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PRESENTATION

Operator

Ladies and gentlemen, thank you for standing by, and welcome to today's Yum China 2019 Second Quarter Earnings Conference Call. (Operator Instructions) I must advise you that this conference is being recorded today, Wednesday, the 31st of July 2019.

I would now like to hand the conference over to your speaker today, Florence Lip. Thank you. Please go ahead.

Florence Lip ***Yum China Holdings, Inc. - Senior Director of IR***

Thank you, Shira. Hello, everyone, and thank you for joining Yum China's Second Quarter 2019 Earnings Conference Call. Joining us on today's call are Ms. Joey Wat, CEO of Yum China; and Mr. Jacky Lo, CFO of the company.

Before we get started, I'd like to remind you that our earnings call and investor presentation contain forward-looking statements, which are subject to future events and uncertainties. Our actual results may differ materially from these forward-looking statements. All forward-looking statements should be considered in conjunction with the cautionary statement in our earnings release and the risk factors included in our filings with the SEC. This call contains certain non-GAAP financial measures. You should carefully consider the comparable GAAP measures and reconciliation thereto.

Today's call includes 3 sections. First, Joey will cover Yum China's second quarter 2019 highlights; and Jacky will cover the financial results. We will then open the call to questions.

The webcast of this call will be available on our website. A PowerPoint presentation, which contains operational and financial information for the quarter, is available for download.

At this time, I would like to turn the call over to Ms. Joey Wat, CEO of Yum China.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Thank you, Florence. Hello, everyone, and thank you for joining us today. As we hit the midpoint of the year, I want to share some of the reasons why I'm excited about where we are and the future of Yum China.

First, our strong performance in the first half of the year demonstrate our resilient business model. KFC has consistently delivered strong same-store sales growth, and the revitalization of Pizza Hut is clearly on track. Second, with new and exciting menu options, growing digital data and delivery capabilities and a variety of new store formats, we are driving innovations throughout our business. And I'm confident that these innovations will drive the sustainable and profitable growth of our business. Third, with accelerated store openings, it's clear that there are many untapped opportunities to expand our portfolio of restaurants across all city tiers in China. And of course, all these is enabling us to continue to deliver significant shareholder return with a focused capital return program that combines both dividends and share repurchases.

Now let me share a few highlights of the quarter before diving into the details about our 2 core brands. Yum China delivered another strong quarter in Q2 with solid revenue and profit growth despite several notable challenges such as macro uncertainty and elevated chicken prices. In Q2, we delivered our 11th consecutive quarter of system sales growth since we spun off from Yum! Brands.

Strong system sales growth of 10% was driven by 2 consecutive quarters of positive same-store sales at both of our core brands, KFC and Pizza Hut, as well as our ongoing expansion of the store network to serve attractive markets in China. We opened 178 new stores in the second quarter, increasing our year-to-date total to 415 stores. At this pace, we expect to exceed our original full year target, which Jacky will cover shortly.

Sales leverage and diligent cost control allows us to increase operating profit by 6% despite margin pressure due to rising chicken prices, wage increases, ongoing promotional activities and currency headwinds. And we continue to make strides in digital. With over 200 million digital members already, we have a world-leading restaurant membership program.

Now I will provide more color on the performance and strategy of our key brands, starting with KFC. KFC reported another strong quarter of growth by offering exciting products and great value, driving delivery growth and more effectively engaging with our customers through our digital ecosystem. KFC achieved robust same-store sales growth of 5% in Q2. With our aggressive new store build-outs, system sales increased by 12%. KFC opened 136 new stores in the second quarter, and we will continue to expand to capture the opportunities we see across city tiers in China. Operating profit grew 10% in constant currency, an excellent result considering the cost pressures which Jacky will elaborate on.

We launched exciting new limited time offers, or LTOs, such as chicken and crayfish tacos and double chili chicken. We also launched our new premium burger line nationwide, including shrimp and imported beef, which aims to capture consumers who are willing to pay more for premium products and drive a higher ticket average. These initiatives are aligned with our strategy of increasing nonchicken protein options to better manage commodity costs as well as providing new and exciting options for our customers.

Our key growth categories, namely, breakfast, coffee, dessert and delivery, already accounted for over 1/3 of sales. These initiatives, led by improved customer engagement, menu offerings and store formats, all drove strong sales growth in the quarter. K-Coffee, in particular, has continued to rapidly gain traction, and we sold over 60 million cups in the first half of 2019, which is an increase of over 45 percentage year-over-year, in part due to our effective cross-selling via digital memberships.

Throughout the quarter, we also maintained our focus on smart value, most notably with Crazy Thursday, which has gained very strong consumer awareness. We also launched chicken wing bucket and festival bucket promotion for sharing occasions and continued building on our YUMC Pay platform by offering attractive discounts in partnership with UnionPay.

Turning to digital. We are a market leader in this space, and we continue to build and leverage our powerful digital ecosystem, which is having a significant positive impact across our entire business. In the second quarter, we updated our Super App for KFC with improved customer interface and functionality.

