

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D. C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2022

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission file number 001-37762

Yum China Holdings, Inc.

(Exact Name of Registrant as Specified in Its Charter)

Delaware
(State or Other Jurisdiction of
Incorporation or Organization)

**7100 Corporate Drive
Plano, Texas 75024
United States of America**

81-2421743
(I.R.S. Employer
Identification No.)

**Yum China Building
20 Tian Yao Qiao Road
Shanghai 200030
People's Republic of China**

(Address, Including Zip Code, of Principal Executive Offices)

(469) 980-2898

(Registrant's Telephone Number, Including Area Code)

Not Applicable

(Former Name, Former Address and Former Fiscal Year, if Changed Since Last Report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, par value \$0.01 per share	YUMC	New York Stock Exchange
	9987	The Stock Exchange of Hong Kong Limited

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of shares outstanding of the registrant's common stock as of November 3, 2022 was 418,427,345 shares.

INDEX

	<u>Page No.</u>
Part I. Financial Information	
Item 1 – Financial Statements	3
Condensed Consolidated Statements of Income – Quarters and Years to Date Ended September 30, 2022 and 2021 (Unaudited)	3
Condensed Consolidated Statements of Comprehensive Income – Quarters and Years to Date Ended September 30, 2022 and 2021 (Unaudited)	4
Condensed Consolidated Statements of Cash Flows – Years to Date Ended September 30, 2022 and 2021 (Unaudited)	5
Condensed Consolidated Balance Sheets – September 30, 2022 (Unaudited) and December 31, 2021	6
Notes to Condensed Consolidated Financial Statements (Unaudited)	7
Item 2 – Management’s Discussion and Analysis of Financial Condition and Results of Operations	26
Item 3 – Quantitative and Qualitative Disclosures About Market Risk	42
Item 4 – Controls and Procedures	43
Part II. Other Information	
Item 1 – Legal Proceedings	44
Item 1A – Risk Factors	44
Item 2 – Unregistered Sales of Equity Securities and Use of Proceeds	46
Item 6 – Exhibits	47
Signatures	48

Item 1. Financial Statements

Condensed Consolidated Statements of Income (Unaudited)

Yum China Holdings, Inc.

(in US\$ millions, except per share data)

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Revenues				
Company sales	\$ 2,561	\$ 2,310	\$ 7,135	\$ 6,874
Franchise fees and income	22	40	65	120
Revenues from transactions with franchisees and unconsolidated affiliates	80	184	219	519
Other revenues	22	20	62	49
Total revenues	2,685	2,554	7,481	7,562
Costs and Expenses, Net				
Company restaurants				
Food and paper	787	743	2,206	2,133
Payroll and employee benefits	603	591	1,819	1,675
Occupancy and other operating expenses	691	694	2,034	1,995
Company restaurant expenses	2,081	2,028	6,059	5,803
General and administrative expenses	157	142	449	408
Franchise expenses	9	17	27	50
Expenses for transactions with franchisees and unconsolidated affiliates	76	180	212	509
Other operating costs and expenses	18	17	53	41
Closures and impairment expenses, net	4	2	20	13
Other expenses (income), net	24	(10)	73	(15)
Total costs and expenses, net	2,369	2,376	6,893	6,809
Operating Profit	316	178	588	753
Interest income, net	25	16	51	47
Investment loss	(15)	(39)	(32)	(43)
Income Before Income Taxes and Equity in				
Net Earnings (Losses) from Equity Method Investments	326	155	607	757
Income tax provision	(97)	(44)	(183)	(210)
Equity in net earnings (losses) from equity method investments	(2)	—	(4)	—
Net income – including noncontrolling interests	227	111	420	547
Net income – noncontrolling interests	21	7	31	32
Net Income – Yum China Holdings, Inc.	\$ 206	\$ 104	\$ 389	\$ 515
Weighted-average common shares outstanding (in millions):				
Basic	420	422	422	421
Diluted	424	435	426	435
Basic Earnings Per Common Share	\$ 0.49	\$ 0.25	\$ 0.92	\$ 1.23
Diluted Earnings Per Common Share	\$ 0.49	\$ 0.24	\$ 0.92	\$ 1.19

See accompanying Notes to Condensed Consolidated Financial Statements.

Condensed Consolidated Statements of Comprehensive Income (Unaudited)

Yum China Holdings, Inc.

(in US\$ millions)

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Net income – including noncontrolling interests	\$ 227	\$ 111	\$ 420	\$ 547
Other comprehensive (loss) income, net of tax of nil:				
Foreign currency translation adjustments	(306)	10	(573)	50
Comprehensive (loss) income – including noncontrolling interests	(79)	121	(153)	597
Comprehensive (loss) income – noncontrolling interests	(23)	9	(52)	36
Comprehensive (Loss) Income – Yum China Holdings, Inc.	<u>\$ (56)</u>	<u>\$ 112</u>	<u>\$ (101)</u>	<u>\$ 561</u>

See accompanying Notes to Condensed Consolidated Financial Statements.

Condensed Consolidated Statements of Cash Flows (Unaudited)

Yum China Holdings, Inc.

(in US\$ millions)

	Year to Date Ended	
	9/30/2022	9/30/2021
Cash Flows – Operating Activities		
Net income – including noncontrolling interests	\$ 420	\$ 547
Depreciation and amortization	467	380
Non-cash operating lease cost	333	310
Closures and impairment expenses	20	13
Gain from re-measurement of equity interest upon acquisition	—	(10)
Investment loss	32	43
Equity income from investments in unconsolidated affiliates	—	(38)
Distributions of income received from unconsolidated affiliates	7	21
Deferred income taxes	(7)	17
Share-based compensation expense	31	32
Changes in accounts receivable	(6)	2
Changes in inventories	71	13
Changes in prepaid expenses, other current assets and VAT assets (Note 9(a))	216	—
Changes in accounts payable and other current liabilities	(19)	82
Changes in income taxes payable	70	(5)
Changes in non-current operating lease liabilities	(299)	(309)
Other, net	(7)	(24)
Net Cash Provided by Operating Activities	<u>1,329</u>	<u>1,074</u>
Cash Flows – Investing Activities		
Capital spending	(509)	(482)
Purchases of short-term investments	(4,290)	(4,524)
Purchases of long-term time deposits	—	(25)
Maturities of short-term investments	4,226	4,544
Acquisition of business, net of cash acquired	(23)	—
Acquisition of equity investment	—	(261)
Other, net	3	5
Net Cash Used in Investing Activities	<u>(593)</u>	<u>(743)</u>
Cash Flows – Financing Activities		
Repurchase of shares of common stock	(411)	(32)
Cash dividends paid on common stock	(152)	(152)
Dividends paid to noncontrolling interests	(29)	(22)
Contribution from noncontrolling interests	18	—
Payment of acquisition related holdback	(7)	(8)
Other, net	(2)	(6)
Net Cash Used in Financing Activities	<u>(583)</u>	<u>(220)</u>
Effect of Exchange Rates on Cash, Cash Equivalents and Restricted Cash	<u>(78)</u>	<u>9</u>
Net Increase in Cash, Cash Equivalents and Restricted Cash	75	120
Cash, Cash Equivalents and Restricted Cash – Beginning of Period	1,136	1,158
Cash, Cash Equivalents and Restricted Cash – End of Period	<u>\$ 1,211</u>	<u>\$ 1,278</u>
Supplemental Cash Flow Data		
Cash paid for income tax	124	210
Non-cash Investing and Financing Activities		
Capital expenditures included in accounts payable and other current liabilities	133	208

See accompanying Notes to Condensed Consolidated Financial Statements.

Condensed Consolidated Balance Sheets

Yum China Holdings, Inc.

(in US\$ millions)

	<u>9/30/2022</u>	<u>12/31/2021</u>
	(Unaudited)	
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 1,211	\$ 1,136
Short-term investments	2,826	2,860
Accounts receivable, net	66	67
Inventories, net	321	432
Prepaid expenses and other current assets	286	221
Total Current Assets	<u>4,710</u>	<u>4,716</u>
Property, plant and equipment, net	1,965	2,251
Operating lease right-of-use assets	2,154	2,612
Goodwill	1,927	2,142
Intangible assets, net	176	272
Investments in unconsolidated affiliates	256	292
Deferred income tax assets	89	106
Other assets	419	832
Total Assets	<u>\$ 11,696</u>	<u>\$ 13,223</u>
LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	\$ 1,992	\$ 2,332
Income taxes payable	112	51
Total Current Liabilities	<u>2,104</u>	<u>2,383</u>
Non-current operating lease liabilities	1,862	2,286
Non-current finance lease liabilities	36	40
Deferred income tax liabilities	370	425
Other liabilities	156	167
Total Liabilities	<u>4,528</u>	<u>5,301</u>
Redeemable Noncontrolling Interest	13	14
Equity		
Common stock, \$0.01 par value; 1,000 million shares authorized; 419 million shares and 449 million shares issued at September 30, 2022 and December 31, 2021, respectively; 419 million shares and 428 million shares outstanding at September 30, 2022 and December 31, 2021, respectively	4	4
Treasury stock	—	(803)
Additional paid-in capital	4,408	4,695
Retained earnings	2,228	2,892
Accumulated other comprehensive (loss) income	(222)	268
Total Yum China Holdings, Inc. Stockholders' Equity	<u>6,418</u>	<u>7,056</u>
Noncontrolling interests	737	852
Total Equity	<u>7,155</u>	<u>7,908</u>
Total Liabilities, Redeemable Noncontrolling Interest and Equity	<u>\$ 11,696</u>	<u>\$ 13,223</u>

See accompanying Notes to Condensed Consolidated Financial Statements.

Notes to Condensed Consolidated Financial Statements (Unaudited)

(Tabular amounts in US\$ millions, except as otherwise noted)

Note 1 – Description of Business

Yum China Holdings, Inc. (“Yum China” and, together with its subsidiaries, the “Company,” “we,” “us” and “our”) was incorporated in Delaware on April 1, 2016.

The Company owns, franchises or has ownership in entities that own and operate restaurants (also referred to as “stores” or “units”) under the KFC, Pizza Hut, Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY and Taco Bell concepts (collectively, the “concepts”). In connection with the separation of the Company in 2016 from its former parent company, YUM! Brands, Inc. (“YUM”), a master license agreement was entered into between Yum Restaurants Consulting (Shanghai) Company Limited (“YCCL”), a wholly-owned indirect subsidiary of the Company, and YUM, through YRI China Franchising LLC, a subsidiary of YUM, effective from January 1, 2020 and previously through Yum! Restaurants Asia Pte. Ltd., another subsidiary of YUM, from October 31, 2016 to December 31, 2019. Pursuant to the master license agreement, we are the exclusive licensee of KFC, Pizza Hut and, subject to achieving certain agreed-upon milestones as amended in April 2022, Taco Bell brands and their related marks and other intellectual property rights for restaurant services in the People’s Republic of China (the “PRC” or “China”), excluding Hong Kong, Macau and Taiwan. The term of the license is 50 years from October 31, 2016 for the KFC and Pizza Hut brands and, subject to achieving certain agreed-upon milestones, 50 years from April 15, 2022 for the Taco Bell brand, with automatic renewals for additional consecutive renewal terms of 50 years each, subject only to YCCL being in “good standing” and unless YCCL gives notice of its intent not to renew. In exchange, we pay a license fee to YUM equal to 3% of net system sales from both our Company and franchise restaurants. We own the intellectual property of Little Sheep, Huang Ji Huang and COFFii & JOY, and pay no license fee related to these concepts.

In the second quarter of 2020, the Company partnered with Luigi Lavazza S.p.A. (“Lavazza Group”), the world renowned family-owned Italian coffee company, and entered into a joint venture to explore and develop the Lavazza coffee shop concept in China. In September 2021, the Company and Lavazza Group entered into agreements for the previously formed joint venture (“Lavazza joint venture”) to accelerate the expansion of Lavazza coffee shops in China. Upon execution of these agreements, the Company controls and consolidates the joint venture with its 65% equity interest. The acquisition was considered immaterial.

During the fourth quarter of 2021, the Company completed its investment of a 28% equity interest in Hangzhou Catering Service Group (“Hangzhou Catering”), for cash consideration of \$255 million. Upon closing, the Company directly and indirectly holds an approximately 60% equity interest in the Hangzhou KFC joint venture that operates KFC stores in and around Hangzhou, China (“Hangzhou KFC”), allowing the Company to consolidate Hangzhou KFC. The acquisition was considered immaterial.

As part of our strategy to drive growth from off-premise occasions, we have also developed our own retail brand operations, SoulFun, since 2018, which sells ready meals such as steak, fried rice and pasta through online and offline channels. The operating results of SoulFun are included in our e-commerce business operating segment.

The Company has two reportable segments: KFC and Pizza Hut. Our remaining operating segments, including the operations of Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY, Taco Bell, East Dawning, Daojia and our e-commerce business, are combined and referred to as All Other Segments, as those operating segments are insignificant both individually and in the aggregate. East Dawning was severely impacted by the COVID-19 pandemic. As a result, the Company decided to wind down the operations of East Dawning brand in 2021, and closed all East Dawning units in China by March 2022. In addition, the Company decided to wind down the operations of COFFii & JOY by the end of 2022. The Company will leverage its experience in COFFii & JOY to better capture growing coffee market opportunities in China. Additional details on our reportable operating segments are included in Note 14.

The Company’s common stock is listed on the New York Stock Exchange (“NYSE”) under the symbol “YUMC”. On September 10, 2020, the Company completed a secondary listing of its common stock on the Main Board of the Hong Kong Stock Exchange (“HKEX”) under the stock code “9987”, in connection with a global offering of 41,910,700 shares of its common stock. Net proceeds raised by the Company from the global offering after deducting underwriting fees and the offering expenses amounted to \$2.2 billion. On October 24, 2022, the Company’s voluntary conversion of its secondary listing status to a primary listing status on the HKEX became effective (“Primary Conversion”). On the same day, the Company’s shares of common stock traded on the HKEX was included in the Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect. Yum China is now a dual primary listed company on the NYSE and HKEX. The Company’s common stock listed on the two exchanges will continue to be fully fungible.

Note 2 – Basis of Presentation

Our preparation of the accompanying Condensed Consolidated Financial Statements in conformity with Generally Accepted Accounting Principles in the United States of America (“GAAP”) requires us to make estimates and assumptions that affect reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates.

We have prepared the Condensed Consolidated Financial Statements in accordance with the rules and regulations of the Securities and Exchange Commission (the “SEC”) for interim financial information. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. The Condensed Consolidated Financial Statements include all normal and recurring adjustments considered necessary to present fairly our financial position as of September 30, 2022, our results of operations and comprehensive income for the quarters and years to date ended September 30, 2022 and 2021, and cash flows for the years to date ended September 30, 2022 and 2021. Our results of operations, comprehensive income and cash flows for these interim periods are not necessarily indicative of the results to be expected for the full year. These statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K as filed with the SEC on February 28, 2022.

Through the acquisition of Daojia, the Company also acquired a variable interest entity (“VIE”) and subsidiaries of the VIE effectively controlled by Daojia. There exists a parent-subsidiary relationship between Daojia and its VIE as a result of certain exclusive agreements that require Daojia to consolidate its VIE and subsidiaries of the VIE because Daojia is the primary beneficiary that possesses the power to direct the activities of the VIE that most significantly impact its economic performance, and is entitled to substantially all of the profits and has the obligation to absorb all of the expected losses of the VIE. The acquired VIE and its subsidiaries were considered immaterial, both individually and in the aggregate. The results of Daojia’s operations have been included in the Company’s Condensed Consolidated Financial Statements since the acquisition date.

The results of the Lavazza joint venture and Hangzhou KFC’s operations have been included in the Company’s Condensed Consolidated Financial Statements since the respective acquisition dates.

Certain comparative items in the Condensed Consolidated Financial Statements have been reclassified to conform to the current period’s presentation to facilitate comparison.

Recently Adopted Accounting Pronouncements

In August 2020, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2020-06, *Debt — Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging — Contracts in Entity’s Own Equity (Subtopic 815-40)* (“ASU 2020-06”), which eliminates two of the three models in ASC 470-20 that require separate accounting for embedded conversion features and eliminates some of the conditions for equity classification in ASC 815-40 for contracts in an entity’s own equity. The guidance also requires entities to use the if-converted method for all convertible instruments in the diluted earnings per share calculation and generally requires them to include the effect of share settlement for instruments that may be settled in cash or shares. We adopted this standard on January 1, 2022, and such adoption did not have a material impact on our financial statements.

In May 2021, the FASB issued ASU 2021-04, *Issuer’s Accounting for Certain Modifications or Exchanges of Freestanding Equity-Classified Written Call Options* (“ASU 2021-04”). It requires issuers to account for a modification or exchange of freestanding equity-classified written call options that remain equity-classified after the modification or exchange based on the economic substance of the modification or exchange. We adopted this standard on January 1, 2022, and such adoption did not have a material impact on our financial statements.

In July 2021, the FASB issued ASU 2021-05, *Lessors — Certain Leases with Variable Lease* (“ASU 2021-05”). It requires lessors to classify leases as operating leases if they have variable lease payments that do not depend on an index or rate and would have selling losses if they were classified as sales-type or direct financing leases. We adopted this standard on January 1, 2022, and such adoption did not have a material impact on our financial statements.

Note 3 – Business Acquisitions and Equity Investments

Consolidation of Hangzhou KFC and Equity Investment in Hangzhou Catering

During the fourth quarter of 2021, the Company completed its investment of a 28% equity interest in Hangzhou Catering for total consideration of approximately \$255 million. Hangzhou Catering holds a 45% equity interest in Hangzhou KFC, of which the Company previously held a 47% equity interest. Along with the investment, the Company also obtained two additional seats on the board of directors of Hangzhou KFC. Upon completion of the transaction, the Company directly and indirectly holds an approximately 60% equity interest in Hangzhou KFC and has majority representation on its board of directors, and thus obtained control over Hangzhou KFC and started to consolidate its results from the acquisition date.

