4.0%	-4.1%
Operating Profit	996	1,224	1,467	1,208	1,544	1,820	-17.6%	-20.7%	-19.4%
Net profit	781	960	1,147	924	1,180	1,388	-15.5%	-18.6%	-17.3%
EPS (US\$ cents)	1.773	2.169	2.576	2.098	2.665	3.117	-15.5%	-18.6%	-17.3%
Gross margin	71.0%	71.2%	71.3%	71.1%	71.3%	71.4%	-0.1ppt	-0.1ppt	-0.1ppt
EBIT margin	8.8%	9.6%	10.4%	10.5%	11.6%	12.4%	-1.6ppt	-2ppt	-2ppt
Net profit att. margin	6.9%	7.5%	8.1%	8.0%	8.9%	9.4%	-1.1ppt	-1.4ppt	-1.3ppt

Source: Company data, CMBIS estimates

Figure 2: CMBIS estimates vs consensus

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Revenue	11,269	12,743	14,128	11,289	12,697	13,892	-0.2%	0.4%	1.7%
Gross profit	8,004	9,079	10,075	8,077	9,130	9,869	-0.9%	-0.6%	2.1%
Operating Profit	996	1,224	1,467	1,189	1,428	1,783	-16.2%	-14.3%	-17.7%
Net profit	781	960	1,147	882	1,061	1,360	-11.5%	-9.5%	-15.7%
EPS (US\$ cents)	1.773	2.169	2.576	2.063	2.499	3.110	-14.0%	-13.2%	-17.2%
Gross Margin	71.0%	71.2%	71.3%	71.6%	71.9%	71.0%	-0.5ppt	-0.7ppt	0.3ppt
Operating Margin	8.8%	9.6%	10.4%	10.5%	11.2%	12.8%	-1.7ppt	-1.6ppt	-2.5ppt
Net Margin	6.9%	7.5%	8.1%	7.8%	8.4%	9.8%	-0.9ppt	-0.8ppt	-1.7ppt

Source: Company data, CMBIS estimates

Assumptions

Figure 3: CMBIS' assumptions

Major assumptions	FY18A	FY19A	FY20A	FY21E	FY22E	FY23E
Sales by segment (RMB mn)						
KFC - dine in sales	4,152	4,855	5,379	5,840	6,176	4,152
KFC - delivery sales	1,623	2,148	2,685	3,303	3,997	1,623
PH - dine in sales	1,146	1,340	1,444	1,620	1,796	1,146
PH- delivery sales	642	769	923	1,061	1,167	642
Others	701	741	838	918	991	701
Total	8,263	9,853	11,269	12,743	14,128	8,263
Sales by segment growth (%)						
KFC - dine in sales	-15.5%	16.9%	10.8%	8.6%	5.8%	-15.5%
KFC - delivery sales	43.7%	32.4%	25.0%	23.0%	21.0%	43.7%
PH - dine in sales	-25.0%	17.0%	7.8%	12.2%	10.9%	-25.0%
PH- delivery sales	21.7%	19.8%	20.0%	15.0%	10.0%	21.7%
Others	2.8%	5.7%	13.1%	9.6%	7.9%	2.8%
Total	-5.8%	19.2%	14.4%	13.1%	10.9%	-5.8%
Sales network by brand						
KFC	7,166	8,168	9,008	9,848	10,488	7,166
Pizza Hut	2,355	2,590	2,830	3,070	3,310	2,355
Others	985	1,030	1,110	1,190	1,270	985
Total	10,506	11,788	12,948	14,108	15,068	10,506
Restaurant profit margin by brand						
KFC	15.8%	14.5%	14.1%	14.9%	15.4%	15.8%
Pizza hut	10.5%	10.6%	12.2%	13.3%	14.3%	10.5%
Others	-0.4%	-1.3%	-0.2%	-0.2%	0.4%	-0.4%
Total	14.8%	13.7%	12.6%	13.5%	14.1%	14.8%
Costs breakdown						
Food and paper/ sales	28.3%	28.5%	29.0%	28.8%	28.7%	28.3%
Payroll and employee benefits/ sales	20.9%	22.9%	23.5%	23.4%	23.2%	20.9%
Rental and other operating expenses/ sales	26.9%	27.0%	26.3%	26.2%	26.2%	26.9%
G & A expenses/ sales	5.8%	5.7%	5.2%	5.2%	5.0%	5.8%
Franchisees expenses/ sales	7.7%	6.6%	6.2%	5.8%	5.5%	7.7%
Effective tax rate	26.6%	26.5%	25.5%	25.0%	25.0%	26.6%
NP att. margin	9.5%	10.0%	6.9%	7.5%	8.1%	9.5%
NP att. growth (%)	10.0%	26.3%	-21.2%	23.0%	19.4%	10.0%