The power of our digital ecosystem to drive sales and improve customer experience continues to expand. Members now accounted for 54% of total sales, up 9 percentage points; and digital orders accounted for 63%, up 21 percentage points year-over-year, largely due to the growth in mobile preorders. Combined, our various digital initiatives and capabilities are having a positive impact on spending per user.

In particular, our Privilege subscription program, which is essentially paid membership, increased in popularity with over 4 million sold in the second quarter, 3x as many as in the first quarter. We continue to see a significant uptick in frequency and spending from these members, and we are creating new offers that will roll out in the second half of the year.

Delivery represent 18% of KFC business in the second quarter, up 5 percentage points year-over-year, and growth through our own channels continue to exceed growth rates via aggregators. KFC's ability to address customer preferences through offering smart value, continuous innovations in menu and daypart and leadership in digital and delivery have created a robust platform for sustainable and profitable growth. We will pursue an aggressive store-building program for the remainder of 2019 and remain very excited about KFC's long runway for growth in China.

Next, I will provide some color on Pizza Hut performance. Pizza Hut continues to make good progress on the path towards revitalization. We achieved a second consecutive quarter of same-store sales growth on the back of a significant increase in traffic in both dining and delivery. We were particularly pleased by the ongoing traffic growth in dine-in stores, which is the first time we have achieved successive quarters of traffic growth at Pizza Hut dining since 2014.

The Pizza Hut revitalization program continue to focus on 4 pillars: fixing the fundamentals, driving digital, optimizing delivery and enhancing asset portfolio. First, let's look at the fundamentals. This was the first full quarter since launching our new permanent menu in March. We streamlined and improved our menu with around 35 percentage less items compared with the prerevitalization menu, and approximately 75% of our menu items are either new or upgraded. The new menu has been well received by customers, particularly the innovative and trendy products, ease of ordering and abundant choices of steak.

We introduced exciting limited time offers such as salty -- salted egg yolk shrimp pizza, Xian Dan Huang Da Xia pizza; and Musang King durian pizza Mao Shan Wang Liu Llian pizza, which is the best; as well as our double crispy pizza, which is a cheese-filled, thin and crispy pizza. We also launched specials to drive strong sales over holidays such as Children's Day and Labor Day, among others. We remain focused on continuing to drive increased traffic, in particular, with attractive value offers. Our signature Scream Wednesday promotion with special offers on steak, pizza, dessert and drinks at CNY 29 or CNY 39 continue to drive strong incremental sales during the quarter.

Like KFC, we are leveraging and building on our digital ecosystem to drive increased traffic and sales and continue to make progress. Digital members now account for 47% of sales. We continue to refine and expand our Privilege subscription offer with 1 million sold in Q2. With enhanced offer, our family privilege program remains popular and has resulted in increased member frequency and spending. We will further build on the member program in the second half of the year.

Turning to delivery. Effective promotions and improved operations continue to drive significant growth. Delivery now accounts for 25% of sales, up 2 percentage points year-over-year, with sales from our own channels growing much faster than via aggregators. We continue to optimize operations after taking back control of last-mile delivery late last year, and we are seeing continuous improvement in operational efficiency and customer satisfaction. For example, the average fulfillment time and complaint rates have been improving month on month since the beginning of the year. Lastly, we continue to enhance our asset portfolio through accelerated remodels and multiple store formats. To create a more comfortable and stylish dining environment, we are targeting around 500 remodels in 2019 and to complete the refresh of our portfolio by 2021. We remodeled 78 stores in the second quarter, and we will accelerate the pace through the rest of the year.

We also opened 26 new stores in the second quarter, similar to the same period in 2018. We are continuing to test smaller store formats, including the hub and spoke model, to more efficiently increase our service coverage. We are encouraged by the initial result and plan to open more stores in smaller format in the second half of the year.

Together, these revitalization initiatives are having a positive impact on the brand, and I'm confident in the long-term opportunity for Pizza Hut in China. We are encouraged to see the second consecutive quarter of positive same-store sales growth and improving profitability. This is a result of relentless focus on our 4 pillars. They are important operational areas that will always have our ongoing attention as they are crucial to support the core business. Given the scale of the business and the competitive environment, we will maintain focus on these areas in order to make additional important improvements to cement the positive momentum of the Pizza Hut brand.

Lastly, turning to our new standalone coffee concept, COFFii & JOY, added 8 stores in the second quarter, taking up to -- taking us up to 26 stores now across 8 cities. Our coffee machines have also been rolled out to 11 WeWork offices in Shanghai and Beijing.

Coffee as a category that's not new to us, and we have many reasons to be confident in this as an important market opportunity in China. That said, we are taking our time to explore different formats, fine-tuning the dayparts and product mix, building store density in primary trade zones and learning more about the supply chain.