As a result of the acquisition of Hangzhou KFC, \$66 million of the purchase price was allocated to the reacquired franchise right, which is amortized over the remaining franchise contract period of 1 year.

In addition to its equity interest in Hangzhou KFC, Hangzhou Catering operates approximately 60 Chinese dining restaurants under four time-honored brands and a food processing business. The Company applies the equity method of accounting to the 28% equity interest in Hangzhou Catering excluding the Hangzhou KFC business and classified this investment in Investment in unconsolidated affiliates based on its then fair value. The Company elected to report its share of Hangzhou Catering's financial results with a one-quarter lag because its results are not available in time for the Company to record them in the concurrent period. The Company's equity loss from Hangzhou Catering, net of taxes, was immaterial for both the quarter and year to date ended September 30, 2022, which was included in Equity in net earnings (losses) from equity method investments in our Condensed Consolidated Statement of Income. As of September 30, 2022, the carrying amount of the Company's equity method investment in Hangzhou Catering was \$35 million, exceeding the Company's interest in Hangzhou Catering's underlying net assets by \$26 million. Substantially all of this difference was attributable to its self-owned properties and impact of related deferred tax liabilities determined upon acquisition, which is being depreciated over a weighted-average remaining useful life of 20 years.

Consolidation of Lavazza Joint Venture

In April 2020, the Company and Lavazza Group established the Lavazza joint venture to explore and develop the Lavazza coffee shop concept in China, with equity ownership of 65% and 35%, respectively. The Company accounted for the Lavazza joint venture under the equity method of accounting because Lavazza Group held substantive participating rights on certain significant financial and operating decisions. In September 2021, the Company and Lavazza Group entered into agreements for the joint venture, whereby substantive participating rights previously held by Lavazza Group were removed, and thus the Company obtained control over the joint venture and started to consolidate its results from the acquisition date.

As a result of the consolidation of the Lavazza joint venture, the Company also recognized a gain of \$10 million in the third quarter of 2021 from the re-measurement of our previously held equity interest at fair value. The gain was recorded in Other expenses (income), net and not allocated to any segment for performance reporting purposes.

Fujian Sunner Development Co., Ltd. ("Sunner") Investment

In the first quarter of 2021, the Company acquired a 5% equity interest in Sunner, a Shenzhen Stock Exchange-listed company, for total consideration of approximately \$261 million. Sunner is China's largest white-feathered chicken producer and the Company's largest poultry supplier.

The Company accounted for the equity securities at fair value based on their closing market price on each measurement date, with subsequent fair value changes recorded in our Condensed Consolidated Statements of Income. The unrealized loss of \$22 million was included in Investment gain or loss in our Condensed Consolidated Statements of Income for the year to date ended September 30, 2021, representing changes in fair value before the equity method of accounting was applied.

In May 2021, a senior executive of the Company was nominated and appointed to Sunner’s board of directors upon Sunner’s shareholder approval. Through this representation, the Company participates in Sunner’s policy making process. The representation on Sunner’s board, along with the Company being one of Sunner’s significant shareholders, provides the Company with the ability to exercise significant influence over the operating and financial policies of Sunner. As a result, the Company started to apply the equity method of accounting to the investment and reclassified this investment from Other assets to Investment in unconsolidated affiliates in May 2021 based on its then fair value. The Company elected to report its share of Sunner’s financial results with a one-quarter lag because Sunner’s results are not available in time for the Company to record them in the concurrent period. In the quarter and year to date ended September 30, 2022, the Company's equity loss from Sunner, net of taxes, was immaterial, which was included in Equity in net earnings (losses) from equity method investments in our Condensed Consolidated Statement of Income.

Since Sunner became the Company’s unconsolidated affiliate in May 2021, the Company purchased inventories of \$125 million and \$198 million from Sunner for the quarter and year to date ended September 30, 2021. The Company purchased inventories of \$116 million and \$307 million for the quarter and year to date ended September 30, 2022, respectively. The Company’s accounts payable and other current liabilities due to Sunner were \$44 million and \$56 million as of September 30, 2022 and December 31, 2021, respectively.

As of September 30, 2022, the carrying amount of the Company’s investment in Sunner was \$219 million, exceeding the Company’s interest in Sunner’s underlying net assets by \$153 million. Of this basis difference, \$17 million was related to finite-lived intangible assets determined upon acquisition, which are being amortized over estimated useful life of 20 years. The remaining differences were related to goodwill and indefinite-lived intangible assets, which are not subject to amortization, as well as deferred tax liabilities impact. As of September 30, 2022, the market value of the Company’s investment in Sunner was \$169 million based on its quoted closing price.

Meituan Dianping (“Meituan”) Investment

In the third quarter of 2018, the Company subscribed for 8.4 million, or less than 1%, of the ordinary shares of Meituan, an e-commerce platform for services in China, for total consideration of approximately \$74 million, when it launched its initial public offering on the HKEX in September 2018. In the second quarter of 2020, the Company sold 4.2 million of the ordinary shares of Meituan.

The Company accounts for the equity securities at fair value with subsequent fair value changes recorded in our Condensed Consolidated Statements of Income. The fair value of the investment in Meituan is determined based on the closing market price for the shares at the end of each reporting period. The fair value change, to the extent the closing market price of shares of Meituan as of the end of reporting period is higher than our cost, is subject to U.S. tax.

A summary of pre-tax gains or losses on investment in equity securities of Meituan recognized, which was included in Investment gain or loss in our Condensed Consolidated Statements of Income, is as follows:

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Unrealized losses recorded on equity securities still held as of the end of the period	\$ (15)	\$ (41)	\$ (33)	\$ (27)

Note 4 – Revenue Recognition

The Company’s revenues primarily include Company sales, Franchise fees and income and Revenues from transactions with franchisees and unconsolidated affiliates.

Company Sales

Revenues from Company-owned restaurants are recognized when a customer takes possession of the food and tenders payment, which is when our obligation to perform is satisfied. The Company presents sales net of sales-related taxes. We also offer our customers delivery through both our own mobile applications and third-party aggregators' platforms. For delivery orders placed through our mobile applications, we use our dedicated riders, while for orders placed through third-party aggregators' platforms, we either used our dedicated riders or third-party aggregators' delivery staff in the past. With respect to delivery orders delivered by our dedicated riders, we control and determine the price for the delivery service and generally recognize revenue, including delivery fees, when a customer takes possession of the food. When orders are fulfilled by the delivery staff of third-party aggregators, who control and determine the price for the delivery service, we recognize revenue, excluding delivery fees, when control of the food is transferred to the third-party aggregators' delivery staff. The payment terms with respect to these sales are short-term in nature. Starting in 2019, we use our own dedicated riders to deliver orders placed through aggregators' platforms to customers of KFC and Pizza Hut stores.

We recognize revenues from prepaid stored-value products, including gift cards and product vouchers, when they are redeemed by the customer. Prepaid gift cards sold at any given point generally expire over the next 36 months, and product vouchers generally expire over a period of up to 12 months. We recognize breakage revenue, which is the amount of prepaid stored-value products that is not expected to be redeemed, either (1) proportionally in earnings as redemptions occur, in situations where the Company expects to be entitled to a breakage amount, or (2) when the likelihood of redemption is remote, in situations where the Company does not expect to be entitled to breakage, provided that there is no requirement for remitting balances to government agencies under unclaimed property laws. The Company reviews its breakage estimates at least annually based upon the latest available information regarding redemption and expiration patterns.

Our privilege membership programs offer privilege members rights to multiple benefits, such as free delivery and discounts on certain products. For certain KFC and Pizza Hut privilege membership programs offering a pre-defined amount of benefits that can be redeemed ratably over the membership period, revenue is ratably recognized over the period based on the elapse of time. With respect to the KFC and Pizza Hut family privilege membership program offering members a mix of distinct benefits, including a welcome gift and assorted discount coupons with pre-defined quantities, consideration collected is allocated to the benefits provided based on their relative standalone selling price and revenue is recognized when food or services are delivered or the benefits expire. In determining the relative standalone selling price of the benefits, the Company considers likelihood of future redemption based on historical redemption pattern and reviews such estimates periodically based upon the latest available information regarding redemption and expiration patterns.

Franchise Fees and Income

Franchise fees and income primarily include upfront franchise fees, such as initial fees and renewal fees, and continuing fees. We have determined that the services we provide in exchange for upfront franchise fees and continuing fees are highly interrelated with the franchise right. We recognize upfront franchise fees received from a franchisee as revenue over the term of the franchise agreement or the renewal agreement because the franchise rights are accounted for as rights to access our symbolic intellectual property. The franchise agreement term is generally 10 years for KFC and Pizza Hut, five or 10 years for Little Sheep and three or 10 years for Huang Ji Huang. We recognize continuing fees, which are based upon a percentage of franchisee sales, as those sales occur.

Revenues from Transactions with Franchisees and Unconsolidated Affiliates

Revenues from transactions with franchisees and unconsolidated affiliates consist primarily of sales of food and paper products, advertising services and other services provided to franchisees and unconsolidated affiliates that operate our concepts.

The Company centrally purchases substantially all food and paper products from suppliers for substantially all of our restaurants, including franchisees and unconsolidated affiliates that operate our concepts, and then sells and delivers them to the restaurants. In addition, the Company owns seasoning facilities for its Chinese dining business unit, which manufacture and sell seasoning products to Huang Ji Huang and Little Sheep franchisees. The performance obligation arising from such transactions is considered distinct from the franchise agreement as it is not highly dependent on the franchise agreement and the customer can benefit from the procurement service on its own. We consider ourselves the principal in this arrangement as we have the ability to control a promised good or service before transferring that good or service to the franchisees and unconsolidated affiliates that operate our concepts. Revenue is recognized upon transfer of control over ordered items, generally upon delivery to the franchisees and unconsolidated affiliates.

For advertising services, the Company often engages third parties to provide services and acts as a principal in the transaction based on our responsibilities of defining the nature of the services and administering and directing all marketing and advertising programs in accordance with the provisions of our franchise agreements. The Company collects advertising contributions, which are generally based on certain percentage of sales from substantially all of our restaurants, including franchisees and unconsolidated affiliates. Other services provided to franchisees and unconsolidated affiliates consist primarily of customer and technology support services. Advertising services and other services provided are highly interrelated to franchise right, and are not considered individually distinct. We recognize revenue when the related sales occur.

Loyalty Programs

Each of the Company's KFC and Pizza Hut reportable segments operates a loyalty program that allows registered members to earn points for each qualifying purchase. Points, which generally expire 18 months after being earned, may be redeemed for future purchases of KFC or Pizza Hut branded products or other products for free or at a discounted price. Points cannot be redeemed or exchanged for cash. The estimated value of points earned by the loyalty program members is recorded as a reduction of revenue at the time the points are earned, based on the percentage of points that are projected to be redeemed, with a corresponding deferred revenue liability included in Accounts payable and other current liabilities on the Condensed Consolidated Balance Sheets and subsequently recognized into revenue when the points are redeemed or expire. The Company estimates the value of the future redemption obligations based on the estimated value of the product for which points are expected to be redeemed and historical redemption patterns and reviews such estimates periodically based upon the latest available information regarding redemption and expiration patterns.

Disaggregation of Revenue

The following tables present revenue disaggregated by types of arrangements and segments:

Quarter Ended 9/30/2022							
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 1,992	\$ 556	\$ 13	\$ —	\$ 2,561	\$ —	\$ 2,561
Franchise fees and income	15	2	5	—	22	—	22
Revenues from transactions with franchisees and unconsolidated affiliates	9	1	11	59	80	—	80
Other revenues	1	2	157	12	172	(150)	22
Total revenues	\$ 2,017	\$ 561	\$ 186	\$ 71	\$ 2,835	\$ (150)	\$ 2,685

Quarter Ended 9/30/2021							
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 1,750	\$ 546	\$ 14	\$ —	\$ 2,310	\$ —	\$ 2,310
Franchise fees and income	32	2	6	—	40	—	40
Revenues from transactions with franchisees and unconsolidated affiliates	17	2	26	139	184	—	184
Other revenues	2	1	88	7	98	(78)	20
Total revenues	\$ 1,801	\$ 551	\$ 134	\$ 146	\$ 2,632	\$ (78)	\$ 2,554

Year to Date Ended 9/30/2022							
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 5,554	\$ 1,541	\$ 40	\$ —	\$ 7,135	\$ —	\$ 7,135
Franchise fees and income	44	6	15	—	65	—	65
Revenues from transactions with franchisees and unconsolidated affiliates	24	3	29	163	219	—	219
Other revenues	6	6	407	31	450	(388)	62
Total revenues	\$ 5,628	\$ 1,556	\$ 491	\$ 194	\$ 7,869	\$ (388)	\$ 7,481

Year to Date Ended 9/30/2021

Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 5,220	\$ 1,617	\$ 37	\$ —	\$ 6,874	\$ —	\$ 6,874
Franchise fees and income	95	6	19	—	120	—	120
Revenues from transactions with franchisees and unconsolidated affiliates	46	5	75	393	519	—	519
Other revenues	6	2	187	11	206	(157)	49
Total revenues	\$ 5,367	\$ 1,630	\$ 318	\$ 404	\$ 7,719	\$ (157)	\$ 7,562

Accounts Receivable

Accounts receivable primarily consist of trade receivables and royalties from franchisees, and are generally due within 30 days of the period in which the corresponding sales occur and are classified as Accounts receivable on the Condensed Consolidated Balance Sheets. Our provision of credit losses for accounts receivable is based upon the current expected credit losses (“CECL”) model. The CECL model requires an estimate of the credit losses expected over the life of accounts receivable since initial recognition, and accounts receivable with similar risk characteristics are grouped together when estimating CECL. In assessing the CECL, the Company considers both quantitative and qualitative information that is reasonable and supportable, including historical credit loss experience, adjusted for relevant factors impacting collectability and forward-looking information indicative of external market conditions. While we use the best information available in making our determination, the ultimate recovery of recorded receivables is also dependent upon future economic events and other conditions that may be beyond our control. Accounts receivable that are ultimately deemed to be uncollectible, and for which collection efforts have been exhausted, are written off against the allowance for doubtful accounts. As of September 30, 2022 and December 31, 2021, the ending balances of provision for accounts receivable were \$2 million and \$1 million, respectively, and amounts of accounts receivable past due were immaterial. Accounts receivable due from unconsolidated affiliates were insignificant as of both September 30, 2022 and December 31, 2021.

Costs to Obtain Contracts

Costs to obtain contracts consist of upfront franchise fees that we paid to YUM prior to the separation in relation to initial fees or renewal fees we received from franchisees and unconsolidated affiliates that operate our concepts, as well as license fees that are payable to YUM in relation to our deferred revenue of prepaid stored-value products, privilege membership programs and customer loyalty programs. They meet the requirements to be capitalized as they are incremental costs of obtaining contracts with customers and the Company expects to generate future economic benefits from such costs incurred. Such costs to obtain contracts are included in Other assets on the Condensed Consolidated Balance Sheets and are amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the assets relate. Subsequent to the separation, we are no longer required to pay YUM initial or renewal fees that we receive from franchisees and unconsolidated affiliates. The Company did not incur any impairment losses related to costs to obtain contracts during any of the periods presented. Costs to obtain contracts were \$5 million and \$7 million at September 30, 2022 and December 31, 2021, respectively.

Contract Liabilities

Contract liabilities at September 30, 2022 and December 31, 2021 were as follows:

Contract liabilities	9/30/2022	12/31/2021
– Deferred revenue related to prepaid stored-value products	\$ 112	\$ 134
– Deferred revenue related to upfront franchise fees	29	30
– Deferred revenue related to customer loyalty programs	23	25
– Deferred revenue related to privilege membership programs	12	18
– Others	—	1
Total	\$ 176	\$ 208

Contract liabilities primarily consist of deferred revenue related to prepaid stored-value products, privilege membership programs, customer loyalty programs and upfront franchise fees. Deferred revenue related to prepaid stored-value products, privilege membership programs and customer loyalty programs is included in Accounts payable and other current liabilities in the Condensed Consolidated Balance Sheets. Deferred revenue related to upfront franchise fees that we expect to recognize as revenue in the next 12 months is

included in Accounts payable and other current liabilities, and the remaining balance is included in Other liabilities in the Condensed Consolidated Balance Sheets. Revenue recognized that was included in the contract liability balance at the beginning of each period amounted to \$60 million and \$68 million for the quarters ended September 30, 2022 and 2021, respectively, and \$103 million and \$115 million for the years to date ended September 30, 2022 and 2021, respectively. Changes in contract liability balances were not materially impacted by business acquisition, change in estimate of transaction price or any other factors during any of the periods presented.

The Company has elected, as a practical expedient, not to disclose the value of remaining performance obligations associated with sales-based royalty promised to franchisees in exchange for the franchise right and other related services. The remaining duration of the performance obligation is the remaining contractual term of each franchise agreement. We recognize continuing franchisee fees and revenues from advertising services and other services provided to franchisees and unconsolidated affiliates that operate our concepts based on a certain percentage of sales, as those sales occur.