Source: Company data, CMBIS estimates

Valuation

Figure 4: Peers valuation table

Company	Ticker	Rating	12m TP (LC)	Price (LC)	Up/Down-side	Mkt. Cap (HK\$m)	Year End	P/E (x)		P/B (x)		ROE (%)	3yrs PEG (x)	Yield (%)	
								FY1E	FY2E	FY1E	FY2E	FY1E	FY1E	FY1E	
Leading Greater China Catering															
Yum China	9987 HK	HOLD	343.43	347.40	-1%	148,687	Dec-21	19.8	23.9	2.4	2.2	16.3	3.1	1.1	
Jiumaojiu	9922 HK	BUY	19.67	17.32	14%	25,173	Dec-20	49.8	31.2	6.0	5.2	14.3	0.6	0.5	
Haidilao	6862 HK	HOLD	16.85	18.40	-8%	102,562	Dec-20	653.2	31.5	7.3	6.1	14.3	5.3	0.2	
Nayuki	2150 HK	HOLD	7.83	7.13	10%	12,229	Dec-20	n/a	41.6	2.5	2.6	n/a	n/a	n/a	
Helens	9869 HK	NR	n/a	19.28	n/a	24,426	Dec-20	281.1	34.1	12.8	8.8	56.2	n/a	0.0	
Tam Jai	2217 HK	NR	n/a	2.92	n/a	3,914	Mar-21	13.3	10.1	2.2	1.9	62.4	1.1	1.8	
Cafe De Coral	341 HK	BUY	19.05	13.30	43%	7,790	Mar-21	33.4	19.9	2.5	2.4	9.6	2.6	1.7	
Xiabuxiabu	520 HK	NR	n/a	5.45	n/a	5,918	Dec-20	35.9	12.3	2.0	1.8	9.6	0.1	1.5	
Yihai	1579 HK	BUY	108.52	35.45	206%	37,113	Dec-20	33.2	27.6	7.3	6.0	26.9	4.1	0.8	
Gourmet Master	2723 TT	NR	n/a	110.00	n/a	5,545	Dec-20	16.9	15.7	1.7	1.7	12.0	1.1	3.6	
								Avg.	126.3	24.8	4.7	3.9	24.6	2.2	1.3
								Med.	33.4	25.8	2.5	2.5	14.3	1.9	1.1
Other Greater China Catering															
Tai Hing	6811 HK	NR	n/a	1.29	n/a	1,295	Dec-20	n/a	n/a	n/a	n/a	14.3	n/a	n/a	
Ajisen China	538 HK	NR	n/a	1.26	n/a	1,375	Dec-20	15.4	10.4	n/a	n/a	2.6	n/a	4.9	
								Avg.	15.4	10.4	n/a	n/a	9.0	n/a	4.9
								Med.	15.4	10.4	n/a	n/a	8.4	n/a	4.9
Greater China Catering															
								Avg.	115.2	23.5	4.7	3.9	19.8	2.2	1.6
								Med.	33.3	23.9	2.5	2.5	14.3	1.9	1.3
International Catering															
Yum! Brands	YUM US	NR	n/a	124.97	n/a	285,461	Dec-21	25.2	22.6	n/a	n/a	n/a	4.1	1.7	
Mcdonald'S	MCD US	NR	n/a	260.08	n/a	1,514,422	Dec-21	25.6	23.4	n/a	n/a	n/a	4.4	2.2	
Starbucks Corp	SBUX US	NR	n/a	94.92	n/a	850,836	Oct-21	28.4	24.3	n/a	n/a	n/a	3.7	2.1	
Rest' Brands	QSR US	NR	n/a	56.68	n/a	200,979	Dec-20	20.5	18.7	8.3	11.7	30.9	0.7	3.7	
Chipotle	CMG US	NR	n/a	1460.4	n/a	320,175	Dec-21	45.9	34.9	15.0	12.4	30.2	1.5	n/a	
Darden	DRI US	NR	n/a	141.00	n/a	140,335	May-21	18.6	16.6	7.1	6.6	36.9	0.8	3.1	
Domino'S Pizza	DPZ US	NR	n/a	438.73	n/a	124,399	Jan-21	32.2	28.8	n/a	n/a	n/a	2.8	0.9	
Wendy'S Co	WEN US	NR	n/a	22.82	n/a	39,234	Jan-21	28.2	25.7	10.3	11.9	35.1	1.1	1.9	
Shake Shack	SHAK US	NR	n/a	71.98	n/a	23,593	Dec-20	n/a	594.9	7.4	7.2	(4.4)	n/a	n/a	
Wingstop Inc	WING US	NR	n/a	148.87	n/a	34,600	Dec-20	104.9	79.7	n/a	n/a	n/a	2.5	0.4	
Jollibee Foods	JFC PM	NR	n/a	241.60	n/a	40,760	Dec-20	86.4	46.0	4.8	4.3	8.6	(0.5)	0.6	
								Avg.	41.6	83.2	8.8	9.0	22.9	2.1	1.8
								Med.	28.3	25.7	7.8	9.5	30.6	2.0	1.9
H-shares Consumer Staples															
UPC	220 HK	NR	n/a	8.07	n/a	34,857	Dec-20	19.3	17.0	2.1	2.1	10.6	23.7	5.3	
Tingyi	322 HK	NR	n/a	17.22	n/a	96,974	Dec-20	20.9	18.4	3.8	3.8	19.7	2.5	6.1	
Want Want	151 HK	NR	n/a	7.75	n/a	92,221	Mar-21	17.7	16.5	4.5	4.3	29.5	1.9	3.6	
China Mengniu	2319 HK	NR	n/a	48.60	n/a	192,125	Dec-20	29.7	24.6	4.2	3.7	16.4	0.9	0.9	
Vitasoy	345 HK	NR	n/a	15.62	n/a	16,714	Mar-21	118.3	34.9	4.9	4.4	(2.6)	123.1	0.1	
Budweiser	1876 HK	NR	n/a	21.90	n/a	290,030	Dec-20	40.1	33.9	3.3	3.1	8.3	1.2	1.0	
Tsingtao	168 HK	NR	n/a	70.90	n/a	125,728	Dec-20	27.3	24.6	3.5	3.2	12.7	1.3	1.6	
CR Beer	291 HK	NR	n/a	59.20	n/a	192,055	Dec-20	36.1	34.8	6.4	5.8	18.4	1.1	1.1	
Dali Foods	3799 HK	NR	n/a	4.41	n/a	60,391	Dec-20	12.8	12.0	2.6	2.4	22.8	1.6	4.1	
								Avg.	35.8	24.1	3.9	3.6	15.1	17.5	2.6
								Med.	27.3	24.6	3.8	3.7	16.4	1.6	1.6