With that, I will hand over the call to our CFO, Jacky Lo, who will cover our financial performance in more detail.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Thank you, Joey. Good day, everyone, and thank you for joining us.

Total revenues reached $2.1 billion in the second quarter of 2019, up 10% year-over-year, excluding foreign exchange translation. Total system sales grew 10% year-over-year, ex FX, primarily due to strong same-store sales growth and accelerated new store openings at KFC as well as improving sales at Pizza Hut.

We opened 178 new stores during the quarter, increasing our total portfolio to 8,751 restaurants as of the end of June. For the full year, as Joey mentioned, we are ahead of schedule on this front, which highlights the large volume of untapped market opportunities throughout China. We now anticipate opening. 800 to 850 new stores in 2019, with incremental stores planned across multiple brands. The majority of these are coming from KFC and the new inclusion of COFFii & JOY in the target.

During the quarter, KFC year-over-year system sales grew 12%, while Pizza Hut system sales increased 4%, both excluding FX. Yum China same-store sales increased 4%, and KFC same-store sales grew 5%, while Pizza Hut achieved its second consecutive quarter of same-store sales growth of 1%.

During the quarter, KFC traffic increased 3% year-over-year, and ticket average increased 2% year-over-year due to pricing and increased share of delivery, offset by increased promotions. Pizza Hut traffic increased 9% year-over-year and remains positive for both dine-in and delivery due to our successful ongoing efforts to drive traffic, including increased value promotions. Combined with the increasing share of delivery, which has a lower ticket average, overall ticket average decreased 7% year-over-year.

KFC restaurant margin remained under pressure at 16.1% in the second quarter of 2019 compared to 16.8% in the same period last year. The previously flagged chicken inflation, wage inflation and value campaigns continued to offset positive sales leverage. Average commodity inflation was slightly higher compared to the first quarter at mid-single digit. And due to the lack of inventory benefit, the margin impact was more than in the first quarter. Pizza Hut slightly improved its restaurant margin year-over-year from 11.1% to 11.3%. Commodity deflation and other store cost savings offset the margin pressure from promotional activities. Overall, Yum China restaurant margin was 14.7%, down 0.4 percentage points from the same period last year. Wage inflation was 6%, while commodity inflation was 3% compared to the same period last year, with chicken price increase the major driver of commodity inflation. Cost inflation was partly offset by sales leverage and effective store cost management. For the remainder of 2019, we anticipate that year-over-year impact of the chicken price increase has peaked in the second quarter, although we continue to expect to see pressure in the second half. We continue to expect overall commodity inflation to be low single digit for the full year.

G&A expense was up 16% year-over-year, ex FX, or 11% excluding one-off benefits in both periods, mainly due to salary increases and higher performance-related compensation. Our long-term goal remains to maintain a G&A growth rate lower than the revenue growth rate. Our closure and impairment charge in the second quarter was $4 million, down from $17 million during the second quarter in 2018, mainly due to the additional impairment review completed in the first quarter following the adoption of the new lease accounting standard. On a year-to-date basis, the closure and impairment charge is in line with the same period last year.

Operating profit for the second quarter of 2019 increased 6% year-over-year. Due to the depreciation of renminbi against the U.S. dollar, foreign exchange translation negatively impact our total operating profit by $16 million or 8% during the quarter. Excluding FX, operating profit increased 14% year-over-year. For the second quarter of 2019, KFC operating profit increased 10% year-over-year, ex FX, mainly driven by same-store sales growth and net unit growth. Pizza Hut operating profit improved 60%, ex FX, largely due to lower impairment charge.

Finally, diluted EPS was $0.46 in the second quarter of 2019 compared to $0.36 in the same period last year. Diluted EPS includes a positive mark-to-market of $17 million or $0.04 per share from our equity investment in Meituan.

Our effective tax rate during the second quarter was 20%, 6 percentage points lower than the second quarter last year, primarily due to lower accrued residual U.S. tax; benefit from the Meituan mark-to-market gain, which is nontaxable; and lower accrued foreign withholding tax on estimated repatriation of earnings outside of China. Our best estimate of the effective tax rate in 2019 continues to be below 28%, excluding any impact from the mark-to-market gain or loss from our equity investment in Meituan.

Next, let me cover our capital allocation strategy. Our strong free cash flow generation continued in the first half of 2019 with net cash from operations of $657 million and free cash flow of $445 million after subtracting $212 million in capital expenditures. We have over $1.58 billion in cash and short-term investment. We remain committed to returning excess capital to shareholders with $120 million total returns in the second quarter, including a cash dividend of $45 million and share repurchases of $75 million. There's approximately $820 million remaining under the share repurchase authorization as of the end of June 2019.

As we stated at our recent Investor Day, we have the capacity to return at least $1.5 billion to shareholders over the next 3 years. In the first 6 months of 2019, we have already returned $231 million. We'll also continue to invest for growth given the strong returns from new build.

Full year 2019 CapEx is expected to be above $475 million to $525 million, up slightly from our initial expectations due to the increase in store builds.