Note 5 – Earnings Per Common Share (“EPS”)

The following table summarizes the components of basic and diluted EPS (in millions, except per share data):

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Net Income – Yum China Holdings, Inc.	\$ 206	\$ 104	\$ 389	\$ 515
Weighted-average common shares outstanding (for basic calculation) ^(a)	420	422	422	421
Effect of dilutive share-based awards ^(a)	4	6	4	6
Effect of dilutive warrants ^(b)	—	7	—	8
Weighted-average common and dilutive potential common shares outstanding (for diluted calculation) ^(a)	424	435	426	435
Basic Earnings Per Common Share	\$ 0.49	\$ 0.25	\$ 0.92	\$ 1.23
Diluted Earnings Per Common Share	\$ 0.49	\$ 0.24	\$ 0.92	\$ 1.19
Share-based awards excluded from the diluted EPS computation ^(c)	4	2	4	2

- (a) As a result of the separation, shares of Yum China common stock were distributed to YUM’s shareholders of record as of October 19, 2016 and included in the calculated weighted-average common shares outstanding. Holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety. Any subsequent exercise of these awards, whether held by the Company’s employees or YUM’s employees, would increase the number of common shares outstanding. The incremental shares arising from outstanding equity awards are included in the computation of diluted EPS, if there is dilutive effect. In September 2020, 41,910,700 common shares were issued as a result of the Company’s global offering and secondary listing on the HKEX and they were included in the calculated weighted-average common shares outstanding.
- (b) Pursuant to the investment agreements dated September 1, 2016, Yum China issued to strategic investors two tranches of warrants on January 9, 2017, with each tranche initially providing the right to purchase 8,200,405 shares of Yum China common stock, at an initial exercise price of \$31.40 and \$39.25 per share, respectively, subject to customary anti-dilution adjustments. The warrants were exercisable at any time through October 31, 2021. The incremental shares arising from outstanding warrants were included in the computation of diluted EPS, if there is dilutive effect when the average market price of Yum China common stock for the periods exceeds the applicable exercise price of the warrants. During the second half of 2021, an aggregate of 7,534,316 common shares were issued as a result of the cashless exercise of all warrants outstanding, which upon exercise were excluded from the calculation of dilutive warrants and included in the weighted-average common shares outstanding.
- (c) These outstanding stock appreciation rights (“SARs”), restricted stock units (“RSUs”) and performance stock units (“PSUs”) were excluded from the computation of diluted EPS because to do so would have been antidilutive for the quarters presented, or because certain PSUs are contingently issuable based on the achievement of performance and market conditions, which have not been met as of September 30, 2022 and 2021.

Note 6 – Equity

Changes in Equity and Redeemable Noncontrolling Interest (in millions)

Yum China Holdings, Inc.										
	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock		Noncontrolling Interests	Total Equity	Redeemable Noncontrolling Interest
	Shares*	Amount				Shares*	Amount			
Balance at June 30, 2022	420	\$ 4	\$ 4,402	\$ 2,083	\$ 40	—	—	\$ 760	\$ 7,289	\$ 13
Net Income				206				21	227	—
Foreign currency translation adjustments					(262)			(44)	(306)	—
Comprehensive loss									(79)	—
Cash dividends declared (\$0.12 per common share)				(51)					(51)	—
Repurchase and retirement of shares	—	—	(3)	(10)					(13)	—
Exercise and vesting of share-based awards	—	—	(1)						(1)	—
Share-based compensation			10						10	—
Balance at September 30, 2022	419	\$ 4	\$ 4,408	\$ 2,228	\$ (222)	—	\$ —	\$ 737	\$ 7,155	\$ 13
Balance at June 30, 2021	440	\$ 4	\$ 4,679	\$ 2,415	\$ 205	(20)	\$ (728)	\$ 241	\$ 6,816	\$ 12
Net Income				104				7	111	—
Foreign currency translation adjustments					8			2	10	—
Comprehensive income									121	—
Acquisition of business								7	7	—
Cash dividends declared (\$0.12 per common share)				(51)					(51)	—
Repurchase of shares of common stock						(1)	(34)		(34)	—
Exercise and vesting of share-based awards	1	—	—						—	—
Exercise of warrants	3	—	—						—	—
Share-based compensation			6						6	—
Balance at September 30, 2021	444	\$ 4	\$ 4,685	\$ 2,468	\$ 213	(20)	\$ (762)	\$ 257	\$ 6,865	\$ 12
Yum China Holdings, Inc.										
	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock		Noncontrolling Interests	Total Equity	Redeemable Noncontrolling Interest
	Shares*	Amount				Shares*	Amount			
Balance at December 31, 2021	449	\$ 4	\$ 4,695	\$ 2,892	\$ 268	(21)	\$ (803)	\$ 852	\$ 7,908	\$ 14
Net Income				389				31	420	—
Foreign currency translation adjustments					(490)			(83)	(573)	—
Comprehensive loss									(153)	—
Cash dividends declared (\$0.36 per common share)				(152)					(152)	—
Dividends declared								(81)	(81)	—
Contribution from noncontrolling interests								18	18	—
Repurchase and retirement of shares	(30)	—	(315)	(901)		21	803		(413)	—
Exercise and vesting of share-based awards	1	—	(3)						(3)	—
Share-based compensation			31						31	—
Acquisition of noncontrolling interest									—	(1)
Balance at September 30, 2022	419	\$ 4	\$ 4,408	\$ 2,228	\$ (222)	—	\$ —	\$ 737	\$ 7,155	\$ 13
Balance at December 31, 2020	440	\$ 4	\$ 4,658	\$ 2,105	\$ 167	(20)	\$ (728)	\$ 253	\$ 6,459	\$ 12
Net Income				515				32	547	—
Foreign currency translation adjustments					46			4	50	—
Comprehensive income									597	—
Acquisition of business								7	7	—
Cash dividends declared (\$0.36 per common share)				(152)					(152)	—
Dividends declared								(39)	(39)	—
Repurchase of shares of common stock						(1)	(34)		(34)	—
Exercise and vesting of share-based awards	1	—	(5)						(5)	—
Exercise of warrants	3	—	—						—	—
Share-based compensation			32						32	—
Balance at September 30, 2021	444	\$ 4	\$ 4,685	\$ 2,468	\$ 213	(20)	\$ (762)	\$ 257	\$ 6,865	\$ 12

*: Shares may not add due to rounding.

Share Repurchase and Retirement

Our Board of Directors has authorized an aggregate of \$2.4 billion for our share repurchase program, including its most recent increase in authorization in March 2022. The Company repurchased 9 million and 0.6 million shares of Yum China common stock at a total cost of \$413 million and \$34 million during the years to date ended September 30, 2022 and 2021, respectively. The total repurchase cost

included \$2 million settled subsequent to both September 30, 2022 and 2021, for shares repurchased with trade dates prior to September 30, 2022 and 2021, respectively. As of September 30, 2022, \$1.2 billion remained available for future share repurchases under the authorization.

As of September 30, 2022, all shares repurchased under the current and previous authorizations were retired and resumed the status of authorized and unissued shares of common stock. When shares are retired, the Company's accounting policy is to allocate the excess of the repurchase price over the par value of shares acquired between Additional paid-in capital and Retained earnings. The amount allocated to Additional paid-in capital is based on the value of Additional paid-in capital per share outstanding at the time of retirement and the number of shares to be retired. Any remaining amount is allocated to Retained earnings.

Note 7 – Items Affecting Comparability of Net Income

Impact of COVID-19 Pandemic

Starting in the first quarter of 2020, the COVID-19 pandemic significantly impacted the Company's operations. Since then, fluid COVID-19 conditions have caused significant volatility in our operations. During the first half of 2022, the most severe COVID-19 outbreaks to date in China significantly affected the Company's business and operating profit. During the third quarter of 2022, the Company reported significant year-over-year operating profit growth as the Company captured the sales demand when COVID-19 conditions were relatively calmer in July and August, and also benefited from lapping the Delta variant outbreak in the prior year period.

Fair Value Changes for Investment in Equity Securities

In September 2018, we invested in the equity securities of Meituan, the fair value of which is determined based on the closing market price for the shares at the end of each reporting period, with subsequent fair value changes recorded in our Condensed Consolidated Statements of Income. We recorded related pre-tax loss of \$15 million and \$41 million for the quarters ended September 30, 2022 and 2021, respectively, and related pre-tax loss of \$33 million and \$27 million for the years to date ended September 30, 2022 and 2021, respectively.

In the first quarter of 2021, we invested in a 5% equity interest in Sunner. The investment in Sunner was recorded at fair value based on its closing market price on each measurement date before it became subject to the equity method of accounting when the Company established significant influence over the operating and financial policies of Sunner in May 2021. We recorded related pre-tax loss of \$22 million for the year to date ended September 30, 2021, representing changes in fair value before the equity method of accounting was applied.

See Note 3 for additional information on our investment in Meituan and Sunner.

Note 8 – Other Expenses (Income), net

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Amortization of reacquired franchise rights ^(a)	\$ 24	\$ 10	\$ 74	\$ 29
Equity income from investments in unconsolidated affiliates ^(b)	—	(10)	—	(37)
Gain from re-measurement of equity interest upon acquisition ^(c)	—	(10)	—	(10)
Foreign exchange impact and others	—	—	(1)	3
Other expenses (income), net	\$ 24	\$ (10)	\$ 73	\$ (15)

(a) Increase in amortization of reacquired franchise rights as a result of the acquisition of Hangzhou KFC as disclosed in Note 3, with \$66 million of the purchase price allocated to intangible assets related to reacquired franchise right, which is being amortized over the remaining franchise contract period of 1 year.

(b) Includes equity income from our investments in Hangzhou KFC and the Lavazza joint venture before we consolidated the results of these entities upon completion of the acquisitions in 2021 (See Note 3 for additional information).

(c) For the quarter and year to date ended September 30, 2021, the Company recognized a gain of \$10 million from the re-measurement of our previously held equity interest at fair value, as a result the consolidation of Lavazza joint venture as disclosed in Note 3.

Note 9 – Supplemental Balance Sheet Information

	<u>9/30/2022</u>	<u>12/31/2021</u>
<u>Accounts Receivable, net</u>		
Accounts receivable, gross	\$ 68	\$ 68
Allowance for doubtful accounts	(2)	(1)
Accounts receivable, net	<u>\$ 66</u>	<u>\$ 67</u>
<u>Prepaid Expenses and Other Current Assets</u>		
VAT assets ^(a)	\$ 93	\$ —
Receivables from payment processors and aggregators	37	45
Dividends receivable from unconsolidated affiliates	6	—
Other prepaid expenses and current assets	150	176
Prepaid expenses and other current assets	<u>\$ 286</u>	<u>\$ 221</u>
<u>Property, Plant and Equipment</u>		
Buildings and improvements, and construction in progress	\$ 2,727	\$ 2,984
Finance leases, primarily buildings	52	52
Machinery and equipment	1,525	1,589
Property, plant and equipment, gross	4,304	4,625
Accumulated depreciation	(2,339)	(2,374)
Property, plant and equipment, net	<u>\$ 1,965</u>	<u>\$ 2,251</u>
<u>Other Assets</u>		
Land use right	\$ 120	\$ 138
Investment in equity securities	89	122
Long-term deposits	87	101
Investment in long-term time deposits ^(b)	83	90
Costs to obtain contracts	5	7
VAT assets ^(a)	4	322
Others	31	52
Other Assets	<u>\$ 419</u>	<u>\$ 832</u>
<u>Accounts Payable and Other Current Liabilities</u>		
Accounts payable	\$ 673	\$ 830
Operating lease liabilities	441	508
Accrued compensation and benefits	252	283
Contract liabilities	152	182
Accrued capital expenditures	133	269
Accrued marketing expenses	107	71
Dividends payable	93	38
Other current liabilities	141	151
Accounts payable and other current liabilities	<u>\$ 1,992</u>	<u>\$ 2,332</u>
<u>Other Liabilities</u>		
Accrued income tax payable	\$ 50	\$ 56
Contract liabilities	24	26
Other non-current liabilities	82	85
Other liabilities	<u>\$ 156</u>	<u>\$ 167</u>

- (a) On June 7, 2022, the Chinese Ministry of Finance and the Chinese State Tax Administration jointly issued Circular [2022] No. 21, to extend full VAT credit refunds to more sectors and increase the frequency for accepting taxpayers' applications with an aim to support business recovery. Beginning on July 1, 2022, entities engaged in providing catering services in China are allowed to apply for a lump sum refund of VAT assets accumulated prior to March 31, 2019. In addition, VAT assets accumulated after March 31, 2019 can be refunded on a monthly basis. As the benefits of certain VAT assets are expected to be realized within one year pursuant to Circular [2022] No. 21, \$303 million of VAT assets as of June 30, 2022 were reclassified from Other assets to Prepaid expense and other current assets. As of September 30, 2022, VAT assets of \$93 million were included in Prepaid expenses and other current assets.

- (b) As of September 30, 2022 and December 31, 2021, the Company had \$83 million and \$90 million invested in long-term time deposits, respectively, bearing a fixed interest rate, with original maturity of three years. The asset is restricted for use in order to secure the balance of prepaid stored-value cards issued by the Company pursuant to regulatory requirements.

Note 10 – Goodwill and Intangible Assets

The changes in the carrying amount of goodwill are as follows:

	Total Company	KFC	Pizza Hut	All Other Segments
Balance as of December 31, 2021				
Goodwill, gross	\$ 2,533	\$ 2,040	\$ 20	\$ 473
Accumulated impairment losses ^(a)	(391)	—	—	(391)
Goodwill, net	2,142	2,040	20	82
Goodwill acquired ^(b)	16	15	1	—
Effect of currency translation adjustment	(231)	(220)	(2)	(9)
Balance as of September 30, 2022				
Goodwill, gross	2,318	1,835	19	464
Accumulated impairment losses ^(a)	(391)	—	—	(391)
Goodwill, net	\$ 1,927	\$ 1,835	\$ 19	\$ 73

- (a) Accumulated impairment losses represent goodwill impairment attributable to the reporting units of Little Sheep and Daojia.
- (b) Goodwill acquired as a result of the acquisition of restaurants from our existing franchisees. The acquisition is considered immaterial.

Intangible assets, net as of September 30, 2022 and December 31, 2021 are as follows:

	9/30/2022				12/31/2021			
	Gross Carrying Amount ^(a)	Accumulated Amortization ^(a)	Accumulated Impairment Losses ^(b)	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Accumulated Impairment Losses ^(b)	Net Carrying Amount
Finite-lived intangible assets								
Reacquired franchise rights	\$ 268	\$ (240)	\$ —	\$ 28	\$ 295	\$ (191)	\$ —	\$ 104
Huang Ji Huang franchise related assets	21	(3)	—	18	23	(2)	—	21
Daojia platform	16	(4)	(12)	—	16	(4)	(12)	—
Customer-related assets	12	(10)	(2)	—	12	(9)	(2)	1
Others	9	(5)	—	4	10	(5)	—	5
	<u>\$ 326</u>	<u>\$ (262)</u>	<u>\$ (14)</u>	<u>\$ 50</u>	<u>\$ 356</u>	<u>\$ (211)</u>	<u>\$ (14)</u>	<u>\$ 131</u>
Indefinite-lived intangible assets								
Little Sheep trademark	\$ 51	\$ —	\$ —	\$ 51	\$ 57	\$ —	\$ —	\$ 57
Huang Ji Huang trademark	75	—	—	75	84	—	—	84
	<u>\$ 126</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 126</u>	<u>\$ 141</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 141</u>
Total intangible assets	<u>\$ 452</u>	<u>\$ (262)</u>	<u>\$ (14)</u>	<u>\$ 176</u>	<u>\$ 497</u>	<u>\$ (211)</u>	<u>\$ (14)</u>	<u>\$ 272</u>

- (a) Changes in gross carrying amount and accumulated amortization include effect of currency translation adjustments.
- (b) Accumulated impairment losses represent impairment charges on intangible assets acquired from Daojia primarily attributable to the Daojia platform.

Amortization expense of finite-lived intangible assets was \$24 million and \$10 million for the quarters ended September 30, 2022 and 2021, respectively, and \$76 million and \$31 million for the years to date ended September 30, 2022 and 2021, respectively. As of September 30, 2022, expected amortization expense for the unamortized finite-lived intangible assets is approximately \$23 million for the remainder of 2022, \$4 million in 2023, and \$2 million in each of 2024, 2025 and 2026. Increase in amortization expenses for finite-lived intangible assets in 2022 primarily relates to reacquired franchise rights resulting from the acquisition of Hangzhou KFC (Note 3).

Note 11 – Leases

As of September 30, 2022, we leased over 10,600 properties in China for our Company-owned restaurants. We generally enter into lease agreements for our restaurants with initial terms of 10 to 20 years. Most of our lease agreements contain termination options that permit us to terminate the lease agreement early if the restaurant's unit contribution is negative for a specified period of time. We generally do not have renewal options for our leases. Such options are accounted for only when it is reasonably certain that we will exercise the options. The rent under the majority of our current restaurant lease agreements is generally payable in one of three ways: (i) fixed rent; (ii) the higher of a fixed base rent or a percentage of the restaurant's sales; or (iii) a percentage of the restaurant's sales. Most leases require us to pay common area maintenance fees for the leased property. In addition to restaurants leases, we also lease office spaces, logistics centers and equipment. Our lease agreements do not contain any material residual value guarantees or material restrictive covenants.

In limited cases, we sub-lease certain restaurants to franchisees in connection with franchising transactions or lease our properties to other third parties. The lease payments under these leases are generally based on the higher of a fixed base rent or a percentage of the restaurant's annual sales. Income from sub-lease agreements with franchisees or lease agreements with other third parties are included in Franchise fees and income and Other revenues, respectively, within our Condensed Consolidated Statements of Income.