Source: Bloomberg, Company data, CMBIS estimates,

Financial Summary

Income statement						Cash flow summary					
YE 31 Dec (USD mn)	FY20A	FY21A	FY22E	FY23E	FY24E	YE 31 Dec (USD mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	8,263	9,853	11,269	12,743	14,128	Net income	961	1,386	996	1,224	1,467
Company sales	7,396	8,961	10,300	11,706	13,030	D&A	386	431	427	491	564
Franchise fees and income	148	153	166	180	195	Change in working capital	69	43	67	99	94
Fran. & uncol. affiliates sales	647	663	731	790	836	Income tax paid	111	160	(276)	(331)	(395)
Other revenues	72	76	72	67	67	Others	(413)	(889)	341	250	165
Cost of goods sold	(2,342)	(2,812)	(3,265)	(3,664)	(4,052)	Net cash from operating	1,114	1,131	1,555	1,734	1,895
Gross profit	5,921	7,041	8,004	9,079	10,075	Capex & investments	(419)	(689)	(845)	(828)	(848)
Other net income	285	643	79	89	99	Associated companies	-	-	-	-	-
Operating expenses	(5,245)	(6,298)	(7,087)	(7,944)	(8,708)	Interest received	-	-	-	-	-
Staff costs	(1,730)	(2,258)	(2,652)	(2,982)	(3,281)	Others	(2,690)	(166)	-	-	-
Admin	(591)	(663)	(699)	(790)	(848)	Net cash from investing	(3,109)	(855)	(845)	(828)	(848)
Property rent & related	(814)	(968)	(1,112)	(1,264)	(1,407)	Equity raised	2,187	(75)	-	-	-
D & A	(404)	(443)	(490)	(547)	(617)	Change of Debts	-	-	-	-	-
Other operating expenses	(1,706)	(1,967)	(2,134)	(2,361)	(2,555)	Dividend paid	(95)	(203)	(208)	(188)	(231)
EBIT	961	1,386	996	1,224	1,467	Others	(34)	(35)	-	-	-
Finance costs, net	43	60	64	73	84	Net cash from financing	2,058	(313)	(208)	(188)	(231)
JV & associates	-	-	-	-	-	Net change in cash	63	(37)	502	717	817
Exceptional	104	(54)	23	25	28	Beginning cash balance	1,046	1,158	1,136	1,638	2,355
Pre-tax profit	1,108	1,392	1,082	1,322	1,579	Exchange difference	49	15	-	-	-
Income tax	(295)	(369)	(276)	(331)	(395)	Cash at the end of the year	1,158	1,136	1,638	2,355	3,172
Less: Minority interests	29	33	26	31	37						
Net profit	784	990	781	960	1,147						