Now I will turn to our outlook. We have about 2019 with 2 good quarters of strong sales and operating profit growth, which shows that we have a solid foundation in place. We'll continue to focus on leveraging our leading digital capabilities to drive business and leading development capabilities to expand our store network. However, there are some specific near-term headwinds we do need to manage through in the second half of the year.

At KFC, while we believe that the impact of year-over-year chicken price increases has peaked in the second quarter, we expect that commodity inflation will continue to weigh on margins in the second half of the year. We intend to be more selective in our promotional activities to manage margin pressure. We'll also begin to lap several key sales initiatives such as our value promotions that successfully drove same-store sales since the second half of 2018. As a result, we expect that our same-store sales growth will moderate in the second half of the year.

At Pizza Hut, while we continue to expect quarterly fluctuations as we roll out our initiatives at scale, we are very encouraged by the progress of our brand revitalization program. We'll maintain our strategy of driving traffic through value promotions. In addition, our remodeling program will ramp up with approximately 400 planned remodels over the next 2 quarters. This will put pressure on sales and restaurant margin in the short term but is an important component of the long-term revitalization of the brand.

With all of this said, we are pleased with where we are as a business, and we are confident in our ability to deliver sustainable and profitable growth and shareholder value over the long term.

With that, I'll pass you back to Florence to start the Q&A.

Florence Lip ***Yum China Holdings, Inc. - Senior Director of IR***

Thanks, Jacky. We will now open the call for questions. (Operator Instructions) Operator, please start the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) And our first question comes from the line of Michelle Cheng from Goldman Sachs.

Michelle Cheng ***Goldman Sachs Group Inc., Research Division - Executive Director***

Congratulations for the good results again. And I would like to look into more details on the cost side. Jacky, you just mentioned that for the first quarter, KFC's commodity inflation is slightly above mid-single digit. And can you give us more details about chicken costs? And also, we understand other commodity costs are actually down, so can you also share any major commodity items like packaging material, et cetera, and how much this benefit we have been seeing in the first half?

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Yes, Michelle. On the commodity inflation for KFC, the chicken -- the commodity inflation was mid-single digit for both Q1 and Q2. But if you recall, in Q1, we actually benefit a little bit from the inventory we stock up in Q4 2018. And so even though both quarters are missing a digit, it was slightly higher this quarter. And also, in terms of chicken, I mean it's only one of many commodities for KFC. So it represents about 40% of our cost of sales. And so overall, the chicken price has gone up, and the impact year-over-year, we already talked about, we expect to peak this quarter. So it will moderate a little bit in the second half, but it will put pressure on the margin.

And so in terms of the inflation rate, so KFC has managed it really well. So it has been about low double digit for both Q1 and Q2 because we have very strong partnership with our suppliers. So we work closely with them to actually manage the inflation rate. So -- and yes, as you point out, there are other commodities that the price has actually gone down, but I will just continue to work on our margin initiatives through.

I talk about maybe we'll put back down on the promotional activities in the second half, and we'll continue to explore like other parts of chicken or nonchicken protein. So these are all the ways that we can use to mitigate the commodity inflation pressure.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Yes. And Michelle, you mentioned about the other commodity. I'll give an example. The other commodity price actually has a bit of deflation versus steak for Pizza Hut. I mean not to forget for Pizza Hut, 10% of our sales actually is from steak. And how did we get there? We explore more choices because steak, so in Pizza Hut, were imported. So we went for steaks in different countries and sourced different part of steaks and cooked it well and then served to the customer. So as you can see, as we manage the chicken price increase, which was significant for the first half, we not only explore other parts of chicken such as chicken breast or even the (Ji Chi Jian), the tip of the chicken wing, to manage, of course, but we also look at other opportunities outside chicken to balance the pressure in the commodity price increase. Thank you, Michelle.

Operator

And our next question comes from the line of Xiaopo Wei from Citigroup.

Xiaopo Wei ***Citigroup Inc, Research Division - Director & Head of Asia-Pacific Consumer Research***

Joey and Jacky, congratulations on another strong quarter. And my question is related to your commentary on the second half sales growth. As indicated press release, management mentioned that the top line growth in the second half will be moderated due to the high lapping, which is understandable, but shall we say that second half, the restaurant margin will be -- the pressure will be much less than the first half due to the peak-out of the chicken cost in the second quarter and also some just more control of the promotion cost?

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Joey, do you want me to take it and then you can elaborate?

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Yes, please.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Yes. Xiaopo, thanks for the questions. So first on the sales. So yes, as we point out, we expect same-store sales growth will moderate as we begin to lap several key sales initiative, for example, the Crazy Thursday and also the Privilege program for KFC. So these initiatives have driven our same-store sales growth in the second half of 2018. So we'll be lapping these. And so in a way, we expect the sales leverage impact will reduce in the second half.