Supplemental Balance Sheet

	9/30/2022	12/31/2021	Account Classification
Assets			
Operating lease right-of-use assets	\$ 2,154	\$ 2,612	Operating lease right-of-use assets
Finance lease right-of-use assets	31	33	Property, plant and equipment, net
Total leased assets	<u>\$ 2,185</u>	<u>\$ 2,645</u>	
Liabilities			
Current			
Operating lease liabilities	\$ 441	\$ 508	Accounts payable and other current liabilities
Finance lease liabilities	4	3	Accounts payable and other current liabilities
Non-current			
Operating lease liabilities	1,862	2,286	Non-current operating lease liabilities
Finance lease liabilities	36	40	Non-current finance lease liabilities
Total lease liabilities	<u>\$ 2,343</u>	<u>\$ 2,837</u>	

Summary of Lease Cost

	Quarter Ended		Year to Date Ended		Account Classification
	9/30/2022	9/30/2021	9/30/2022	9/30/2021	
Operating lease cost	\$ 133	\$ 140	\$ 433	\$ 414	Occupancy and other operating expenses, G&A or Franchise expenses
Finance lease cost					
Amortization of leased assets	1	1	3	2	Occupancy and other operating expenses
Interest on lease liabilities	1	—	2	1	Interest expense, net
Variable lease cost ^(a)	89	91	248	273	Occupancy and other operating expenses or Franchise expenses
Short-term lease cost	3	3	10	8	Occupancy and other operating expenses or G&A
Sub-lease income	(5)	(6)	(18)	(20)	Franchise fees and income or Other revenues
Total lease cost	<u>\$ 222</u>	<u>\$ 229</u>	<u>\$ 678</u>	<u>\$ 678</u>	

- (a) The Company was granted \$13 million and \$2 million in lease concessions from landlords related to the effects of the COVID-19 pandemic during the quarters ended September 30, 2022 and 2021, respectively, and \$27 million and \$9 million during the years to date ended September 30, 2022 and 2021, respectively. The lease concessions were primarily in the form of rent reduction over the period of time when the Company's restaurant business was adversely impacted. The Company applied the interpretive guidance in a FASB staff Q&A document issued in April 2020 and elected: (1) not to evaluate whether a concession received in response to the COVID-19 pandemic is a lease modification and (2) to assume such concession was contemplated as part of the existing lease contract with no contract modification. Such concession was recognized as negative variable lease cost in the period the concession was granted.

Supplemental Cash Flow Information

	Year to Date Ended	
	9/30/2022	9/30/2021
Cash paid for amounts included in the measurement of lease liabilities:		
Operating cash flows from operating leases	\$ 416	\$ 423
Operating cash flows from finance leases	2	1
Financing cash flows from finance leases	3	2
Right-of-use assets obtained in exchange for lease liabilities ^(b) :		
Operating leases	\$ 106	\$ 394
Finance leases	4	7

- (b) This supplemental non-cash disclosure for right-of-use (“ROU”) assets obtained in exchange for lease liabilities includes an increase in lease liabilities associated with obtaining new ROU assets of \$232 million and \$399 million for the years to date ended September 30, 2022 and 2021, respectively, as well as adjustments to lease liabilities or ROU assets due to modification or other reassessment events, which resulted in a \$122 million decrease and \$2 million increase in lease liabilities for the years to date ended September 30, 2022 and 2021, respectively.

Lease Term and Discount Rate

	9/30/2022	9/30/2021
Weighted-average remaining lease term (years)		
Operating leases	7.1	7.0
Finance leases	11.3	11.2
Weighted-average discount rate		
Operating leases	5.2%	5.7%
Finance leases	5.3%	5.6%

Summary of Future Lease Payments and Lease Liabilities

Maturities of lease liabilities as of September 30, 2022 were as follows:

	Amount of Operating Leases	Amount of Finance Leases	Total
Remainder of 2022	\$ 175	\$ 1	\$ 176
2023	490	6	496
2024	430	5	435
2025	366	5	371
2026	317	5	322
Thereafter	981	31	1,012
Total undiscounted lease payment	2,759	53	2,812
Less: imputed interest ^(c)	456	13	469
Present value of lease liabilities	\$ 2,303	\$ 40	\$ 2,343

- (c) As the rate implicit in the lease cannot be readily determined, we use our incremental borrowing rate based on the information available at the lease commencement date in determining the imputed interest and present value of lease payments. We used the incremental borrowing rate on January 1, 2019 for operating leases that commenced prior to that date.

As of September 30, 2022, we have additional lease agreements that have been signed but not yet commenced, with total undiscounted minimum lease payments of \$131 million. These leases will commence between the fourth quarter of 2022 and 2026 with lease terms of 1 year to 20 years.

Note 12 – Fair Value Measurements and Disclosures

The Company’s financial assets and liabilities primarily consist of cash and cash equivalents, short-term investments, long-term time deposits, accounts receivable, accounts payable and lease liabilities, and the carrying values of these assets and liabilities approximate their fair value in general.

The Company accounts for its investment in equity securities of Meituan at fair value, which is determined based on the respective closing market price for the shares at the end of each reporting period, with subsequent fair value changes recorded in our Condensed Consolidated Statements of Income.

The following table is a summary of our financial assets measured on a recurring basis or disclosed at fair value and the level within the fair value hierarchy in which the measurement falls. The Company classifies its cash equivalents, short-term investments, long-term time deposits and investment in equity securities within Level 1 or Level 2 in the fair value hierarchy because it uses quoted market prices or alternative pricing sources and models utilizing market observable inputs to determine their fair value, respectively. No transfers among the levels within the fair value hierarchy occurred during the quarters and years to date ended September 30, 2022 and 2021.

	Balance at September 30, 2022	Fair Value Measurement or Disclosure at September 30, 2022		
		Level 1	Level 2	Level 3
Cash equivalents:				
Time deposits	\$ 291		\$ 291	
Fixed income debt securities ^(a)	100		100	
Money market funds	63	63		
Total cash equivalents	454	63	391	—
Short-term investments:				
Time deposits	1,990		1,990	
Fixed income debt securities ^(a)	550		550	
Structured deposits	267		267	
Variable return investments	19	19		
Total short-term investments	2,826	19	2,807	—
Other assets:				
Investment in equity securities	89	89		
Long-term time deposits	83		83	
Total	\$ 3,452	\$ 171	\$ 3,281	\$ —

	Balance at December 31, 2021	Fair Value Measurement or Disclosure at December 31, 2021		
		Level 1	Level 2	Level 3
Cash equivalents:				
Time deposits	\$ 321		\$ 321	
Fixed income debt securities ^(a)	163	63	100	
Money market funds	45	45		
Total cash equivalents	529	108	421	—
Short-term investments:				
Time deposits	1,726		1,726	
Fixed income debt securities ^(a)	1,055		1,055	
Variable return investments	79	79		
Total short-term investments	2,860	79	2,781	—
Other assets:				
Investment in equity securities	122	122		
Long-term time deposits	90		90	
Total	\$ 3,601	\$ 309	\$ 3,292	\$ —

(a) Classified as held-to-maturity investments and measured at amortized cost.

Non-Recurring Fair Value Measurements

In addition, certain of the Company's restaurant-level assets (including operating lease ROU assets, property, plant and equipment), goodwill and intangible assets, are measured at fair value based on unobservable inputs (Level 3) on a non-recurring basis, if determined to be impaired.

In determining the fair value of restaurant-level assets, the Company considered the highest and best use of the assets from a market participants' perspective, which is represented by the higher of the forecasted discounted cash flows from operating restaurants and the price market participants would pay to sub-lease the ROU assets and acquire the remaining restaurant assets, even if that use differs from the current use by the Company. The after-tax cash flows incorporate reasonable assumptions we believe a franchisee would make, such as sales growth, and include a deduction for royalties we would receive under a franchise agreement with terms substantially at market. The discount rate used in the fair value calculation is our estimate of the required rate-of-return that a franchisee would expect to receive when purchasing a similar restaurant and the related long-lived assets. In situations where the highest and best use of restaurant-level assets are represented by sub-leasing the operating lease ROU assets and acquiring the remaining restaurant assets, the Company continues to use these assets in operating its restaurant business, which is consistent with its long-term strategy of growing revenue through operating restaurant concepts.

As of each relevant measurement date, the fair value of restaurant-level assets, if determined to be impaired, are primarily represented by the price market participant would pay to sub-lease the operating lease ROU assets and acquire the remaining restaurant assets, which reflects the highest and best use of the assets. Significant unobservable inputs used in the fair value measurement include market rental prices, which were determined with the assistance of an independent valuation specialist. The direct comparison approach is used as the valuation technique by assuming a sub-lease of each of the properties in its existing state with vacant possession. By making reference to lease transactions as available in the relevant market, comparable properties in close proximity have been selected and adjustments have been made to account for any difference in factors such as location and property size.

The following table presents amounts recognized from all non-recurring fair value measurements based on unobservable inputs (Level 3) during the quarters and years to date ended September 30, 2022 and 2021. These amounts exclude fair value measurements made for restaurants that were subsequently closed or refranchised prior to those respective period-end dates.

	Quarter Ended		Year to Date Ended		Account Classification
	9/30/2022	9/30/2021	9/30/2022	9/30/2021	
Restaurant-level impairment ^(a)	\$ —	\$ —	\$ 15	\$ 13	Closure and impairment expenses, net

(a) Restaurant-level impairment charges are recorded in Closures and impairment expenses, net and resulted from our semi-annual impairment evaluation of long-lived assets of individual restaurants that were being operated at the time of impairment and had not been offered for refranchising. After considering the impairment charges recorded during the corresponding periods, the fair value of assets as of the relevant measurement date was \$67 million and \$50 million for the years to date ended September 30, 2022 and 2021, respectively.

Note 13 – Income Taxes

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Income tax provision	\$ 97	\$ 44	\$ 183	\$ 210
Effective tax rate	29.9%	28.3%	30.1%	27.7%

The higher effective tax rate for the quarter ended September 30, 2022 was primarily due to a prior year tax benefit from equity income from investments in unconsolidated affiliates. The higher effective tax rate for the year to date ended September 30, 2022 was primarily due to a prior year tax benefit from equity income from investments in unconsolidated affiliates and the impact of lower pre-tax income.

In December 2017, the U.S. enacted the Tax Cuts and Jobs Act (the "Tax Act"), which included a broad range of tax reforms. The Tax Act requires a U.S. shareholder to be subject to tax on Global Intangible Low Taxed Income ("GILTI") earned by certain foreign subsidiaries. We have elected the option to account for current year GILTI tax as a period cost as incurred, and therefore included it in estimating the annual effective tax rate.

In August 2022, the Inflation Reduction Act of 2022 (the "IRA") was signed into law in the U.S. The IRA contains certain tax measures, including a corporate alternative minimum tax of 15% on certain large corporations and an excise tax of 1% on net share repurchases that occur after December 31, 2022. Based on our preliminary analysis of the provisions, we do not believe this legislation will have a material impact on our financial statements. However, the details of the computation will be subject to regulations to be issued by the Department of the Treasury. The Company will monitor the regulatory developments and continue to evaluate the impact, if any.

We are subject to reviews, examinations and audits by Chinese tax authorities, the Internal Revenue Service and other tax authorities with respect to income and non-income based taxes. Since 2016, we have been under a national audit on transfer pricing by the Chinese State Tax Administration (the “STA”) regarding our related party transactions for the period from 2006 to 2015. The information and views currently exchanged with the tax authorities focus on our franchise arrangement with YUM. We continue to provide information requested by the tax authorities to the extent it is available to the Company. It is reasonably possible that there could be significant developments, including expert review and assessment by the STA, within the next 12 months. The ultimate assessment and decision of the STA will depend upon further review of the information provided, as well as ongoing technical and other discussions with the STA and in-charge local tax authorities, and therefore, it is not possible to reasonably estimate the potential impact at this time. We will continue to defend our transfer pricing position. However, if the STA prevails in the assessment of additional tax due based on its ruling, the assessed tax, interest and penalties, if any, could have a material adverse impact on our financial position, results of operations and cash flows.

Note 14 –Segment Reporting

We have two reportable segments: KFC and Pizza Hut. Our remaining non-reportable operating segments, including the operations of Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY, Taco Bell, East Dawning, Daojia and our e-commerce business, are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in aggregate.

	Quarter Ended 9/30/2022						
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 2,017	\$ 561	\$ 41	\$ 66	\$ 2,685	\$ —	\$ 2,685
Inter-segment revenue	—	—	145	5	150	(150)	—
Total	<u>\$ 2,017</u>	<u>\$ 561</u>	<u>\$ 186</u>	<u>\$ 71</u>	<u>\$ 2,835</u>	<u>\$ (150)</u>	<u>\$ 2,685</u>

	Quarter Ended 9/30/2021						
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 1,801	\$ 551	\$ 59	\$ 143	\$ 2,554	\$ —	\$ 2,554
Inter-segment revenue	—	—	75	3	78	(78)	—
Total	<u>\$ 1,801</u>	<u>\$ 551</u>	<u>\$ 134</u>	<u>\$ 146</u>	<u>\$ 2,632</u>	<u>\$ (78)</u>	<u>\$ 2,554</u>

	Year to Date Ended 9/30/2022						
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 5,628	\$ 1,556	\$ 115	\$ 182	\$ 7,481	\$ —	\$ 7,481
Inter-segment revenue	—	—	376	12	388	(388)	—
Total	<u>\$ 5,628</u>	<u>\$ 1,556</u>	<u>\$ 491</u>	<u>\$ 194</u>	<u>\$ 7,869</u>	<u>\$ (388)</u>	<u>\$ 7,481</u>

	Year to Date Ended 9/30/2021						
Revenues	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 5,367	\$ 1,630	\$ 164	\$ 401	\$ 7,562	\$ —	\$ 7,562
Inter-segment revenue	—	—	154	3	157	(157)	—
Total	<u>\$ 5,367</u>	<u>\$ 1,630</u>	<u>\$ 318</u>	<u>\$ 404</u>	<u>\$ 7,719</u>	<u>\$ (157)</u>	<u>\$ 7,562</u>

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Operating Profit (Loss)				
KFC ^(b)	\$ 328	\$ 196	\$ 670	\$ 763
Pizza Hut	49	18	90	117
All Other Segments	(9)	(6)	(39)	(15)
Unallocated revenues from transactions with franchisees and unconsolidated affiliates ^(c)	59	139	163	393
Unallocated other revenues	12	7	31	11
Unallocated expenses from transactions with franchisees and unconsolidated affiliates ^(c)	(58)	(138)	(163)	(390)
Unallocated other operating costs and expenses	(10)	(5)	(28)	(10)
Unallocated and corporate G&A expenses	(55)	(42)	(138)	(123)
Unallocated other income, net ^(d)	—	9	2	7
Operating Profit	\$ 316	\$ 178	\$ 588	\$ 753
Interest income, net ^(a)	25	16	51	47
Investment loss ^(a)	(15)	(39)	(32)	(43)
Income Before Income Taxes and Equity in Net Earnings (Losses) from Equity Method Investments	\$ 326	\$ 155	\$ 607	\$ 757

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Impairment Charges				
KFC ^(e)	\$ 5	\$ 3	\$ 24	\$ 14
Pizza Hut ^(e)	—	1	5	8
All Other Segments ^(e)	2	—	8	1
	\$ 7	\$ 4	\$ 37	\$ 23

	Total Assets	
	9/30/2022	12/31/2021
KFC	\$ 5,137	\$ 6,072
Pizza Hut	835	972
All Other Segments	364	454
Corporate and Unallocated ^(f)	5,360	5,725
	\$ 11,696	\$ 13,223

(a) Amounts have not been allocated to any segment for performance reporting purposes.

(b) Includes equity income from our investment in Hangzhou KFC of \$13 million and \$45 million for the quarter and year to date ended September 30, 2021 before we consolidated the results of the entity upon completion of the acquisition. See Note 3 for details.

(c) Primarily includes revenues and associated expenses of transactions with franchisees and unconsolidated affiliates derived from the Company's central procurement model whereby the Company centrally purchases substantially all food and paper products from suppliers and then sells and delivers them to KFC and Pizza Hut restaurants, including franchisees and unconsolidated affiliates that operate our concepts. Amounts have not been allocated to any segment for purposes of making operating decisions or assessing financial performance as the transactions are deemed corporate revenues and expenses in nature.

(d) Primarily includes a gain from the re-measurement of our previously-held equity interest in connection with the acquisition of the Lavazza joint venture for the quarter and year to date ended September 30, 2021. As the re-measurement at fair value resulted from the acquisition, it was not allocated to any segment for performance reporting purposes. See Note 3.

(e) Primarily includes store closure impairment charges and restaurant-level impairment charges resulting from our semi-annual impairment evaluation. See Note 12.

(f) Primarily includes cash and cash equivalents, short-term investments, investments in equity securities of Meituan, investments in Sunner and Hangzhou Catering, long-term time deposits and inventories that are centrally managed.

Note 15 – Contingencies

Indemnification of China Tax on Indirect Transfers of Assets

In February 2015, the STA issued Bulletin 7 on Income arising from Indirect Transfers of Assets by Non-Resident Enterprises. Pursuant to Bulletin 7, an “indirect transfer” of Chinese taxable assets, including equity interests in a Chinese resident enterprise, by a non-resident enterprise, may be recharacterized and treated as a direct transfer of Chinese taxable assets, if such arrangement does not have reasonable commercial purpose and the transferor has avoided payment of Chinese enterprise income tax. As a result, gains derived from such an indirect transfer may be subject to Chinese enterprise income tax at a rate of 10%.

YUM concluded, and we concurred, that it is more likely than not that YUM will not be subject to this tax with respect to the pro rata distribution of all outstanding shares of Yum China common stock to shareholders of YUM in connection with the separation (the “distribution”). However, there are significant uncertainties regarding what constitutes a reasonable commercial purpose, how the safe harbor provisions for group restructurings are to be interpreted, and how the taxing authorities will ultimately view the distribution. As a result, YUM’s position could be challenged by Chinese tax authorities resulting in a 10% tax assessed on the difference between the fair market value and the tax basis of the separated China business. As YUM’s tax basis in the China business is minimal, the amount of such a tax could be significant.

