

Yum! Brands, Inc.(YUM)

\$69.83 (As of 03/16/20)

Price Target (6-12 Months): **\$59.00**

Long Term: 6-12 Months

Zacks Recommendation: Underperform

(Since: 02/10/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)
5-Strong Sell

Zacks Style Scores:

VGM:C

Value: F

Growth: A

Momentum: B

Summary

Yum Brands' shares have underperformed the industry in the past year. The downtrend might persist as it reported lower-than-expected fourth-quarter 2019 earnings. The bottom line missed the consensus mark for the second straight quarter. Moreover, choppy sales trend at Pizza Hut division remains a concern. In fourth-quarter 2019, Pizza Hut same-store sales declined 2%. The company believes that the choppy sales trend will persist through 2020. Yum! Brands business is likely to be impacted by the coronavirus outbreak. Of late, earning estimates for 2020 have witnessed downward revisions, reflecting analyst concern regarding growth potential. However, increased franchising is anticipated to stabilize earnings, increase profit margins, lower capital requirements and strengthen cash flow. Further, solid focus on restaurant development bodes well.

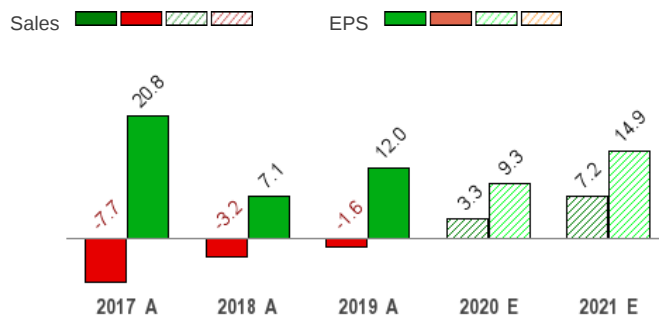
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$119.72 - \$67.08
20 Day Average Volume (sh)	2,873,283
Market Cap	\$21.0 B
YTD Price Change	-30.7%
Beta	0.53
Dividend / Div Yld	\$1.88 / 2.7%
Industry	Retail - Restaurants
Zacks Industry Rank	Top 33% (84 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	-9.9%
Last Sales Surprise	2.2%
EPS F1 Est- 4 week change	-0.7%
Expected Report Date	05/06/2020
Earnings ESP	-5.4%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	1,390 E	1,469 E	1,509 E	1,813 E	6,195 E
2020	1,287 E	1,367 E	1,431 E	1,703 E	5,779 E
2019	1,254 A	1,310 A	1,339 A	1,694 A	5,597 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$0.94 E	\$1.11 E	\$1.12 E	\$1.32 E	\$4.46 E
2020	\$0.78 E	\$0.94 E	\$1.00 E	\$1.14 E	\$3.88 E
2019	\$0.82 A	\$0.93 A	\$0.80 A	\$1.00 A	\$3.55 A

*Quarterly figures may not add up to annual.

P/E TTM	19.7
P/E F1	18.0
PEG F1	1.5
P/S TTM	3.8

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/16/2020. The reports text is as of 03/17/2020.

Overview

Louisville, KY-based YUM! Brands Inc. – formerly Tricon Global Restaurants, Inc. – had spun off from PepsiCo in October 1997. YUM! Brands is the global leader in multi-branding and offers consumers more choice and convenience at one outlet. The company presently reports through three segments – KFC (44.5% of total revenues in 2019), Pizza Hut (18.3%) and Taco Bell (37.2%). Notably, Yum! Brands now owns, operates and franchises over 50,000 fast food stores under KFC, Pizza Hut and Taco Bell brands in more than 150 countries and territories. As of Dec 31, 2019, the company's 98% of units were operated by independent franchisees or licensees under the terms of franchise or license agreements.