In terms of margin, yes, so chicken price, as I mentioned, we believe the year-over-year impact of chicken price increase has peaked in Q2, but it will continue to put pressure on the margin. And also, we have wage inflation. And also, as the delivery business grows, we also incur additional rider cost. So these are all additional costs pressure on the margin.

And also, for KFC, we will continue to accelerate new unit builds to capture market share. So -- and the new unit sales usually are margin dilutive because it takes time to nurture the store until maturity. So that will also put some pressure on KFC restaurant margin.

And also, for Pizza Hut, we mentioned there are about 400 remodels that we have to do in the second half of the year. So that will also cause pressure on the top line and also the restaurant margin for Pizza Hut as well as Yum China.

Yes. But I mean, we have downward price volatility and we have dealt with inflation before, so we will just continue to identify like labor productivity to address cost of labor. And also, we'll work with our suppliers and also look at our product mix to improve our cost of sales.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Thank you, Jacky. For the -- maybe just a small point about the cost pressure on the delivery because of the very exciting growth in the business, that's one part of it. The other part is the delivery prices. Delivery -- the rider -- the rider cost, we probably remember earlier in the year, we talk about we are growing out Delivery 3.0 this year. And then from second half of the year, we are moving to the zone of having trade zone for the brand on a standalone basis. We'll do it one at a time, one trade zone at a time, because it's very detailed work. And next year, our plan is to look at multiple brand in the trade zone.

So we have very clear short-term and long-term trends how to look at the productivity of delivery rider while also emphasizing on the delivery quality, the on-time delivery, the complaint rate and the sales growth for the delivery business. So it's a holistic consideration other than just cost pressure. Thank you, Xiaopo.

Operator

And our next question comes from the line of Brian Bittner from Oppenheimer.

Michael A. Tamas ***Oppenheimer & Co. Inc., Research Division - Associate***

This is actually Mike Tamas on for Brian. I was wondering if you could just kind of talk about the Pizza Hut margins and what sort of changed there between the first quarter and the second quarter. You guys had similar sales trends, but the margin performance was much different. So just trying to figure out what happened there and what does that look going forward, excluding some of the pressure from the remodels that you were talking about, so just like the core margins and if you can kind of just address those.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Yes, Mike, I'll take your question. So the first question, like the difference between Q1 and Q2, so if you remember, Q1, we actually mentioned this. We have very low base in the year before. So particularly during Chinese New Year 2018, we have some labor inefficiency. So that's why the base was really low. And so the year-over-year improvement was quite significant. So I recall it was over 3.5 percentage points improvement in Q1 versus only about 2.2-percentage-point increase this quarter. And also, we actually initiate a lot of labor productivity initiatives in the second half of last year. And so we'll actually start lapping all these initiatives in the second quarter.

And also, if you recall, we are also continuing to invest a lot in promotional activities to drive traffic. So in terms of like the impacts of -- yes, in terms of food and paper, there was actually deflation of Pizza Hut, but that's offset by all the discount activities, the promotional activities and value campaigns such as Scream Wednesday because we want to continue to drive traffic and build on the value propositions.

And in terms of labor costs, also (inaudible) labor inflation and also because Pizza Hut delivery is growing, so that's also increased rider cost as well. And -- but I mean we have some occupancy savings like less depreciation at the store impairment. We have savings in utilities. So this kind of offset the margin pressure from inflation.

But looking ahead for the second half, I think generally speaking, I think keep in mind that the margin in the second half is typically lower than the first half. And also, we have a very clear and deliberate strategy to continue to drive traffic through promotional activities. So we'll continue to invest in our cost of sales, but this is part of our revitalization strategy to stabilize and restore traffic and sales and then we will work on profit.

So -- and we will continue to look for opportunities to reduce our operating cost and optimize our menu costs. So I think Joey touched on this earlier. We launched a new menu in late March, so that will actually optimize some of our menu costs as well. So that will impact -- offset some of the impact from the value promotion. Yes. But because as I mentioned, we have a lot of initiatives that were initiated in the second half of last year, so the -- we'll continue to have productivity, but the impact will diminish for sure in the second half.

Yes. So -- and also, I talked about this earlier. We are going to remodel about 400 stores in the second half, mostly coming in Q3 and Q4. And -- so -- and keep in mind, Q3 is actually our peak season. So that would put some pressure on our top line and also the restaurant margin.

Yes. But overall, in the long term, we are very confident, like the brand is moving in the right direction. We are -- we'll be able to restore the restaurant margin back to the prerevitalization level.

Operator

And your next question comes from the line of Lillian Lou from Morgan Stanley.

Lillian Lou *Morgan Stanley, Research Division - Executive Director*

I have a question on the store expansion plan because I think you mentioned earlier, we are accelerating the new unit expansion, and the guidance actually increased quite significantly to 800 to 850. So -- but I also note that during the CapEx guidance, increase was much less compared to the (inaudible) store expansion. So just trying to understand the rationale here because are we going to see smaller formats in the new store opening? And in terms of the store expansion plan, where are the majority of the new actual units going to be in the lower tier markets? So that's the question.