Any tax liability arising from the application of Bulletin 7 to the distribution is expected to be settled in accordance with the tax matters agreement between the Company and YUM. Pursuant to the tax matters agreement, to the extent any Chinese indirect transfer tax pursuant to Bulletin 7 is imposed, such tax and related losses will be allocated between YUM and the Company in proportion to their respective share of the combined market capitalization of YUM and the Company during the 30 trading days after the separation. Such a settlement could be significant and have a material adverse effect on our results of operations and our financial condition. At the inception of the tax indemnity being provided to YUM, the fair value of the non-contingent obligation to stand ready to perform was insignificant and the liability for the contingent obligation to make payment was not probable or estimable.

Guarantees for Franchisees

From time to time, we have guaranteed certain lines of credit and loans of franchisees. As of September 30, 2022, no guarantees were outstanding for franchisees.

Legal Proceedings

The Company is subject to various lawsuits covering a variety of allegations from time to time. The Company believes that the ultimate liability, if any, in excess of amounts already provided for these matters in the Condensed Consolidated Financial Statements, is not likely to have a material adverse effect on the Company’s results of operations, financial condition or cash flows. Matters faced by the Company from time to time include, but are not limited to, claims from landlords, employees, customers and others related to operational, contractual or employment issues.

Note 16 – Subsequent Events

Cash Dividend

On November 1, 2022, the Company announced that the Board of Directors declared a cash dividend of \$0.12 per share on Yum China’s common stock, payable as of the close of business on December 20, 2022, to stockholders of record as of the close of business on November 29, 2022. Total estimated cash dividend payable is approximately \$50 million.

Long Term Incentive Plan

In connection with the Primary Conversion, the Company’s stockholders approved the Yum China Holdings, Inc. 2022 Long Term Incentive Plan (the “2022 Plan”). The 2022 Plan became effective on October 24, 2022 upon consummation of the Primary Conversion. The 2022 Plan replaces the Yum China Holdings, Inc. Long Term Incentive Plan (the “2016 Plan”). No new awards will be granted under the 2016 Plan after the 2022 Plan becomes effective, but the 2016 Plan will continue to govern awards granted under the 2016 Plan prior to the effectiveness of the 2022 Plan. Subject to the terms and conditions of the 2022 Plan, the number of shares of Company common stock authorized for grants under the 2022 Plan is 31,000,000 shares.

Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations

References to the Company throughout this Management’s Discussion and Analysis of Financial Condition and Results of Operations (this “MD&A”) are made using the first person notations of “we,” “us” or “our.” This MD&A contains forward-looking statements, including statements with respect to the ongoing transfer pricing audit, the retail tax structure reform, impacts of COVID-19, our growth plans, future capital resources to fund our operations and anticipated capital expenditures, share repurchases and dividends, and the impact of new accounting pronouncements not yet adopted. See “Cautionary Note Regarding Forward-Looking Statements” at the end of this Item 2 for information regarding forward-looking statements.

Introduction

Yum China Holdings, Inc. is the largest restaurant company in China in terms of system sales, with over 12,000 restaurants covering over 1,700 cities primarily in China as of September 30, 2022. Our growing restaurant base consists of our flagship KFC and Pizza Hut brands, as well as emerging brands such as Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY and Taco Bell. We have the exclusive right to operate and sublicense the KFC, Pizza Hut and, subject to achieving certain agreed-upon milestones, Taco Bell brands in China, excluding Hong Kong, Macau and Taiwan, and own the intellectual property of the Little Sheep, Huang Ji Huang and COFFii & JOY concepts outright. KFC was the first major global restaurant brand to enter China as early as 1987. With more than 30 years of operations, we have developed extensive operating experience in the China market. We have since grown to become the largest restaurant company in China in terms of system sales. We believe that there are significant opportunities to further expand within China, and we intend to focus our efforts on increasing our geographic footprint in both existing and new cities.

KFC is the leading and the largest quick-service restaurant (“QSR”) brand in China in terms of system sales. As of September 30, 2022, KFC operated over 8,600 restaurants in over 1,700 cities across China. During the fourth quarter of 2021, the Company completed the acquisition of a 28% equity interest in Hangzhou Catering Service Group (“Hangzhou Catering”), which holds a 45% equity interest in an unconsolidated affiliate that operates KFC stores in and around Hangzhou, China (“Hangzhou KFC”), increasing our equity interest to approximately 60% directly and indirectly, and allowing the Company to consolidate Hangzhou KFC.

Pizza Hut is the leading and the largest casual dining restaurant (“CDR”) brand in China in terms of system sales and number of restaurants. As of September 30, 2022, Pizza Hut operated over 2,800 restaurants in over 600 cities.

In the second quarter of 2020, the Company partnered with Luigi Lavazza S.p.A. (“Lavazza Group”), the world renowned family-owned Italian coffee company, and entered into a joint venture to explore and develop the Lavazza coffee shop concept in China. In September 2021, the Company and Lavazza Group entered into agreements for the previously formed joint venture (“Lavazza joint venture”) to accelerate the expansion of Lavazza coffee shops in China. Upon execution of these agreements, the Company controls and consolidates the joint venture with its 65% equity interest.

On April 15, 2022, the Company and YUM, through their respective subsidiaries, entered into an amendment to the master license agreement to amend the development milestones for the Taco Bell brand. The Company has committed to expanding the Taco Bell store network to at least 100 stores by the end of 2022 and at least 225 stores by the end of 2025, with certain investment support from YUM. Subject to achieving these milestones, the Company will have the exclusive right to operate and sublicense the Taco Bell brand in China for 50 years.

The Company’s common stock is listed on the NYSE under the symbol “YUMC”. On September 10, 2020, the Company completed its secondary listing on the Main Board of the HKEX under the stock code “9987”, in connection with a global offering of 41,910,700 shares of its common stock. Net proceeds raised by the Company from the global offering after deducting underwriting fees and the offering expenses amounted to \$2.2 billion. On October 24, 2022, the Company’s voluntary conversion of its secondary listing status to a primary listing status on the HKEX became effective. On the same day, the Company’s shares of common stock traded on the HKEX was included in the Shanghai-Hong Kong Stock Connect and Shenzhen-Hong Kong Stock Connect. Yum China is now a dual primary listed company on the NYSE and HKEX. The Company’s common stock listed on the two exchanges will continue to be fully fungible.

Overview

We intend for this MD&A to provide the reader with information that will assist in understanding our results of operations, including metrics that management uses to assess the Company's performance. Throughout this MD&A, we discuss the following performance metrics:

- The Company provides certain percentage changes excluding the impact of foreign currency translation ("F/X"). These amounts are derived by translating current year results at prior year average exchange rates. We believe the elimination of the F/X impact provides better year-to-year comparability without the distortion of foreign currency fluctuations.
- System sales growth reflects the results of all restaurants regardless of ownership, including Company-owned, franchise and unconsolidated affiliate restaurants that operate our concepts, except for sales from non-Company-owned restaurants for which we do not receive a sales-based royalty. Sales of franchise and unconsolidated affiliate restaurants typically generate ongoing franchise fees for the Company at an average rate of approximately 6% of system sales. Franchise and unconsolidated affiliate restaurant sales are not included in Company sales in the Condensed Consolidated Statements of Income; however, the franchise fees are included in the Company's revenues. We believe system sales growth is useful to investors as a significant indicator of the overall strength of our business as it incorporates all of our revenue drivers, Company and franchise same-store sales as well as net unit growth.
- Effective January 1, 2018, the Company revised its definition of same-store sales growth to represent the estimated percentage change in sales of food of all restaurants in the Company system that have been open prior to the first day of our prior fiscal year, excluding the period during which stores are temporarily closed. We refer to these as our "base" stores. Previously, same-store sales growth represented the estimated percentage change in sales of all restaurants in the Company system that have been open for one year or more, including stores temporarily closed, and the base stores changed on a rolling basis from month to month. This revision was made to align with how management measures performance internally and focuses on trends of a more stable base of stores.
- Company sales represent revenues from Company-owned restaurants. Company Restaurant profit ("Restaurant profit") is defined as Company sales less expenses incurred directly by our Company-owned restaurants in generating Company sales. Company restaurant margin percentage is defined as Restaurant profit divided by Company sales. Within the Company sales and Restaurant profit analysis, Store Portfolio Actions represent the net impact of new-unit openings, acquisitions, refranchising and store closures, and Other primarily represents the impact of same-store sales as well as the impact of changes in restaurant operating costs such as inflation/deflation.

All Note references in this MD&A refer to the Notes to the Condensed Consolidated Financial Statements. Tabular amounts are displayed in millions of U.S. dollars except percentages and per share and unit count amounts, or as otherwise specifically identified. Percentages may not recompute due to rounding. References to quarters are references to the Company's fiscal quarters.

Quarters and Years to Date Ended September 30, 2022 and 2021

Results of Operations

Summary

The Company has two reportable segments: KFC and Pizza Hut. Our remaining operating segments, including the operations of Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY, Taco Bell, East Dawning, Daojia and our e-commerce business, are combined and

referred to as All Other Segments, as those operating segments are insignificant both individually and in the aggregate. Additional details on our reportable operating segments are included in Note 14.

Quarterly highlights:

	% Change				
	System Sales ^(a)	Same-Store Sales ^(a)	Net New Units	Operating Profit (Reported)	Operating Profit (Ex F/X)
KFC	+5	—	+10	+67	+76
Pizza Hut	+7	+2	+12	+159	+169
All Other Segments ^(b)	(21)	(15)	(8)	(57)	(67)
Total	+5	—	+9	+77	+86

Year to date highlights:

	% Change				
	System Sales ^(a)	Same-Store Sales ^(a)	Net New Units	Operating Profit (Reported)	Operating Profit (Ex F/X)
KFC	(5)	(8)	+10	(12)	(10)
Pizza Hut	(3)	(6)	+12	(23)	(21)
All Other Segments ^(b)	(23)	(19)	(8)	NM	NM
Total	(5)	(8)	+9	(22)	(20)

NM refers to not meaningful.

(a) System sales and same-store sales percentages as shown in tables exclude the impact of F/X. Effective January 1, 2018, temporary store closures are normalized in the same-store sales calculation by excluding the period during which stores are temporarily closed.

(b) Sales from non-Company-owned restaurants, for which we do not receive a sales-based royalty, are excluded from system sales and same-store sales.

As of September 30, 2022, the Company operated over 12,000 units, predominately KFC and Pizza Hut restaurants, which are the leading and largest QSR and CDR brands, respectively, in mainland China in terms of system sales. We believe that there are significant opportunities to expand within China, and we intend to focus our efforts on increasing our geographic footprint in both existing and new cities.

The COVID-19 pandemic continued to impact the Company's operations and results in the third quarter. COVID-related health measures remained in effect across China, impacting travel and social activities. We captured the growing demand for delivery and takeaway, which offset the subdued dine-in volume. Same-store sales for the quarter recovered to the same level a year ago but remain below pre-COVID 2019 levels. From a timing perspective, same-store sales recovered sequentially in July and August with August exceeding the prior year level. This is primarily due to lapping the Delta variant outbreak in the prior year period. However, same-store sales percentage declined year over year in September as preventive health measures were tightened. In September, on average, approximately 900 of our stores were temporarily closed or offered only takeaway and delivery services, compared to approximately 400 stores on average in July and August.

As compared to the third quarter of 2021, Company sales in the third quarter of 2022 increased 11%, or 17% excluding the impact of F/X. Company sales for the year to date ended September 30, 2022 increased 4%, or 6% excluding the impact of F/X. The increase in Company sales for the quarter, excluding the impact of F/X, was driven by net unit growth of 19% in Company-owned stores including the acquisition of Hangzhou KFC, partially offset by temporary store closures due to the impact of the COVID-19 pandemic. The year to date increase in Company sales was driven by net unit growth of 19% including the acquisition of Hangzhou KFC, partially offset by same-store sales decline of 8% and substantially more temporary store closures due to the impact of the COVID-19 pandemic.

The increase in Operating profit for the quarter, excluding the impact of F/X, was primarily driven by the increase in Company sales, higher productivity and temporary relief. These factors were partially offset by inflation in commodities in the low single digits, wages of 2% and utility rates, increased rider cost associated with a rise of approximately four percentage points in delivery sales mix from the prior year period and higher compensation costs.

The year to date decrease in Operating profit, excluding the impact of F/X, was primarily driven by same-store sales decline, temporary store closures due to the impact of the COVID-19 pandemic, inflation in commodities in the low single digits, wages of 4% and utility rates, increased rider cost associated with a rise of approximately six percentage points in delivery sales mix from the prior year period due to more severe outbreaks and higher compensation costs. These factors were partially offset by higher productivity, temporary relief and the acquisition of Hangzhou KFC.

The Consolidated Results of Operations for the quarters and years to date ended September 30, 2022 and 2021 are presented below:

	Quarter Ended		% B/(W) ^(a)		Year to Date Ended		% B/(W) ^(a)	
	9/30/2022	9/30/2021	Reported	Ex F/X	9/30/2022	9/30/2021	Reported	Ex F/X
Company sales	\$ 2,561	\$ 2,310	11	17	\$ 7,135	\$ 6,874	4	6
Franchise fees and income	22	40	(45)	(42)	65	120	(46)	(45)
Revenues from transactions with franchisees and unconsolidated affiliates	80	184	(57)	(54)	219	519	(58)	(57)
Other revenues	22	20	11	17	62	49	27	29
Total revenues	\$ 2,685	\$ 2,554	5	11	\$ 7,481	\$ 7,562	(1)	1
Restaurant profit	\$ 480	\$ 282	71	79	\$ 1,076	\$ 1,071	1	3
Restaurant Margin %	18.8 %	12.2 %	6.6 ppts.	6.6 ppts.	15.1 %	15.6 %	(0.5) ppts.	(0.5) ppts.
Operating Profit	\$ 316	\$ 178	77	86	\$ 588	\$ 753	(22)	(20)
Interest income, net	25	16	51	54	51	47	8	10
Investment loss	(15)	(39)	61	61	(32)	(43)	26	26
Income tax provision	(97)	(44)	(121)	(130)	(183)	(210)	13	11
Equity in net earnings (losses) from equity method investments	(2)	—	NM	NM	(4)	—	NM	NM
Net Income – including noncontrolling interests	227	111	103	114	420	547	(23)	(21)
Net Income – noncontrolling interests	21	7	(171)	(187)	31	32	5	1
Net Income – Yum China Holdings, Inc.	\$ 206	\$ 104	98	109	\$ 389	\$ 515	(25)	(22)
Diluted Earnings Per Common Share	\$ 0.49	\$ 0.24	104	113	\$ 0.92	\$ 1.19	(23)	(21)
Effective tax rate	29.9 %	28.3 %			30.1 %	27.7 %		
Supplementary information – Non-GAAP Measures ^(b)								
Adjusted Operating Profit	\$ 318	\$ 168			\$ 593	\$ 750		
Adjusted Net Income – Yum China Holdings, Inc.	\$ 208	\$ 96			\$ 394	\$ 514		
Adjusted Diluted Earnings Per Common Share	\$ 0.49	\$ 0.22			\$ 0.93	\$ 1.18		
Adjusted Effective Tax Rate	29.7 %	28.8 %			29.9 %	27.6 %		
Adjusted EBITDA	\$ 475	\$ 300			\$ 1,097	\$ 1,153		

(a) Represents the period-over-period change in percentage.

(b) See “Non-GAAP Measures” below for definitions and reconciliations of the most directly comparable GAAP financial measures to the non-GAAP measures.

Performance Metrics

	Quarter Ended 9/30/2022	Year to Date Ended 9/30/2022
	% change	% change
System Sales Decline	(1)%	(7)%
System Sales Growth (Decline), excluding F/X	5%	(5)%
Same-Store Sales Growth (Decline)	—	(8)%

Unit Count	9/30/2022	9/30/2021	% Increase (Decrease)
	Company-owned ^(a)	10,679	8,938
Unconsolidated affiliates ^(a)	—	762	(100)
Franchisees	1,730	1,715	1
	12,409	11,415	9

(a) As a result of the acquisition of Hangzhou KFC in the fourth quarter of 2021, the restaurant units of Hangzhou KFC were transferred from unconsolidated affiliates to Company-owned.

Non-GAAP Measures

In addition to the results provided in accordance with GAAP throughout this MD&A, the Company provides non-GAAP measures adjusted for Special Items, which include Adjusted Operating Profit, Adjusted Net Income, Adjusted Earnings Per Common Share (“EPS”), Adjusted Effective Tax Rate and Adjusted EBITDA, which we define as net income including noncontrolling interests adjusted for equity in net earnings (losses) from equity method investments, income tax, interest income, net, investment gain or loss, certain non-cash expenses, consisting of depreciation and amortization as well as store impairment charges and Special Items.

The following table sets forth the reconciliations of the most directly comparable GAAP financial measures to the non-GAAP adjusted financial measures.

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Non-GAAP Reconciliations				
Reconciliation of Operating Profit to Adjusted Operating Profit				
Operating Profit	\$ 316	\$ 178	\$ 588	\$ 753
Special Items, Operating Profit	(2)	10	(5)	3
Adjusted Operating Profit	<u>\$ 318</u>	<u>\$ 168</u>	<u>\$ 593</u>	<u>\$ 750</u>
Reconciliation of Net Income to Adjusted Net Income				
Net Income – Yum China Holdings, Inc.	\$ 206	\$ 104	\$ 389	\$ 515
Special Items, Net Income – Yum China Holdings, Inc.	(2)	8	(5)	1
Adjusted Net Income – Yum China Holdings, Inc.	<u>\$ 208</u>	<u>\$ 96</u>	<u>\$ 394</u>	<u>\$ 514</u>
Reconciliation of EPS to Adjusted EPS				
Basic Earnings Per Common Share	\$ 0.49	\$ 0.25	\$ 0.92	\$ 1.23
Special Items, Basic Earnings Per Common Share	—	0.02	(0.01)	0.01
Adjusted Basic Earnings Per Common Share	<u>\$ 0.49</u>	<u>\$ 0.23</u>	<u>\$ 0.93</u>	<u>\$ 1.22</u>
Diluted Earnings Per Common Share	\$ 0.49	\$ 0.24	\$ 0.92	\$ 1.19
Special Items, Diluted Earnings Per Common Share	—	0.02	(0.01)	0.01
Adjusted Diluted Earnings Per Common Share	<u>\$ 0.49</u>	<u>\$ 0.22</u>	<u>\$ 0.93</u>	<u>\$ 1.18</u>
Reconciliation of Effective Tax Rate to Adjusted Effective Tax Rate				
Effective tax rate (See Note 13)	29.9%	28.3%	30.1%	27.7%
Impact on effective tax rate as a result of Special Items	0.2%	(0.5)%	0.2%	0.1%
Adjusted effective tax rate	<u>29.7%</u>	<u>28.8%</u>	<u>29.9%</u>	<u>27.6%</u>

Net income, along with the reconciliation to Adjusted EBITDA, is presented below.