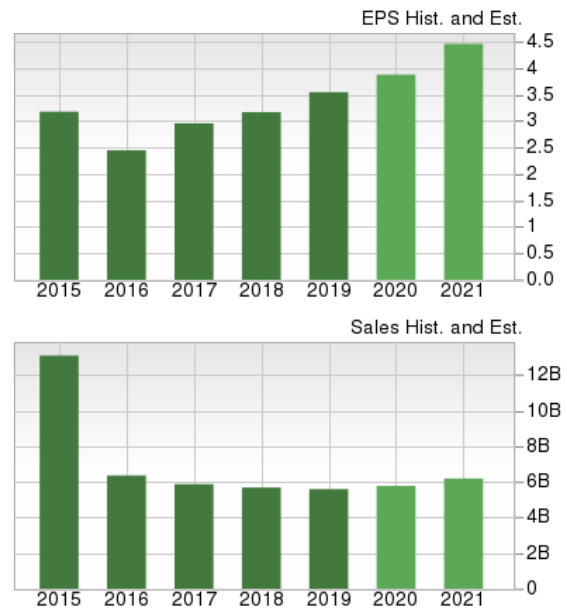
The company opened 1,757 net new units in 2018 and added 1,282 Telepizza, reflecting 7% year-over-year net unit growth. Yum! Brands refranchised 660 restaurants — including 364 KFC, 97 Pizza Hut and 199 Taco Bell units — for pre-tax proceeds of \$825 million, recording net refranchising gains of \$540 million.

The company exercises store-level franchise and master franchise programs to grow its businesses. Nearly 30% of its franchised units operate under master franchise programs. The remaining franchised units operate under store-level franchise agreement.

On Oct 31, 2016, Yum! Brands' completed the spin-off of the China business into an independent, publicly-traded company. Yum China Holdings began trading as an independent company, effective Nov 1, 2016, on the New York Stock Exchange (NYSE), under the ticker symbol "YUMC".

In February 2018, Yum! Brands announced a partnership with online food delivery platform Grubhub, to enhance online sales and delivery from its restaurants. As part of the deal, Yum! Brands will acquire \$200 million of Grubhub stock. The proceeds are used by Grubhub to speed up the expansion of its delivery capacity.

Yum! Brands was 98% franchised by the end of 2018. The company will have the provision to triple its unit count in the long term, with strong growth from emerging markets.



Reasons To Sell:

- ▼ **Dismal Performance at Pizza Hut:** Despite effective innovation across products, marketing and promotions, Pizza Hut sales trend has been choppy in the recent quarter. In fourth-quarter 2019, Pizza Hut same-store sales declined 2%. Same-store sales were flat in the third-quarter 2019. YUM! Brands is focusing on transforming its Pizza Hut business to a modern delivery asset base in the United States. It is also restructuring and upgrading its franchisee base. The company believes that the choppy sales trend will continue through 2020.
- ▼ **Coronavirus of Impact:** Yum! Brands business is likely to be impacted by the coronavirus in China and the threat of it spreading to adjacent areas. The company announced that it is closely monitoring the situation.
- ▼ **High Costs:** An increase in the cost of employee wages, benefits and insurance, and other operating costs such as rent and energy costs led to significant pressure on the company's margins. A competitive retail environment also put pressure on the restaurants' costs. The company is also susceptible to profit margin pressure owing to relentless expansion. In fourth-quarter 2019, company restaurant expenses and general and administrative expenses increased 3% and 13%, respectively.
- ▼ **Overvalued:** Yum! Brands' valuation looks a bit stretched compared with its industry average. Looking at the company's forward 12-month price-to-earnings (P/E) ratio, which is one of the most commonly used valuation ratios and is best suited for evaluating restaurants, investors might not want to pay any further premium. It currently has a forward 12-month P/E ratio of 17.44. So, the stock is relatively overvalued right now compared with its peers as the industry's average PE is 16.93 currently.
- ▼ **Industry Susceptible to Consumer Discretionary Spending:** Yum Brands operates in the retail restaurant space that is highly dependent on consumer discretionary spending. Consumers' propensity to spend largely depends on the overall macroeconomic scenario. Although higher disposable income and increased wages are favoring the industry right now, it can change with the slightest disruption in the economy. The company, therefore, is highly vulnerable to the inconsistent nature of consumer discretionary spending. If it does not make pragmatic use of advanced technologies to innovate across value chains, it has high chances of fading out like many other restaurant retailers.

Yum! Brands have been facing declining revenues at its Pizza Hut division. Decline in net new unit growth and low system sales have been affecting comps as well.