Balance sheet						Key ratios					
YE 31 Dec (USD mn)	FY20A	FY21A	FY22E	FY23E	FY24E	YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Non-current assets	5,939	8,507	8,670	8,855	9,086	Sales mix (%)					
Fixed asset	1,765	2,251	2,669	3,006	3,290	Company sales	89.5	90.9	91.4	91.9	92.2
Intangible assets & goodwill	246	272	209	153	101	Franchise fees and income	1.8	1.6	1.5	1.4	1.4
Prepaid lease payments	-	-	-	-	-	Fran. & uncol. affiliates sales	7.8	6.7	6.5	6.2	5.9
Interest in asso. & JV	85	292	292	292	292	Other revenues	0.9	0.8	0.6	0.5	0.5
Others	3,843	5,692	5,500	5,404	5,404	Total	100.0	100.0	100.0	100.0	100.0
Current assets	4,936	4,716	5,328	6,149	7,066	P&L ratios (%)					
Cash and cash equivalents	1,158	1,136	1,638	2,355	3,172	Gross margin	71.7	71.5	71.0	71.2	71.3
Inventories	398	432	482	541	598	Operating margin	11.6	14.1	8.8	9.6	10.4
Trade and other receivables	99	67	95	107	119	Pre-tax margin	13.4	14.1	9.6	10.4	11.2
Prepayments	176	221	253	286	317	Net margin	9.5	10.0	6.9	7.5	8.1
Others	3,105	2,860	2,860	2,860	2,860	Effective tax rate	26.6	26.5	25.5	25.0	25.0
Current liabilities	2,067	2,383	2,559	2,762	2,957	Balance sheet ratios					
Borrowings	-	-	-	-	-	Current ratio (x)	2.4	2.0	2.1	2.2	2.4
Trade payables	708	782	865	971	1,074	Quick ratio (x)	2.2	1.8	1.9	2.0	2.2
Accruals & other payables	514	650	743	841	932	Cash ratio (x)	0.6	0.5	0.6	0.9	1.1
Tax payables	72	51	51	51	51	Inventory turnover days	61	54	54	54	54
Others	773	900	900	900	900	Trade receivables days	4	3	3	3	3
Non-current liabilities	2,337	2,918	2,918	2,918	2,918	Trade payables days	104	97	97	97	97
Borrowings	-	-	-	-	-	Total debt / total equity ratio (%)	-	-	-	-	-
Deferred income	-	-	-	-	-	Net debt / equity ratio (%)	Net cash	Net cash	Net cash	Net cash	Net cash
Deferred tax	-	-	-	-	-	Returns (%)					
Others	2,337	2,918	2,918	2,918	2,918	ROE	12.1	12.5	9.2	10.3	11.2
Minority Interest	-	-	-	-	-	ROA	7.2	7.5	5.6	6.4	7.1
Total net assets	6,471	7,922	8,520	9,324	10,277	Per share					
Shareholders' equity	6,471	7,922	8,520	9,324	10,277	EPS (USD)	1.89	2.26	1.77	2.17	2.58
						DPS (USD)	0.23	0.49	0.44	0.54	0.64
						BVPS (USD)	15.41	18.75	20.04	21.81	23.89

Source: Company data, CMBIS estimates

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