	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Reconciliation of Net Income to Adjusted EBITDA				
Net Income – Yum China Holdings, Inc.	\$ 206	\$ 104	\$ 389	\$ 515
Net Income – noncontrolling interests	21	7	31	32
Equity in net (earnings) losses from equity method investments	2	—	4	—
Income tax provision	97	44	183	210
Interest income, net	(25)	(16)	(51)	(47)
Investment loss	15	39	32	43
Operating Profit	316	178	588	753
Special Items, Operating Profit	2	(10)	5	(3)
Adjusted Operating Profit	318	168	593	750
Depreciation and amortization	150	128	467	380
Store impairment charges	7	4	37	23
Adjusted EBITDA	<u>\$ 475</u>	<u>\$ 300</u>	<u>\$ 1,097</u>	<u>\$ 1,153</u>

Details of Special Items are presented below:

Details of Special Items	Quarter Ended		Year to Date Ended	
	9/30/2022	9/30/2021	9/30/2022	9/30/2021
Share-based compensation expense for Partner PSU Awards ⁽¹⁾	\$ (2)	\$ —	\$ (5)	\$ (7)
Gain from re-measurement of equity interest upon acquisition ⁽²⁾	—	10	—	10
Special Items, Operating Profit	(2)	10	(5)	3
Tax Expenses on Special Items ⁽³⁾	—	(2)	—	(2)
Special items, net income – including noncontrolling interests	(2)	8	(5)	1
Special items, net income – noncontrolling interests	—	—	—	—
Special Items, Net Income – Yum China Holdings, Inc.	\$ (2)	\$ 8	\$ (5)	\$ 1
Weighted-average diluted shares outstanding (in millions)	424	435	426	435
Special Items, Diluted Earnings Per Common Share	\$ —	\$ 0.02	\$ (0.01)	\$ 0.01

- (1) In February 2020, the Company granted Partner PSU Awards to select employees who were deemed critical to the Company's execution of its strategic operating plan. These PSU awards will only vest if threshold performance goals are achieved over a four-year performance period, with the payout ranging from 0% to 200% of the target number of shares subject to the PSU awards. Partner PSU Awards were granted to address increased competition for executive talent, motivate transformational performance and encourage management retention. Given the unique nature of these grants, the Compensation Committee does not intend to grant similar special grants to the same employees during the performance period. The impact from these special awards is excluded from metrics that management uses to assess the Company's performance. The Company recognized share-based compensation expenses of \$2 million and \$5 million associated with the Partner PSU Awards for the quarter and year to date ended September 30, 2022, respectively, and nil and \$7 million associated with the Partner PSU Awards for the quarter and year to date ended September 30, 2021, respectively.
- (2) In the quarter ended September 30, 2021, as a result of the consolidation of the Lavazza joint venture, the Company recognized a gain of \$10 million from the re-measurement of our previously held equity interest at fair value, which was not allocated to any segment for performance reporting purposes.
- (3) The tax expense was determined based upon the nature, as well as the jurisdiction, of each Special Item at the applicable tax rate.

The Company excludes impact from Special Items for the purpose of evaluating performance internally. Special Items are not included in any of our segment results. In addition, the Company provides Adjusted EBITDA because we believe that investors and analysts may find it useful in measuring operating performance without regard to items such as equity in net earnings (losses) from equity method investments, income tax, interest income, net investment gain or loss, depreciation and amortization, store impairment charges and Special Items. Store impairment charges included as an adjustment item in Adjusted EBITDA primarily resulted from our semi-annual impairment evaluation of long-lived assets of individual restaurants, and additional impairment evaluation whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. If these restaurant-level assets were not impaired, depreciation of the assets would have been recorded and included in EBITDA. Therefore, store impairment charges were a non-cash item similar to depreciation and amortization of our long-lived assets of restaurants. The Company believes that investors and analysts may find it useful in measuring operating performance without regard to such non-cash item.

These adjusted measures are not intended to replace the presentation of our financial results in accordance with GAAP. Rather, the Company believes that the presentation of these adjusted measures provides additional information to investors to facilitate the comparison of past and present results, excluding those items that the Company does not believe are indicative of our ongoing operations due to their nature.

Segment Results

KFC

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	9/30/2022	9/30/2021	Reported	Ex F/X	9/30/2022	9/30/2021	Reported	Ex F/X
Company sales	\$ 1,992	\$ 1,750	14	20	\$ 5,554	\$ 5,220	6	9
Franchise fees and income	15	32	(52)	(49)	44	95	(53)	(52)
Revenues from transactions with franchisees and unconsolidated affiliates	9	17	(47)	(44)	24	46	(48)	(47)
Other revenues	1	2	(33)	(29)	6	6	(1)	—
Total revenues	\$ 2,017	\$ 1,801	12	18	\$ 5,628	\$ 5,367	5	7
Restaurant profit	\$ 410	\$ 238	72	81	\$ 922	\$ 877	5	8
Restaurant margin %	20.6 %	13.6 %	7.0	7.0	16.6 %	16.8 %	(0.2)	(0.2)
G&A expenses	\$ 63	\$ 62	(1)	(7)	\$ 191	\$ 175	(9)	(11)
Franchise expenses	\$ 8	\$ 16	49	46	\$ 23	\$ 47	50	49
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 8	\$ 16	49	47	\$ 22	\$ 45	51	50
Other operating costs and expenses	\$ 1	\$ 2	5	(1)	\$ 4	\$ 3	(22)	(25)
Closures and impairment expenses, net	\$ 3	\$ 1	(114)	(130)	\$ 11	\$ 7	(40)	(48)
Other expenses (income), net	\$ 24	\$ (4)	NM	NM	\$ 75	\$ (16)	NM	NM
Operating Profit	\$ 328	\$ 196	67	76	\$ 670	\$ 763	(12)	(10)

	Quarter Ended 9/30/2022	Year to Date Ended 9/30/2022
	% change	% change
System Sales Growth (Decline)	—	(6)%
System Sales Growth (Decline), excluding F/X	5%	(5)%
Same-Store Sales Growth (Decline)	—	(8)%

Unit Count	9/30/2022	9/30/2021	% Increase (Decrease)
Company-owned ^(a)	7,852	6,450	22
Unconsolidated affiliates ^(a)	—	762	(100)
Franchisees	823	696	18
	8,675	7,908	10

(a) As a result of the acquisition of Hangzhou KFC in the fourth quarter of 2021, the restaurant units of Hangzhou KFC were transferred from unconsolidated affiliates to Company-owned.

Company Sales and Restaurant Profit

The changes in Company sales and Restaurant profit were as follows:

Income (Expense)	Quarter Ended				9/30/2022
	9/30/2021	Store Portfolio Actions	Other	F/X	
Company sales	\$ 1,750	\$ 362	\$ (9)	\$ (111)	\$ 1,992
Cost of sales	(567)	(105)	31	34	(607)
Cost of labor	(425)	(76)	26	26	(449)
Occupancy and other operating expenses	(520)	(79)	43	30	(526)
Restaurant profit	\$ 238	\$ 102	\$ 91	\$ (21)	\$ 410

Year to Date Ended

Income (Expense)	9/30/2021	Store Portfolio Actions	Other	F/X	9/30/2022
Company sales	\$ 5,220	\$ 859	\$ (411)	\$ (114)	\$ 5,554
Cost of sales	(1,629)	(260)	142	35	(1,712)
Cost of labor	(1,214)	(227)	52	26	(1,363)
Occupancy and other operating expenses	(1,500)	(234)	146	31	(1,557)
Restaurant profit	<u>\$ 877</u>	<u>\$ 138</u>	<u>\$ (71)</u>	<u>\$ (22)</u>	<u>\$ 922</u>

The increase in Company sales for the quarter, excluding the impact of F/X, was primarily driven by net unit growth including the acquisition of Hangzhou KFC, partially offset by temporary store closures due to the impact of the COVID-19 pandemic. The increase in Restaurant profit for the quarter, excluding the impact of F/X, was primarily driven by the increase in Company sales, higher productivity and temporary relief, partially offset by inflation in commodities in the low single digits, wages of 2% and utility rates, as well as increased rider cost associated with a rise of approximately four percentage points in delivery sales mix from the prior year period.

The year to date increase in Company sales, excluding the impact of F/X, was primarily driven by net unit growth including the acquisition of Hangzhou KFC, partially offset by same-store sales decline and temporary store closures due to the impact of the COVID-19 pandemic. The year to date increase in Restaurant profit, excluding the impact of F/X, was primarily driven by higher productivity and temporary relief, partially offset by inflation in commodities in the low single digits, wages of 4% and utility rates, as well as increased rider cost associated with a rise of approximately six percentage points in delivery sales mix from the prior year period due to more severe outbreaks.

Franchise Fees and Income/Revenues from Transactions with Franchisees and Unconsolidated Affiliates

The quarter and year to date decrease in Franchise fees and income and Revenues from transactions with franchisees and unconsolidated affiliates, excluding the impact of F/X, was primarily driven by the acquisition of Hangzhou KFC in December 2021.

G&A Expenses

The quarter and year to date increase in G&A expenses, excluding the impact of F/X, was primarily driven by the acquisition of Hangzhou KFC in December 2021 and merit increases.

Operating Profit

The increase in Operating profit for the quarter, excluding the impact of F/X, was primarily driven by the increase in Restaurant profit, partially offset by higher amortization of reacquired franchise rights as well as lower equity income as a result of the acquisition of Hangzhou KFC and higher G&A expenses.

The year to date decrease in Operating profit, excluding the impact of F/X, was primarily driven by higher amortization of reacquired franchise rights as well as lower equity income as a result of the acquisition of Hangzhou KFC and higher G&A expenses, partially offset by the increase in Restaurant profit.

	Quarter Ended				Year to Date Ended			
	9/30/2022	9/30/2021	% B/(W)		9/30/2022	9/30/2021	% B/(W)	
			Reported	Ex F/X			Reported	Ex F/X
Company sales	\$ 556	\$ 546	2	7	\$ 1,541	\$ 1,617	(5)	(3)
Franchise fees and income	2	2	(9)	(4)	6	6	(1)	1
Revenues from transactions with franchisees and unconsolidated affiliates	1	2	(33)	(29)	3	5	(35)	(34)
Other revenues	2	1	158	175	6	2	NM	NM
Total revenues	<u>\$ 561</u>	<u>\$ 551</u>	<u>2</u>	<u>8</u>	<u>\$ 1,556</u>	<u>\$ 1,630</u>	<u>(4)</u>	<u>(2)</u>
Restaurant profit	\$ 75	\$ 44	67	75	\$ 171	\$ 196	(13)	(11)
Restaurant margin %	13.4 %	8.2 %	5.2 ppts.	5.2 ppts.	11.1 %	12.2 %	(1.1) ppts.	(1.1) ppts.
G&A expenses	\$ 27	\$ 27	1	(5)	\$ 84	\$ 80	(5)	(7)
Franchise expenses	\$ 1	\$ 1	10	5	\$ 3	\$ 3	6	5
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 1	\$ 2	30	26	\$ 3	\$ 5	34	32
Other operating costs and expenses	\$ 2	\$ 1	(199)	(220)	\$ 5	\$ 1	NM	NM
Closures and impairment expenses, net	\$ —	\$ —	(36)	(54)	\$ 1	\$ 3	85	86
Operating Profit	\$ 49	\$ 18	159	169	\$ 90	\$ 117	(23)	(21)

	Quarter Ended 9/30/2022	Year to Date Ended 9/30/2022
	% change	% change
System Sales Growth (Decline)	2 %	(5) %
System Sales Growth (Decline), excluding F/X	7 %	(3) %
Same-Store Sales Growth (Decline)	2 %	(6) %

Unit Count	9/30/2022	9/30/2021	% Increase
Company-owned	2,666	2,369	13
Franchisees	140	134	4
	<u>2,806</u>	<u>2,503</u>	<u>12</u>

Company Sales and Restaurant Profit

The changes in Company sales and Restaurant profit were as follows:

Income (Expense)	Quarter Ended				
	9/30/2021	Store Portfolio Actions	Other	F/X	9/30/2022
Cost of sales	(173)	(9)	(3)	9	(176)
Cost of labor	(161)	(9)	11	10	(149)
Occupancy and other operating expenses	(168)	(8)	11	9	(156)
Restaurant profit	<u>\$ 44</u>	<u>\$ 5</u>	<u>\$ 28</u>	<u>\$ (2)</u>	<u>\$ 75</u>

Income (Expense)	Year to Date Ended				
	9/30/2021	Store Portfolio Actions	Other	F/X	9/30/2022
Cost of sales	(493)	(12)	14	10	(481)
Cost of labor	(450)	(20)	23	10	(437)
Occupancy and other operating expenses	(478)	(17)	34	9	(452)
Restaurant profit	<u>\$ 196</u>	<u>\$ (10)</u>	<u>\$ (12)</u>	<u>\$ (3)</u>	<u>\$ 171</u>

The increase in Company sales for the quarter, excluding the impact of F/X, was primarily driven by net unit growth and same-store sales growth, partially offset by temporary store closures due to the impact of the COVID-19 pandemic. The increase in Restaurant profit for the quarter, excluding the impact of F/X, was primarily driven by the increase in Company sales, higher productivity and temporary relief, partially offset by inflation in commodities in the low single digits, wages of 2% and utility rates.

The year to date decrease in Company sales, excluding the impact of F/X, was primarily driven by same-store sales decline and temporary store closures due to the impact of the COVID-19 pandemic, partially offset by net unit growth. The year to date decrease in Restaurant profit, excluding the impact of F/X, was primarily driven by the decrease in Company sales and inflation in commodities in the low single digits, wages of 5% and utility rates, partially offset by higher productivity and temporary relief.

G&A Expenses

The quarter and year to date increase in G&A expenses, excluding the impact of F/X, was primarily driven by merit increases.

Operating Profit

The increase in Operating profit for the quarter, excluding the impact of F/X, was primarily driven by the increase in Restaurant profit, partially offset by higher G&A expenses.

The year to date decrease in Operating profit, excluding the impact of F/X, was primarily driven by the decrease in Restaurant profit and higher G&A expenses.

All Other Segments

All Other Segments reflects the results of Little Sheep, Huang Ji Huang, Lavazza, COFFii & JOY, Taco Bell, East Dawning, Daojia and our e-commerce business.

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	9/30/2022	9/30/2021	Reported	Ex F/X	9/30/2022	9/30/2021	Reported	Ex F/X
Company sales	\$ 13	\$ 14	(1)	5	\$ 40	\$ 37	10	12
Franchise fees and income	5	6	(22)	(17)	15	19	(21)	(20)
Revenues from transactions with franchisees and unconsolidated affiliates	11	26	(59)	(57)	29	75	(63)	(62)
Other revenues	157	88	77	87	407	187	118	123
Total revenues	<u>\$ 186</u>	<u>\$ 134</u>	38	46	<u>\$ 491</u>	<u>\$ 318</u>	54	57
Restaurant loss	\$ (5)	\$ —	NM	NM	\$ (15)	\$ (3)	NM	NM
Restaurant margin %	(30.6)%	(9.5)%	(21.1) ppts.	(21.1) ppts.	(36.3)%	(10.0)%	(26.3) ppts.	(26.3) ppts.
G&A expenses	\$ 12	\$ 11	(12)	(19)	\$ 36	\$ 30	(20)	(23)
Franchise expenses	\$ —	\$ —	31	27	\$ 1	\$ —	NM	NM
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 9	\$ 24	62	59	\$ 24	\$ 69	65	64
Other operating costs and expenses	\$ 155	\$ 87	(76)	(87)	\$ 406	\$ 183	NM	NM
Closures and impairment expenses, net	\$ 1	\$ 1	(151)	(167)	\$ 8	\$ 3	NM	NM
Other expenses, net	\$ —	\$ 3	NM	NM	\$ —	\$ 8	NM	NM
Operating Loss	\$ (9)	\$ (6)	(57)	(67)	\$ (39)	\$ (15)	NM	NM

	Quarter Ended 9/30/2022	Year to Date Ended 9/30/2022
	% change	% change
Same-Store Sales Decline	(15)%	(19)%

Total Revenues

The quarter and year to date increase in Total revenues of all other segments, excluding the impact of F/X, was primarily driven by inter-segment revenue generated by our delivery team for services provided to KFC and Pizza Hut restaurants and the contribution of sales from the Lavazza joint venture, partially offset by same-store sales decline and temporary store closures due to the impact of the COVID-19 pandemic.

Restaurant Loss

The quarter and year to date increase in Restaurant loss, excluding the impact of F/X, was primarily driven by the loss incurred by the Lavazza joint venture, same-store sales decline and temporary store closures due to the impact of the COVID-19 pandemic.

G&A Expenses

The quarter and year to date increase in G&A expenses, excluding the impact of F/X, was primarily driven by G&A expenses incurred by the Lavazza joint venture.