Risks

- **Transformation Initiatives Drive Growth:** Yum! Brands has a three-year strategic transformation plan to drive growth at KFC, Pizza Hut and Taco Bell brands. Notably, the company's transformation and growth strategy involve employing greater focus on the development of its three iconic global brands, increasing its franchise ownership and creating a leaner, more efficient cost structure. It is also focusing on restaurant development to drive continued growth. By relying extensively on the four key drivers of growth — distinctive, relevant and easy brands; unmatched franchise operating capability; bold restaurant developments; and unrivaled culture and talent — the company remains on track to achieve its long-term target.

- **Strong Digital & Delivery Services to Enhance Guest Experience:** The digital wave has hit the U.S. fast-casual restaurant sector. More and more restaurants are deploying technology to enhance guest experience. Yum! Brands is also not far behind in the race as the company is continuing the transformation process toward a single point-of-sale system in the United States. Further, it updated its mobile app and Hut Rewards. It also has more than 12 million active users in the loyalty program.

Yum! Brands' partnership with online food delivery platform Grubhub will enhance online sales and delivery from its restaurants. Additionally, the company implemented various digital features in mobile and online platforms across all brand segments to enhance guest experience. The company has also worked toward making its delivery services swifter and the results have been positive so far. The company currently has 2,800 KFCs, offering delivery, and 3,800 restaurants available for click-and-collect on the Grubhub marketplace. Pizza Hut has 700 locations on the Grubhub marketplace. For Taco Bell, delivery is available in more than 4,800 restaurants.

- **Refranchising Strategy Safeguards Earnings:** Yum! Brands has adopted a de-risking strategy by reducing its ownership of restaurants through refranchising. In fact, the China division's spin-off has largely made Yum! Brands a more asset-light company, as many company-owned restaurants have been in the Chinese market. We note that refranchising a large portion of the system reduces the company's capital requirements and facilitates earnings per share growth and ROE expansion. Alongside, free cash flow will continue to grow, facilitating reinvestments to increase brand recognition and shareholder return. Remarkably, this shift to refranchising has substantially benefited the company's operating margin over the years. Thus, Yum! Brands expects to become a "pure play" franchisor with more stable earnings, higher profit margins, lower capital requirements and stronger cash flow conversion. Moreover, since a major portion of its business is refranchised, Yum! Brands will be less affected by food inflation than most of its peers.
- **Increased Efficiency & Unit Growth:** Yum! Brands' aims to revamp financial profile. This, in turn, will improve efficiency of its organization and cost structure globally. It believes that a "slimmer Yum Brands" would lead to efficiency gains. In 2020, management expects capex net of refranchising proceeds in the range of \$125 million to \$150 million. Additionally, the company aims to maintain an optimized capital structure, with the leverage of five times EBITDA.

In 2019, the company opened 3,332 gross new restaurants and 2,040 restaurants on a net new basis. The company opened on an average nine gross restaurants per day.

Last Earnings Report

YUM! Brands Q4 Earnings Miss, Revenues Top Estimates

YUM! Brands reported mixed fourth-quarter 2019 results, wherein earnings missed the Zacks Consensus Estimate but revenues beat the same. However, both the top and bottom lines improved year over year.

Earnings & Revenues

The company's adjusted earnings of \$1.00 per share missed the Zacks Consensus Estimate of \$1.11. However, the bottom line surged 148% on a year-over-year basis. The shift to refranchising substantially bolstered the company's operating margin and earnings per share. The trend is expected to continue in the coming quarters.

YUM! Brands' total revenues of \$1,694 million were up 9% year over year and surpassed the consensus estimate of \$1,658 million. This upside can be attributed to increase in company sales as well as franchise and property revenues, and franchise contributions for advertising and other services.

Worldwide system sales — excluding foreign currency translation — increased 10% year over year, with KFC, Pizza Hut and Taco Bell growing 11%, 7% and 13%, respectively. The company also opened 1,029 net new units, reflecting unit growth of 4%.

Segmental Performance

YUM! Brands reports results under three segments — KFC, Pizza Hut and Taco Bell.

Revenues from KFC totaled \$732 million, up 7% on a year-over-year basis. Comps at this division rose 3% from the year-ago quarter's growth of 3% and the third quarter's improvement of 3%.

This segment's operating margin was up 180 basis points (bps) year over year to 39%, owing to refranchising and same-store sales growth. Unit growth also drove margins.

In the quarter under review, the segment opened 814 gross new restaurants.