And then related to that, I think also, Joey mentioned the second half same-store sales growth may not see a similar rate, growth rate as in second Q and the first Q. And also, that's primarily because the pace and also remodeling. So for the new store expansion, if it's a smaller format, it's going to add in more in the portfolio. Does it also impact the same-store sales growth as well? So that's my question.

Jacky Lo *Yum China Holdings, Inc. - CFO & Treasurer*

Lillian, this is Jacky. Maybe I'll answer your question on new builds and CapEx, and then Joey can answer your question on same-store sales.

Yes. So -- yes, before I go into the change in our guidance, let me just first reiterate our store openings strategy. I mean we do not chase after specific number, but we will try to remain agile to respond to new opportunities or changing circumstances. And our new store development is driven by opportunities to sustainably grow the business while meeting our disciplined return requirement. And our new store openings depend on our site availability and also business performance. When we see digital opportunities, we'll definitely capitalize on those opportunities by asserting new store openings.

So as I mentioned on the last earnings call, a lot of the site availability will not be finalized until the second half of the year, and we typically have more visibility of the full year pipeline in the second half after our second quarter.

So based on the pipeline we have visibility on and also our brand performance right now, we anticipate 800 to 850 new stores for the year, up from the 600 to 650 we previously guide. But keep in mind that COFFii & JOY was not included in the original guidance. And so we are including our coffee brands store openings in the revised target. So for COFFii & JOY, we expect at least 50 this year.

And also, the incremental stores, they will be coming from multiple brands, but majority will be KFC. And our development team, they have shown very strong capability to open over 800 stores. We actually did that last year, but I will remain practical without sacrificing our discipline and profitability standards.

And in terms of the CapEx questions, so let me give you a breakdown. So we expect about $475 million to $525 million for the full year, and we have spent $212 million so far in the first half. So in terms of breakdown, including the 800 to 850 new store builds, also the store refurbishment, including the 500 Pizza Hut stores that we talked about, also technology investment and also selected real estate purchases, for example, logistics center, our restaurant sites and offices.

So over the years, I think I should point out, we have successfully opened more like smaller store format. And also in the process, we lowered the new store and remodel per store CapEx as well. And we also improved a lot of store opening and remodel efficiency. And also, there are a lot of numbers -- a lot of factors like timing and CapEx for remodel and all the other projects like technology or real estate. So after considering all this, that's why we expect to move into the final CapEx total that we are providing the guidance right now.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Thank you, Jacky. Lillian, thank you. For the new stores, particularly for KFC, the majority of the new store will be from lower tier cities still, although we continue to open new story in Tier 1, Tier 2 city as well because China is just such an exciting and huge market that the growth is everywhere. But it's simply because the fact that we have -- already have more stores in Tier 1, Tier 2 city, so now we are pushing to the lower tier cities.

And you're right to point out that we are quite open to the idea of the smaller stores now as well. It's not only the top tier city, in the lower tier city as well. Smaller store or lower CapEx that comes hand-in-hand, which also, think about it, smaller store also has smaller operating costs, and that helps the success rate for new store opening as well.

Because our new store opening, other than what Jacky has mentioned, is also a function of our sales, we don't have the luxury of opening the store for the sake of opening. So we want to open profitable store. So with improved sales and also with a bit better controlled CapEx, our success rate is a bit more predictable, and then we become more aggressive with new store openings. So it's all the very positive cycle going on right now.

Now when it comes to the same-store sales question, it's a bit different between KFC and Pizza Hut. Let me start with Pizza Hut. The Pizza Hut, as Jacky mentioned, we're going to have 400 store remodeling, and the biggest cost of remodeling, other than the CapEx actually is the lost sales or the lost same-store sales. So we have to put it into equation. But it's absolutely the right thing to do. And the theme of Pizza Hut is always -- in the last 2 years, it's always about doing something very fundamental, very important for the long-term growth of the business, but a bit painful right now or quite a bit painful for the time being. So the remodeling is 1 example. So that will put some pressure on the same-store sales.

And then KFC, because we have -- fortunately, we have gone a long way to remodel more than 80% of our stores in the last few years, we have -- get that challenge out of the way. Now we are moving to new store opening or even more new store opening. That's fantastic. But -- the but is when we open new store, there will be sales transfer. And the sales transfer indeed is a bit more in the lower tier city than the higher tier city simply because, again, the store base in lower tier city is less. And then the market is still maturing, so there will be some sales transfer. So that is the slightly dynamic on the same-store sales. Thank you very much, Lillian.

Operator

And our next question comes from the line of Chen Luo from Bank of America Merrill Lynch.