Operating Loss

The quarter and year to date increase in Operating loss, excluding the impact of F/X, was primarily driven by the increase of Operating loss from certain emerging brands due to the impact of the COVID-19 pandemic.

Corporate and Unallocated

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	9/30/2022	9/30/2021	Reported	Ex F/X	9/30/2022	9/30/2021	Reported	Ex F/X
Revenues from transactions with franchisees and unconsolidated affiliates	\$ 59	\$ 139	(58)	(55)	\$ 163	\$ 393	(58)	(58)
Other revenues	\$ 12	\$ 7	73	80	\$ 31	\$ 11	NM	NM
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 58	\$ 138	58	55	\$ 163	\$ 390	58	57
Other operating costs and expenses	\$ 10	\$ 5	(68)	(78)	\$ 28	\$ 10	NM	NM
Corporate G&A expenses	\$ 55	\$ 42	(31)	(37)	\$ 138	\$ 123	(12)	(14)
Other unallocated income, net	\$ —	\$ (9)	(97)	(97)	\$ (2)	\$ (7)	(81)	(80)
Interest income, net	\$ 25	\$ 16	51	54	\$ 51	\$ 47	8	10
Investment loss	\$ (15)	\$ (39)	61	61	\$ (32)	\$ (43)	26	26
Income tax provision (See Note 13)	\$ (97)	\$ (44)	(121)	(130)	\$ (183)	\$ (210)	13	11
Equity in net earnings (losses) from equity method investments	\$ (2)	\$ —	NM	NM	\$ (4)	\$ —	NM	NM
Effective tax rate (See Note 13)	29.9%	28.3%	(1.6)%	(1.6)%	30.1%	27.7%	(2.4)%	(2.4)%

Revenues from Transactions with Franchisees and Unconsolidated Affiliates

Revenues from transactions with franchisees and unconsolidated affiliates primarily include revenues derived from the Company's central procurement model, whereby food and paper products are centrally purchased and then mainly sold to KFC and Pizza Hut franchisees and unconsolidated affiliates that operate our concepts. The quarter and year to date decrease, excluding the impact of F/X, was mainly due to the acquisition of Hangzhou KFC in December 2021.

Other Revenues/Operating Costs and Expenses

The quarter and year to date increase in Other revenues/operating costs and expenses, excluding the impact of F/X, was mainly driven by logistics and warehousing services provided to third parties.

G&A Expenses

The quarter and year to date increase in Corporate G&A expenses, excluding the impact of F/X, was primarily due to higher compensation costs and one-time professional fees incurred for the Primary Conversion on the HKEX.

Investment Loss

The Investment loss mainly relates to the change in fair value of our investment in Meituan, as well as our unrealized investment loss in Sunner recognized in 2021. See Note 7 for additional information.

Income Tax Provision

Our income tax provision includes tax on our earnings at the Chinese statutory tax rate of 25%, withholding tax on repatriation of earnings outside of China and U.S. corporate income tax, if any. The higher effective tax rate for the quarter ended September 30, 2022

was primarily due to a prior year tax benefit from equity income from investments in unconsolidated affiliates. The higher effective tax rate for the year to date ended September 30, 2022 was primarily due to a prior year tax benefit from equity income from investments in unconsolidated affiliates and impact of lower pre-tax income.

Significant Known Events, Trends or Uncertainties Expected to Impact Future Results

Impact of COVID-19 Pandemic

Starting in late January 2020, the COVID-19 pandemic has significantly impacted the Company's operations and financial results. The COVID-19 pandemic continued to affect the restaurant industry and our operations in the third quarter of 2022. Entering the fourth quarter, new infections continued to increase in October with resurgent outbreaks across China. In October, approximately 1,400 of our stores were either temporarily closed or offered only takeaway and delivery services. According to government data, nationwide, consumers are traveling less and reducing expenditures during the seven-day National Day holiday starting October 1, compared to the same holiday period last year. The COVID situations remain uncertain with regional outbreaks continuing to impact our operations.

Management at this time cannot ascertain the extent to which our operations will continue to be impacted by the COVID-19 pandemic, which depends largely on future developments that are highly uncertain and cannot be accurately predicted, including resurgences and further spread of existing or new COVID-19 variants, the actions by government authorities to contain or treat its impact, the availability and effectiveness of vaccines, the economic recovery within China and globally, the impact on consumer behavior and other related factors. The Company expects that further developments related to the COVID-19 pandemic may continue to have a material and extended adverse impact on the Company's results of operations, as well as the Company's cash flows and financial condition.

Tax Examination on Transfer Pricing

We are subject to reviews, examinations and audits by Chinese tax authorities, the Internal Revenue Service and other tax authorities with respect to income and non-income based taxes. Since 2016, we have been under a national audit on transfer pricing by the STA in China regarding our related party transactions for the period from 2006 to 2015. The information and views currently exchanged with the tax authorities focus on our franchise arrangement with YUM. We continue to provide information requested by the tax authorities to the extent it is available to the Company. It is reasonably possible that there could be significant developments, including expert review and assessment by the STA, within the next 12 months. The ultimate assessment and decision of the STA will depend upon further review of the information provided, as well as ongoing technical and other discussions with the STA and in-charge local tax authorities, and therefore it is not possible to reasonably estimate the potential impact at this time. We will continue to defend our transfer pricing position. However, if the STA prevails in the assessment of additional tax due based on its ruling, the assessed tax, interest and penalties, if any, could have a material adverse impact on our financial position, results of operations and cash flows.

PRC Value-Added Tax ("VAT")

Effective May 1, 2016, a 6% output VAT replaced the 5% business tax ("BT") previously applied to certain restaurant sales. Input VAT would be creditable to the aforementioned 6% output VAT. The latest VAT rates imposed on our purchase of materials and services included 13%, 9% and 6%, which were gradually changed from 17%, 13%, 11% and 6% since 2017. These rate changes impact our input VAT on all materials and certain services, mainly including construction, transportation and leasing. However, the impact on our operating results is not expected to be significant.

Entities that are VAT general taxpayers are permitted to offset qualified input VAT paid to suppliers against their output VAT upon receipt of appropriate supplier VAT invoices on an entity-by-entity basis. When the output VAT exceeds the input VAT, the difference is remitted to tax authorities, usually on a monthly basis; whereas when the input VAT exceeds the output VAT, the difference is treated as a VAT asset which can be carried forward indefinitely to offset future net VAT payables. VAT related to purchases and sales which have not been settled at the balance sheet date is disclosed separately as an asset and liability, respectively, on the Condensed Consolidated Balance Sheets. At each balance sheet date, the Company reviews the outstanding balance of any VAT asset for recoverability, giving consideration to the indefinite life of VAT assets as well as its forecasted operating results and capital spending, which inherently includes significant assumptions that are subject to change. As of September 30, 2022, the Company has not made an allowance for the recoverability of VAT assets, as the balance is expected to be utilized to offset against VAT payables or be refunded in the future.

On June 7, 2022, the Chinese Ministry of Finance and the STA jointly issued Circular [2022] No. 21, to extend full VAT credit refunds to more sectors and increase the frequency for accepting taxpayers' applications with an aim to support business recovery. Beginning

on July 1, 2022, entities engaged in providing catering services in China are allowed to apply for a lump sum refund of VAT assets accumulated prior to March 31, 2019. In addition, VAT assets accumulated after March 31, 2019 can be refunded on a monthly basis.

As the benefits of certain VAT assets are expected to be realized within one year pursuant to Circular [2022] No. 21, \$303 million of VAT assets as of June 30, 2022 were reclassified from Other assets to Prepaid expense and other current assets. As of September 30, 2022, VAT assets of \$93 million, \$4 million and net VAT payable of \$12 million were recorded in Prepaid expense and other current assets, Other assets and Accounts payable and other current liabilities, respectively, on the Condensed Consolidated Balance Sheets.

The Company will continue to review the classification of VAT assets at each balance sheet date, giving consideration to the different local implementation practice of refunding the VAT assets and results of the potential administrative review.

We have been benefiting from the retail tax structure reform since it was implemented on May 1, 2016. However, the amount of our expected benefit from this VAT regime depends on a number of factors, some of which are outside of our control. The interpretation and application of the new VAT regime are not settled at some local governmental levels. In addition, the timetable for enacting the prevailing VAT regulations into national VAT law, including ultimate enacted VAT rates, is not clear. As a result, for the foreseeable future, the benefit of this significant and complex VAT reform has the potential to fluctuate from quarter to quarter.

Foreign Currency Exchange Rate

The reporting currency of the Company is the US\$. Most of the revenues, costs, assets and liabilities of the Company are denominated in Chinese Renminbi (“RMB”). Any significant change in the exchange rate between US\$ and RMB may materially affect the Company’s business, results of operations, cash flows and financial condition, depending on the weakening or strengthening of RMB against the US\$. See “Item 3. Quantitative and Qualitative Disclosures About Market Risk” for further discussion.

Condensed Consolidated Cash Flows

Our cash flows for the years to date ended September 30, 2022 and 2021 were as follows:

Net cash provided by operating activities was \$1,329 million in 2022 as compared to \$1,074 million in 2021. The increase was primarily driven by refunds of VAT assets. See Note 9.

Net cash used in investing activities was \$593 million in 2022 as compared to \$743 million in 2021. The decrease was mainly due to lapping the impact of \$261 million cash consideration for the acquisition of equity investment in Sunner in 2021, partially offset by the net impact on cash flow resulting from purchases and maturities of short-term investments and an increase in capital spending.

Net cash used in financing activities was \$583 million in 2022 as compared to \$220 million in 2021. The increase was primarily due to the resumption of share repurchases starting in the third quarter of 2021.

Liquidity and Capital Resources

Historically we have funded our operations through cash generated from the operation of our Company-owned stores, our franchise operations and dividend payments from our unconsolidated affiliates. Our global offering in September 2020 provided us with \$2.2 billion in net proceeds.

Our ability to fund our future operations and capital needs will primarily depend on our ongoing ability to generate cash from operations. We believe our principal uses of cash in the future will be primarily to fund our operations and capital expenditures for accelerating store network expansion and store remodeling, to step up investments in digitalization, automation and logistics infrastructure, to provide returns to our stockholders, as well as to explore opportunities for acquisitions or investments that build and support our ecosystem. We believe that our future cash from operations, together with our funds on hand and access to the capital markets, will provide adequate resources to fund these uses of cash, and that our existing cash, net cash from operations and credit facilities will be sufficient to fund our operations and anticipated capital expenditures for the next 12 months.

If our cash flows from operations are less than we require, we may need to access the capital markets to obtain financing. Our access to, and the availability of, financing on acceptable terms and conditions in the future or at all will be impacted by many factors, including, but not limited to:

- our financial performance;
- our credit ratings;
- the liquidity of the overall capital markets; and
- the state of the Chinese, U.S. and global economies, as well as relations between the Chinese and U.S. governments.

There can be no assurance that we will have access to the capital markets on terms acceptable to us or at all.

Generally our income is subject to the Chinese statutory tax rate of 25%. However, to the extent our cash flows from operations exceed our China cash requirements, the excess cash may be subject to an additional 10% withholding tax levied by the Chinese tax authority, subject to any reduction or exemption set forth in relevant tax treaties or tax arrangements.

Share Repurchases and Dividends

In March 2022, our Board of Directors increased the share repurchase authorization by \$1 billion to an aggregate of \$2.4 billion. Yum China may repurchase shares under this program from time to time in open market or privately negotiated transactions, including block trades, accelerated share repurchase transactions and the use of Rule 10b5-1 trading plans. Starting in the second quarter of 2020 through July 2021, our share repurchases were suspended due to the impact of the COVID-19 pandemic. During the years to date ended September 30, 2022 and 2021, the Company repurchased \$413 million or 9 million shares and \$34 million or 0.6 million shares of common stock, respectively, under the repurchase program.

For the quarters ended September 30, 2022 and 2021, the Company paid cash dividends of approximately \$51 million and \$51 million, respectively, to stockholders through a quarterly dividend payment of \$0.12 per share.

On November 1, 2022, the Board of Directors declared a cash dividend of \$0.12 per share, payable on December 20, 2022, to stockholders of record as of the close of business on November 29, 2022. The total estimated cash dividend payable is approximately \$50 million.

Our ability to declare and pay any dividends on our stock may be restricted by our earnings available for distribution under applicable Chinese laws. The laws, rules and regulations applicable to our Chinese subsidiaries permit payments of dividends only out of their accumulated profits, if any, determined in accordance with applicable Chinese accounting standards and regulations. Under Chinese law, an enterprise incorporated in China is required to set aside at least 10% of its after-tax profits each year, after making up previous years' accumulated losses, if any, to fund certain statutory reserve funds, until the aggregate amount of such a fund reaches 50% of its registered capital. As a result, our Chinese subsidiaries are restricted in their ability to transfer a portion of their net assets to us in the form of dividends. At the discretion of the Board of Directors, as an enterprise incorporated in China, each of our Chinese subsidiaries may allocate a portion of its after-tax profits based on Chinese accounting standards to staff welfare and bonus funds. These reserve funds and staff welfare and bonus funds are not distributable as cash dividends.

Borrowing Capacity

As of September 30, 2022, the Company had credit facilities of RMB3,766 million (approximately \$529 million), comprised of onshore credit facilities of RMB2,200 million (approximately \$309 million) in aggregate and offshore credit facilities of \$220 million in aggregate.

The credit facilities had remaining terms ranging from less than one year to two years as of September 30, 2022. Each credit facility bears interest based on the Loan Prime Rate ("LPR") published by the National Interbank Funding Centre of the PRC, London Interbank Offered Rate ("LIBOR") administered by the ICE Benchmark Administration, or Secured Overnight Financing Rate ("SOFR") published by the Federal Reserve Bank of New York. Each credit facility contains a cross-default provision whereby our failure to make any payment on a principal amount from any credit facility will constitute a default on other credit facilities. Some of the credit facilities

contain covenants limiting, among other things, certain additional indebtedness and liens, and certain other transactions specified in the respective agreement. Some of the onshore credit facilities contain sub-limits for overdrafts, non-financial bonding, standby letters of credit and guarantees. As of September 30, 2022, we had outstanding bank guarantees of RMB189 million (approximately \$27 million) mainly to secure our lease payments to landlords for certain Company-owned restaurants. The credit facilities were therefore reduced by the same amount, while there were no bank borrowings outstanding as of September 30, 2022.

Off-Balance Sheet Arrangements

See the Guarantees section of Note 15 for discussion of our off-balance sheet arrangements.

New Accounting Pronouncements

Recently Adopted Accounting Pronouncements

See Note 2 for details of recently adopted accounting pronouncements.

New Accounting Pronouncements Not Yet Adopted

In October 2021, the FASB issued ASU 2021-08, *Business Combinations (Topic 805) — Accounting for Contract Assets and Contract Liabilities from Contracts with Customers* (“ASU 2021-08”). It requires issuers to apply ASC 606 *Revenue from Contracts with Customers* to recognize and measure contract assets and contract liabilities from contracts with customers acquired in a business combination. ASU 2021-08 is effective for the Company from January 1, 2023, with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

In November 2021, the FASB issued ASU 2021-10, *Government Assistance (Topic 832) — Disclosures by Business Entities about Government Assistance* (“ASU 2021-10”). It requires issuers to make annual disclosures about government assistance, including the nature of the transaction, the related accounting policy, the financial statement line items affected and the amounts applicable to each financial statement line item, as well as any significant terms and conditions, including commitments and contingencies. We will adopt ASU 2021-10 in the fourth quarter of 2022, and do not expect the adoption of this standard will have a material impact on our financial statements.