At Pizza Hut, revenues amounted to \$297 million, up 8% on a year-over-year basis. Comps were down 2% in the reported quarter. Notably, comps were flat in the in third-quarter 2019.

The segment's operating margin was down 290 bps year over year to 30.2% due to higher provisions for past owing to receivables and related higher G&A, partially offset by lower advertising spend.

Pizza Hut Division opened 431 gross new restaurants in the fourth quarter.

Taco Bell's revenues were \$665 million, up 11% from the year-ago quarter. Comps rose 4% in the reported quarter, down from the year-ago quarter's growth of 6%. In third-quarter 2019, the segment's comps gained 4% year over year. This segment's operating margin was up 180 bps year over year to 33.7%.

Taco Bell recorded 191 gross new restaurants openings during the quarter.

Other Financial Details

Cash and cash equivalents as of Dec 31, 2019 totaled \$605 million compared with \$292 million on Dec 31, 2018. Long-term debt at the end of the reported quarter was \$10,131 million compared with \$9,751 million at 2018-end. During the reported quarter, the company repurchased 3.2 million shares for \$103 million.

Quarter Ending 12/2019

Report Date	Feb 06, 2020
Sales Surprise	2.18%
EPS Surprise	-9.91%
Quarterly EPS	1.00
Annual EPS (TTM)	3.55

Recent News

YUM! Brands to Acquire Habit Burger Grill For \$375 Million- Jan 06,2020

YUM! Brands, Inc. entered into a definitive agreement to acquire fast-casual concept operator, The Habit Restaurants, Inc. (HABT). The addition will enable YUM! Brands to extend its reach in a unique fast-casual concept — The Habit Burger Grill.

The transaction, which is expected to be completed by the end of second-quarter 2020, is valued at approximately \$375 million. The purchase price of \$14 a share suggests a 33% premium over Habit Restaurant's Jan 3, 2020 closing price. Notably, YUM! Brands stated that it will fund the transaction using cash on hand and available borrowing capacity under its credit facilities.

Valuation

Yum! Brands shares are down 30.6% year-to-date and 30.3% in the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Retail-Wholesale sector are down by 30.8% and 20.3% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector is down by 23.9% and 12.8%, respectively..

The S&P 500 index is down 25.9% in the year-to-date period and 16.5% in the past year.

The stock is currently trading at 17.44X forward 12-month earnings, which compares to 16.93X for the Zacks sub-industry, 19.85X for the Zacks sector and 13.88X for the S&P 500 index.

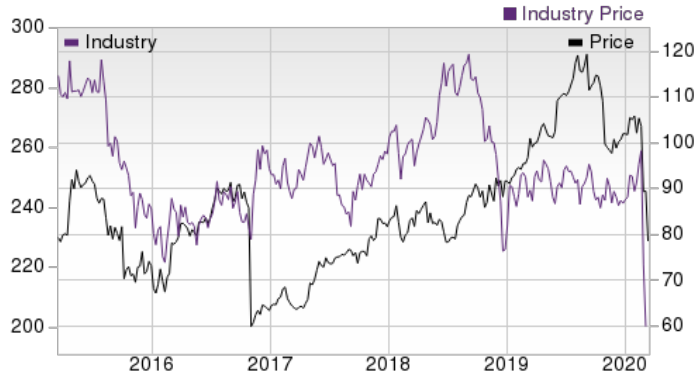
Over the past five years, the stock has traded as high as 29.27X and as low as 14.84X, with a 5-year median of 23.75X. Our Underperform recommendation indicates that the stock will perform worse-than the market. Our \$59 price target reflects 14.75X forward 12-month earnings.

The table below shows summary valuation data for YUM

Valuation Multiples - YUM					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	17.44	16.93	19.85	13.88
	5-Year High	29.27	26.6	26.2	19.34
	5-Year Low	14.84	16.93	19.07	13.88
	5-Year Median	23.75	23.12	23.01	17.42
P/S F12M	Current	3.58	2.43	0.82	2.55
	5-Year High	6.62	3.9	1.11	3.43
	5-Year Low	1.65	2.43	0.8	2.54
	5-Year Median	4.71	3.27	0.92	3
P/CF	Current	16.41	12.03	11.31	12.4
	5-Year High	77.54	20.5	15.19	22.67
	5-Year Low	12.75	8.56	10.75	11.78
	5-Year Median	24.88	16.7	12.88	16.38