Chen Luo ***BofA Merrill Lynch, Research Division - MD***

I've got a follow-up question on the same-store sales growth. We understand because of high lap and other readers such as accelerated store expansion, we expect the same-store sales growth for KFC to moderate in second half. But if you look at the Q3 trend, in fact, last year, Q3 is not that high, but we still think that the same-store sales growth, it doesn't have to be moderate. Is there any other reason? Just now and last year, Jacky mentioned that we are going to be more productive with promotions in the second half. So does that suggest that from second half, we are going to take a more balanced approach between same-store sales growth and margin for the KFC business?

And also a related topic is on the quarter-to-date trend. I know that we are not offering up the guidance of the quarter-to-date trend, but we do notice that the company have introduced a lot of new products recently, including the Chuan Chuan product, which have already actually reaped a lot of attention among the local social media. Can you actually give more color on the new product pipeline in Q3 and the impact on the sales trend?

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Okay. Luo Chen, the line is not fantastic, so I just want to make sure that I got your question. The first question is about the same-store sales for KFC in Q3. Your question is the base last year was not so high, why we say we guide the moderate sales growth. And the second part of the question is the -- are the comments of the new product because of many media attention. So these are the 2 questions. Do I got it right?

Chen Luo ***BofA Merrill Lynch, Research Division - MD***

Yes, yes, yes. That's right.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Okay. Thank you, Luo Chen. One at a time, okay? When we look at the sales growth, same-store sales growth, we look at 2 years. So 2018 Q3, the same-store sales is -- was 1%, but 2017, it was 10%. So if we look at the last 2 years, it's very high base. So that's the number, the 2 years number.

And on top of that, the second half of last year, because of the high base, and we -- well, the 1% from growth kind of give our team a bit more challenges that push us to -- further to push for more marketing innovations. And that's the way that our team works these days.

So with the extra challenges and push, we came out with some really amazing value programs such as the Crazy Thursday -- and Scream Wednesday for Pizza Hut, Crazy Thursday for KFC. And the value focused on 1 day and the amount of food -- or the amount of innovative food that we can sell to customer and to cross-sell, et cetera, et cetera, was fantastic, and thus, all the good result bringing to the Q4 and then this year. So to lap the last 2 years Q3 for this particular year is actually very challenging, and thus, we are sharing with our shareholders.

When it comes to the new products, it's very exciting. KFC is not only about QSR, west food, it's just about good food. It's a wonderful restaurant platform that not only you get good food, good coffee, good drink, good breakfast, fantastic delivery. There's nothing wrong to sell very good fusion food as well.

For Q2, I talked a little bit about the fantastic products such as the double chili chicken, which is Jue Se Shuang Jiao in Chinese, that really comes from a very famous dish called Shuang Jiao Yu Tou double chili fish head. It's the same familiar flavor that we put into chicken, and that, of course, was very, very popular, but that's past.

Coming to Q3, of course, we are going to push out even more products. I cannot say too much for the second half of the year because we -- for whatever we've been selling, of course, you've been eating it already. It's cool, but for those we have not launched yet, unfortunately, this is China. I don't know how long it would take smaller competitors to launch their product ahead of us given the much smaller scales. So unfortunately, I can't. But I can give a little bit of example. For example, other than the exciting chicken, we always have very exciting new flavor chicken, for the second half of the year, we launched Okayama peach ice cream, right? That is just a bit specific. But that's the theme. So next -- for the second half, similar exciting ice cream and then the chicken.

And then burger, we'll continue the burger line as well. So we have a lot of exciting and successful LTO for the first half of the year, and we'll consolidate the learning. And along the similar theme, because this is quite predictable, once you've got the theme, you know what this is -- what customer wants, and then we do more variation. And this is quite a sort of predictable track that we can pursue to make sure we offer something very good for the customer and yet it's different. So burger is an underlying. We launched the premium burger, basically, the import beef burger and salted egg yolk shrimp burger. So these burger are sold at RMB 25. We never sold burger at such high price. RMB 25 is very high price that we price, but they are very popular, and guess what, we're going to continue. And it will continue, continue the LTO, then it might have a chance to get on our permanent menu.

So a lot of amazing product coming. And we have -- typically have 12 months pipeline already in our plan because given the scale of the business, if we don't have the plan, we are not doing a good job. Similar idea for Pizza Hut, but the pipeline for Pizza Hut is coming.

Just to advertise, Pizza Hut this week, we are selling Canadian snow crab pizza, fantastic. So when I get to talk about product, I got very excited. So thanks, Luo Chen.

Operator

And our next question comes from the line of Sara Senatore from Bernstein.

Sara Harkavy Senatore ***Sanford C. Bernstein & Co., LLC., Research Division - Senior Research Analyst***

I got a question about delivery sales. I think you pointed to it a couple of times as a headwind for margins, but if I look at your delivery sales mix, they've been pretty stable at Pizza Hut in the mid-20% for the last 6 quarters, and it seems to be stabilizing in the high teens. KFC, is brilliant just for a couple of quarters now. So I guess I'm trying to understand what gives you confidence that it will continue to grow and be a sales driver. And then conversely, is there a potential that your margin guidance is conservative? Because we aren't seeing quite the rapid mix shift towards delivery that you had seen in perhaps recent quarters.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Okay. Let me talk about the sales and Jacky can talk about the margins. The delivery sales is very exciting part of the business. So KFC first and then Pizza Hut.

So let's say if KFC delivery is a standalone business, actually, by the end of the year, it's likely to be a business with probably USD 1 billion revenue, $1 billion revenue, if KFC delivery is a standalone business. It's growing very, very nicely. And right now, we have more exciting learning about deliveries for the first half of the year. Not only the own channel growth is growing faster than the aggregator. So KFC, the own channel -- the traffic from our own channel is already over 40%, and that's very exciting because we are actually driving the business ourself through our own APP, et cetera.

On top of that, when we look at the growth of breakfast, the coffee late night or even dessert, it becomes very powerful when we combine the digital database knowledge about these particular category with delivery. So we can use delivery to drive the growth of these new category or new daypart. Not new, like emerging, growing daypart. So when we look at the digital bit of the business this year, our CRM business, when we sell the subscription membership, we combine breakfast and delivery, we combine coffee and delivery. So it's not only growing very nicely, but it's also growing other daypart as well. Therefore, for KFC, the delivery sales is really fantastic, and it will be a -- in the foreseeable future, it will continue to be a very important part of our business.

And all of this growth, of course, have something fundamental underneath that's called the building blocks, the fundamental building blocks with our riders, with our management, our trade zones, et cetera, et cetera. So that also explains the difference of growth of Pizza Hut, because Pizza Hut, only by late last year, we took back the last-mile delivery. And right now, we are still working on the building blocks of the Pizza Hut delivery business. So it's a bit -- not late, but it's a bit behind the KFC core capability, the delivery core capability. So Pizza Hut, we're working on the fundamentals, and we understand it's painful in the short term, but it's absolutely the right thing to do. But it's still growing very nicely. And again, the growth from our own channel is still growing much faster than the aggregators. The percentage of the sales from Pizza Hut own channel was 20% before, but now it's more like 27%. It's 6% to 7% growth compared to the quarter before. So we're happy with the progress as well in terms of the Pizza Hut delivery on both margins.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Okay. Thank you, Joey. Sara, your question on delivery on impacts on margin, well, first of all, as Joey mentioned, it's a key growth driver for our business, and because it's growing so fast, it actually generates incremental revenue and profit at this point. And so we look at delivery as a long-term growth trend for the industry. And from our perspective, we always talk about like the future of the restaurant business, it will be a combination of offline assets and online system.

So in a way, delivery and dining, they are 2 inseparable segments of the same business. But if you look at the dining and delivery business separately, so from a cost perspective, so there are additional like rider costs, packaging costs, these are incremental for delivery. But we also receive a delivery fee to offset that. But overall, it's still slightly margins dilutive to the -- versus dine-in.

So -- but we look at initiatives to improve efficiency and lower the rider costs. So for example, we roll out the Dispatch 3.0 system. So we are testing the trade zone-based delivery right now in certain cities. And towards the end of the year, we'll also test maybe sharing the delivery across multiple brands. So these are all the way to naturally improve efficiency and lower the cost on margin. But at this point, delivery is still slightly margin dilutive to the business.

Operator

And our last question comes from the line of Christine Peng from UBS.

Yan Peng ***UBS Investment Bank, Research Division - Executive Director & China Consumer Staples Sector Analyst***

I just have very quick question regarding Pizza Hut. So Jacky mentioned earlier that you are expecting Pizza Hut profitability to go back to the prerevitalization level. So given the turnaround for Pizza Hut has been happening for 2 quarters, so should we expect this kind of profitability for the year of 2019 or 2020? I just want to get a clear idea as we got to the time table for Pizza Hut to go back to the previous profitability.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Yes, Christine, we actually touched on this during the Investor Day as well. We never really put a time table on it. I mean we talk about it's a step-by-step process for the revitalization of Pizza Hut. So the first step is stabilizing traffic and then we'll drive sales, and the last step will be profit. So in the first half of the year, that's a year-over-year increase in the margin, but I already talked about some of the headwinds earlier. So we have all this remodeling. So we are lapping a lot of labor initiatives in the second half. So right now, the focus, at least for this year and next year, will still invest in value propositions to drive traffic and sales. So that's the immediate focus for the brand.

Florence Lip ***Yum China Holdings, Inc. - Senior Director of IR***

Thank you. All right. Operator, thank you very much. Thank you, everyone, for joining the call today. We look forward to speaking with you again, and that concludes today's call. Have a great day. Thank you very much.

Joey Wat ***Yum China Holdings, Inc. - CEO & Director***

Thank you, all.

Jacky Lo ***Yum China Holdings, Inc. - CFO & Treasurer***

Thank you.

Operator

And that does conclude the conference for today. Thank you for participating. You may all disconnect. Speakers, please stand by.