As of 03/16/2020

Industry Analysis Zacks Industry Rank: Top 33% (84 out of 253)



Top Peers

Cracker Barrel Old Country Store, Inc. (CBRL)	Outperform
Dominos Pizza Inc (DPZ)	Neutral
JAKKS Pacific, Inc. (JAKK)	Neutral
McDonalds Corporation (MCD)	Neutral
Papa Johns International, Inc. (PZZA)	Neutral
Red Robin Gourmet Burgers, Inc. (RRGB)	Neutral
The Wendys Company (WEN)	Neutral
Yum China Holdings Inc. (YUMC)	Underperform

Industry Comparison Industry: Retail - Restaurants				Industry Peers		
	YUM Underperform	X Industry	S&P 500	DPZ Neutral	MCD Neutral	YUMC Underperform
VGM Score	C	-	-	C	D	C
Market Cap	21.01 B	239.63 M	16.36 B	11.17 B	111.08 B	15.54 B
# of Analysts	11	6	13	11	15	6
Dividend Yield	2.69%	0.00%	2.63%	1.09%	3.36%	1.16%
Value Score	F	-	-	F	F	F
Cash/Price	0.03	0.06	0.06	0.03	0.01	0.11
EV/EBITDA	15.49	9.50	10.54	21.55	14.60	9.72
PEG Ratio	1.47	1.44	1.46	1.97	1.98	5.53
Price/Book (P/B)	NA	1.41	2.26	NA	NA	4.90
Price/Cash Flow (P/CF)	17.29	6.04	8.80	25.14	14.74	13.44
P/E (F1)	18.00	10.91	13.18	26.29	17.45	52.24
Price/Sales (P/S)	3.75	0.49	1.78	3.09	5.27	1.77
Earnings Yield	5.56%	8.56%	7.56%	3.80%	5.73%	1.91%
Debt/Equity	-1.26	0.96	0.70	-1.25	-5.71	0.01
Cash Flow (\$/share)	4.04	1.81	7.01	11.39	10.11	3.08
Growth Score	A	-	-	A	C	A
Hist. EPS Growth (3-5 yrs)	0.67%	7.16%	10.85%	31.17%	12.23%	NA
Proj. EPS Growth (F1/F0)	9.35%	7.24%	5.72%	13.79%	8.91%	-57.89%
Curr. Cash Flow Growth	3.60%	6.53%	6.15%	9.16%	-0.99%	10.09%
Hist. Cash Flow Growth (3-5 yrs)	-6.71%	6.24%	8.55%	17.68%	1.88%	25.34%
Current Ratio	0.99	0.62	1.24	1.74	0.98	1.30
Debt/Capital	NA%	61.41%	42.57%	NA	NA	0.81%
Net Margin	23.12%	3.73%	11.64%	11.07%	28.59%	8.12%
Return on Equity	-13.90%	7.15%	16.74%	-13.12%	-79.57%	22.96%
Sales/Assets	1.14	1.10	0.54	2.97	0.45	1.29
Proj. Sales Growth (F1/F0)	3.25%	3.05%	3.50%	8.75%	4.32%	-11.61%
Momentum Score	B	-	-	D	D	B
Daily Price Chg	-11.00%	-16.02%	-12.67%	-9.57%	-15.88%	-0.89%
1 Week Price Chg	-12.24%	-18.60%	-11.01%	-5.88%	-10.93%	-1.97%
4 Week Price Chg	-33.67%	-42.86%	-32.63%	-1.81%	-31.36%	-7.78%
12 Week Price Chg	-30.04%	-43.23%	-30.17%	-0.68%	-24.05%	-14.40%
52 Week Price Chg	-30.34%	-49.28%	-23.26%	17.63%	-18.99%	-4.92%
20 Day Average Volume	2,873,283	413,722	3,457,426	1,361,261	5,676,725	3,822,888
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.72%	-0.33%	-0.48%	2.60%	0.00%	0.00%
(F1) EPS Est 12 week change	-6.62%	-0.44%	-0.93%	3.43%	0.70%	-57.32%
(Q1) EPS Est Mthly Chg	-1.61%	-0.16%	-0.60%	1.91%	0.00%	0.00%

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	F
Growth Score	A
Momentum Score	B
VGM Score	C

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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