In March 2022, the FASB issued ASU 2022-01 *Fair Value Hedging—Portfolio Layer Method* (“ASU 2022-01”), which allows entities to expand their use of the portfolio layer method for fair value hedges of interest rate risk. Under the guidance, entities can hedge all financial assets under the portfolio layer method and designate multiple hedged layers within a single closed portfolio. The guidance also clarifies the accounting for fair value hedge basis adjustments in portfolio layer hedges and how these adjustments should be disclosed. ASU 2022-01 is effective for the Company from January 1, 2023 with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

In March 2022, the FASB issued ASU 2022-02 *Financial Instrument—Credit Losses* (“ASU 2022-02”), amending ASC 310 to eliminate the recognition and measurement guidance for a troubled debt restructuring for creditors that have adopted ASC 326 and requiring them to make enhanced disclosures about loan modifications for borrowers experiencing financial difficulty. The guidance also requires entities to present gross write-offs by year of origination in their vintage disclosures. ASU 2022-02 is effective for the Company from January 1, 2023 with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

In June 2022, the FASB issued ASU 2022-03 *Fair Value Measurement—Fair Value Measurement of Equity Securities Subject to Contractual Sale Restriction* (“ASU 2022-03”), clarifying that a contractual restriction on the sales of an equity security is not considered part of the unit of account of the equity security, and therefore, is not considered when measuring fair value. The guidance also clarifies that a contractual sales restriction should not be recognized as a separate unit of account. ASU 2022-03 is effective for the Company from January 1, 2024 with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

In September 2022, the FASB issued ASU 2022-04 *Liabilities—Disclosure of Supplier Finance Program Obligations* (“ASU 2022-04”), requiring entities that use supplier finance programs in connection with the purchase of goods and services to disclose the key terms of the programs and information about their obligations outstanding at the end of the reporting period. ASU 2022-04 is effective for the Company from January 1, 2023 with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

Cautionary Note Regarding Forward-Looking Statements

Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. These statements often include words such as “may,” “will,” “estimate,” “intend,” “seek,” “expect,” “project,” “anticipate,” “believe,” “plan,” “could,” “target,” “aim,” “commit,” “predict,” “likely,” “should,” “forecast,” “outlook,” “model,” “continue,” “ongoing” or other similar terminology. Forward-looking statements are based on our expectations, estimates, assumptions or projections concerning future results or events as of the date of the filing of this Form 10-Q. Forward-looking statements are neither predictions nor guarantees of future events, circumstances or performance and are inherently subject to known and unknown risks, uncertainties and assumptions that could cause our actual results and events to differ materially from those indicated by those statements. We cannot assure you that any of our assumptions are correct or any of our expectations, estimates or projections will be achieved. Numerous factors could cause our actual results to differ materially from those expressed or implied by forward-looking statements, including, without limitation, the following:

- Risks related to our business and industry, such as (a) food safety and foodborne illness concerns, (b) significant failure to maintain effective quality assurance systems for our restaurants, (c) significant liability claims, food contamination complaints from our customers or reports of incidents of food tampering, (d) health concerns arising from outbreaks of viruses or other illnesses, including the COVID-19 pandemic, (e) the fact that the operation of our restaurants is subject to the terms of the master license agreement with YUM, (f) the fact that substantially all of our revenue is derived from our operations in China, (g) the fact that our success is tied to the success of YUM’s brand strength, marketing campaigns and product innovation, (h) shortages or interruptions in the availability and delivery of food products and other supplies, (i) fluctuation of raw materials prices, (j) our inability to attain our target development goals, the potential cannibalization of existing sales by aggressive development and the possibility that new restaurants will not be profitable, (k) risks associated with leasing real estate, (l) inability to obtain desirable restaurant locations on commercially reasonable terms, (m) labor shortages or increases in labor costs, (n) the fact that our success depends substantially on our corporate reputation and on the value and perception of our brands, (o) the occurrence of security breaches and cyber-attacks, (p) failure to protect the integrity and security of our customer or employee personal, financial or other data or our proprietary or confidential information that is stored in our information systems or by third parties on our behalf, (q) failures or interruptions of service or security breaches in our information technology systems, (r) the fact that our business depends on the performance of, and our long-term relationships with, third-party mobile payment processors, internet infrastructure operators, internet service providers and delivery aggregators, (s) failure to provide timely and reliable delivery services by our restaurants, (t) our growth strategy with respect to Lavazza and COFFi & JOY may not be successful, (u) the anticipated benefits of our acquisitions may not be realized in a timely manner or at all, (v) challenges and risks related to our new retail and e-commerce businesses, (w) our inability or failure to recognize, respond to and effectively manage the impact of social media, (x) failure to comply with anti-bribery or anti-corruption laws, (y) U.S. federal income taxes, changes in tax rates, disagreements with tax authorities and imposition of new taxes, (z) changes in consumer discretionary spending and general economic conditions, (aa) the fact that the restaurant industry in which we operate is highly competitive, (bb) loss of or failure to obtain or renew any or all of the approvals, licenses and permits to operate our business, (cc) our inability to adequately protect the intellectual property we own or have the right to use, (dd) our licensor’s failure to protect its intellectual property, (ee) seasonality and certain major events in China, (ff) our failure to detect, deter and prevent all instances of fraud or other misconduct committed by our employees, customers or other third parties, (gg) the fact that our success depends on the continuing efforts of our key management and experienced and capable personnel as well as our ability to recruit new talent, (hh) our strategic investments or acquisitions may be unsuccessful; (ii) our investment in technology and innovation may not generate the expected level of returns, (jj) fair value changes for our investment in equity securities and lower yields of our short-term investments may adversely affect our financial condition and results of operations, and (kk) our operating results may be adversely affected by our investment in unconsolidated affiliates;
- Risks related to doing business in China, such as (a) changes in Chinese political policies and economic and social policies or conditions, (b) uncertainties with respect to the interpretation and enforcement of Chinese laws, rules and regulations, (c) audit reports included in our annual reports are prepared by auditors who are not currently inspected by the Public Company Accounting Oversight Board and, as such, our stockholders are deprived of the benefits of such inspection and our common stock is subject to the risk of delisting from the New York Stock Exchange in the future, (d) changes in political, business, economic and trade relations between the United States and China, (e) fluctuation in the value of the Chinese Renminbi, (f) the fact that we face increasing focus on environmental sustainability issues, (g) limitations on our ability to utilize our cash balances effectively due to governmental control of currency conversion and payments of foreign currency and the Chinese Renminbi out of mainland China, (h) changes in the laws and regulations of China or noncompliance with applicable laws and regulations, (i) reliance on dividends and other distributions on equity paid by our principal subsidiaries in China to fund offshore cash requirements, (j) potential unfavorable tax consequences resulting from our classification as a China resident enterprise for Chinese enterprise income tax purposes, (k) uncertainty regarding indirect transfers of equity interests in China resident enterprises and enhanced scrutiny by Chinese tax authorities, (l) difficulties in effecting service of legal process, conducting investigations, collecting evidence, enforcing foreign judgments or bringing original actions in China against us,

(m) the Chinese government may determine that the variable interest entity structure of Daojia does not comply with Chinese laws on foreign investment in restricted industries, (n) inability to use properties due to defects caused by non-registration of lease agreements related to certain properties, (o) risk in relation to unexpected land acquisitions, building closures or demolitions, (p) potential fines and other legal or administrative sanctions for failure to comply with Chinese regulations regarding our employee equity incentive plans and various employee benefit plans, (q) proceedings instituted by the SEC against certain China-based accounting firms, including our independent registered public accounting firm, could result in our financial statements being determined to not be in compliance with the requirements of the Exchange Act, (r) restrictions on our ability to make loans or additional capital contributions to our Chinese subsidiaries due to Chinese regulation of loans to, and direct investment in, Chinese entities by offshore holding companies and governmental control of currency conversion, and (s) difficulties in pursuing growth through acquisitions due to regulations regarding acquisitions;

- Risks related to the separation and related transactions, such as (a) incurring significant tax liabilities if the distribution does not qualify as a transaction that is generally tax-free for U.S. federal income tax purposes and the Company could be required to indemnify YUM for material taxes and other related amounts pursuant to indemnification obligations under the tax matters agreement, (b) being obligated to indemnify YUM for material taxes and related amounts pursuant to indemnification obligations under the tax matters agreement if YUM is subject to Chinese indirect transfer tax with respect to the distribution, (c) potential indemnification liabilities owing to YUM pursuant to the separation and distribution agreement, (d) the indemnity provided by YUM to us with respect to certain liabilities in connection with the separation may be insufficient to insure us against the full amount of such liabilities, (e) the possibility that a court would require that we assume responsibility for obligations allocated to YUM under the separation and distribution agreement, and (f) potential liabilities due to fraudulent transfer considerations;
- General risks, such as (a) potential legal proceedings, (b) changes in accounting standards and subjective assumptions, estimates and judgments by management related to complex accounting matters, (c) failure of our insurance policies to provide adequate coverage for claims associated with our business operations, (d) unforeseeable business interruptions, and (e) failure by us to maintain effective disclosure controls and procedures and internal control over financial reporting in accordance with the rules of the SEC.

In addition, other risks and uncertainties not presently known to us or that we currently believe to be immaterial could affect the accuracy of any such forward-looking statements. All forward-looking statements should be evaluated with the understanding of their inherent uncertainty. You should consult our filings with the SEC (including the information set forth under the captions “Management’s Discussion and Analysis of Financial Condition and Results of Operations” and “Risk Factors” included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2021 and Quarterly Report on Form 10-Q for the quarter ended March 31, 2022) for additional information regarding factors that could affect our financial and other results. You should not place undue reliance on forward-looking statements, which speak only as of the date of the filing of this Form 10-Q. We are not undertaking to update any of these statements, except as required by law.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency Exchange Rate Risk

Changes in foreign currency exchange rates impact the translation of our reported foreign currency denominated earnings, cash flows and net investments in foreign operations, virtually all of which are denominated in RMB. While substantially all of our supply purchases are denominated in RMB, from time to time, we enter into agreements at predetermined exchange rates with third parties to purchase certain amount of goods and services sourced overseas and make payments in the corresponding local currencies when practical, to minimize the related foreign currency exposure with immaterial impact on our financial statements.

As substantially all of the Company’s assets are located in China, the Company is exposed to movements in the RMB foreign currency exchange rate. For the quarter ended September 30, 2022, the Company’s Operating profit would have decreased by approximately \$30 million if the RMB weakened 10% relative to the US\$. This estimated reduction assumes no changes in sales volumes or local currency sales or input prices.

Commodity Price Risk

We are subject to volatility in food costs as a result of market risks associated with commodity prices. Our ability to recover increased costs through higher pricing is, at times, limited by the competitive environment in which we operate. We manage our exposure to this risk primarily through pricing agreements with our vendors.

Investment Risk

In September 2018, we invested \$74 million in 8.4 million of Meituan's ordinary shares. The Company sold 4.2 million of its ordinary shares of Meituan in the second quarter of 2020 for proceeds of approximately \$54 million. Equity investment in Meituan is recorded at fair value, which is measured on a recurring basis and is subject to market price volatility. See Note 3 for further discussion on our investment in Meituan.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

The Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures pursuant to Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 as of the end of the period covered by this report. Based on the evaluation, performed under the supervision and with the participation of the Company's management, including the Chief Executive Officer (the "CEO") and the Chief Financial Officer (the "CFO"), the Company's management, including the CEO and the CFO, concluded that the Company's disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control Over Financial Reporting

There were no changes with respect to the Company's internal control over financial reporting during the quarter ended September 30, 2022 that have materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

PART II – Other Information

Item 1. Legal Proceedings

Information regarding legal proceedings is incorporated by reference from Note 15 to the Company's Condensed Consolidated Financial Statements set forth in Part I of this report.

Item 1A. Risk Factors

We face a variety of risks that are inherent in our business and our industry, including operational, legal and regulatory risks. Such risks could cause our actual results to differ materially from our forward-looking statements, expectations and historical trends. Except as set forth below, there have been no material changes from the risk factors disclosed in "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2021 and Quarterly Report on Form 10-Q for the quarter ended March 31, 2022.

Health concerns arising from outbreaks of viruses or other illnesses may have a material adverse effect on our business. The COVID-19 pandemic has had, and may continue to have, adverse effects on our results of operations, cash flows and financial condition.

Our business could be materially and adversely affected by the outbreak of a widespread health epidemic, such as COVID-19, avian flu or African swine flu. Outbreaks of contagious illness occur from time to time around the world, including in China where virtually all of our restaurants are located. The occurrence of such an outbreak or other adverse public health developments in China could materially disrupt our business and operations, including if government authorities impose mandatory closures, seek voluntary closures or impose restrictions on operations of restaurants. Furthermore, the risk of contracting viruses or other illnesses that may be transmitted through human contact could cause employees or guests to avoid gathering in public places or interacting with other people, which could materially and adversely affect restaurant guest traffic or the ability to adequately staff restaurants. An outbreak could also cause disruption in our supply chain, increase our raw-material costs, increase operational complexity and adversely impact our ability to provide safety measures to protect our employees and customers, which could materially and adversely affect our continuous operations. Our operating costs may also increase as a result of taking precautionary measures to protect the health and wellbeing of our customers and employees during an outbreak. If an outbreak reaches pandemic levels, there may also be long-term effects on the economies of affected countries. Any of the foregoing within China would severely disrupt our operations and could have a material adverse effect on our business, results of operations, cash flows and financial condition.

For example, starting in the first quarter of 2020, the COVID-19 pandemic significantly impacted the Company's operations, resulting in a significant decline in Operating profit mainly driven by same-store sales declines and temporary store closures. At the peak of the COVID-19 outbreak in China in 2020, approximately 35% of our restaurants were closed. Our operations and financial results for the second half of 2021 were also significantly affected by multiple waves of Delta variant outbreaks, spreading to nearly all provinces in China. In the first half of 2022, the most severe COVID-19 outbreaks to date in China significantly affected our business operations. During April and May 2022, over 2,500 of our stores in China, on average, were either temporarily closed or offered only takeaway and delivery services. Of these stores, approximately 45% were temporarily closed.

We expect that our operations will continue to be impacted by the COVID-19 pandemic, including outbreaks caused by existing or new COVID-19 variants and the actions taken by governmental authorities, such as regional lockdowns, measures restricting travel and large gatherings, and recommendations against dining out. It remains difficult to predict the full impact of the COVID-19 pandemic on the broader economy and how consumer behavior may change, and whether such change is temporary or permanent. Social distancing, telecommunicating and reductions in travel may become the new normal. These conditions could fundamentally impact the way we work and the services we provide, and could have continuing adverse effects on our results of operations, cash flows and financial condition after the pandemic subsides. The extent to which our operations continue to be impacted by the pandemic will depend largely on future developments, which are highly uncertain and cannot be accurately predicted, including resurgences and further spread of existing or new COVID-19 variants, the actions by the government authorities to contain the pandemic or treat its impact, the availability and effectiveness of vaccines, the economic recovery within China and globally, the impact on consumer behavior and other related factors. Our insurance policy does not cover any losses we incur as a result of the pandemic. The COVID-19 pandemic also may have the effect of heightening other risks disclosed in the "Risk Factors" section of the Company's Annual Report on Form 10-K for the year ended December 31, 2021, such as, but not limited to, those related to supply chain management, labor shortage and cost, cybersecurity threats, as well as consumer perceptions of our brands.

Even if a virus or other illness does not spread significantly, the perceived risk of infection or health risk may affect our business. Our operations could also be disrupted if any of our employees or employees of our business partners were suspected of having a contagious illness or susceptible to becoming infected with a contagious illness, since this could require us or our business partners to screen and/or quarantine some or all of such employees or disinfect our restaurant facilities.

With respect to the avian flu, public concern over an outbreak may cause fear about the consumption of chicken, eggs and other products derived from poultry, which could cause customers to consume less poultry and related products. This would likely result in lower revenues and profits. Avian flu outbreaks could also adversely affect the price and availability of poultry, which could negatively impact our profit margins and revenues.

The operation of our restaurants is subject to the terms of the master license agreement which, if terminated or limited, would materially adversely affect our business, results of operations and financial condition.

Under the master license agreement with YUM, we are required to meet a Sales Growth Metric, which requires the average annual Gross Revenue (as defined in the master license agreement) for each of the KFC, Pizza Hut and Taco Bell brands for each rolling five (5) calendar year period throughout the term of the master license agreement (“Measurement Period”), beginning January 1, 2017, to exceed the annual Gross Revenue of the calendar year immediately preceding the corresponding Measurement Period (“Benchmark Year”), unless otherwise agreed by the parties. To illustrate, the first Measurement Period was January 1, 2017 through December 31, 2021 (corresponding to the first Benchmark Year of January 1, 2016 through December 31, 2016) and the second Measurement Period is January 1, 2018 through December 31, 2022 (corresponding to the second Benchmark Year of January 1, 2017 through December 31, 2017).

The requirement regarding the Sales Growth Metric began at the end of the first Measurement Period on December 31, 2021. Within an agreed period after the beginning of each calendar year following December 31, 2021, and during the term of the master license agreement, we are required to provide to YUM a written statement with the calculations of the Sales Growth Metric. If our calculations indicate that any of these restaurant brands failed to meet the Sales Growth Metric (an “SGM Breach”), there is a mechanism under the master license agreement for us to explain and remediate such breach in good faith. YUM has the right to terminate the master license agreement in the event of an SGM Breach. In the event of two consecutive SGM Breaches for KFC, Pizza Hut or Taco Bell, YUM shall be entitled to exercise its right to eliminate or modify the exclusivity of the license granted to us and conduct and further develop the relevant restaurant brand in our licensed territory or license one or more third parties to do so.

The master license agreement may also be terminated upon the occurrence of certain events. We do not believe there has been any material breach of the master license agreement, and we actively monitor our compliance with the terms of the master license agreement on an on-going basis. Under the master license agreement, we have the right to cure any breach of the agreement, except for the dissolution, liquidation, insolvency or bankruptcy of the Company or upon the occurrence of an unauthorized transfer or change of control or other breach that YUM determines will not or cannot be cured. Upon the occurrence of a non-curable breach, YUM will have the right to terminate the master license agreement (or our rights to a particular brand) on delivery of written notice. Upon the occurrence of a curable breach, YUM will provide a notice of breach that sets forth a cure period that is reasonably tailored to the applicable breach. If we do not cure the breach, YUM will have the right to terminate the master license agreement (or our rights to a particular brand). The master license agreement also contemplates remedies other than termination that YUM may use as appropriate. These remedies include: actions for injunctive and/or declaratory relief (including specific performance) and/or damages; limitations on our future development rights or suspension of restaurant operations pending a cure; modification or elimination of our territorial exclusivity; and YUM’s right to repurchase from us the business operated under an affected brand at fair market value, less YUM’s damages.

In the second quarter of 2022, we invoked the dispute resolution process pursuant to the master license agreement to resolve a disagreement with YUM over royalties charged on delivery and aggregator platform fees. We believe, pursuant to the master license agreement, that delivery fees paid by customers for delivery services and commissions paid to third-party aggregator platforms should not be subject to royalties, and we notified YUM in April 2022 that we would stop paying royalties on such fees beginning in January 2022. In June 2022, YUM delivered to the Company a notice of material breach of the master license agreement, demanding among other things payment of the disputed royalty amounts. Following receipt of the notice, we paid the disputed royalty amounts under a reservation of rights, after which YUM suspended its declaration of material breaches related to payment of the disputed royalty amounts. YUM’s notice in June 2022 also alleged, for the first time, that the Company has engaged in unauthorized use of YUM’s intellectual

property under the master license agreement. The Company believes the notice is contrary to the terms of the master license agreement and that these allegations are without merit. The parties are progressing through the dispute resolution process.

If the parties are unable to resolve the dispute pursuant to the master license agreement, either party may submit the dispute to arbitration, while retaining all other rights and remedies, which may include the initiation of proceedings for injunctive or other equitable relief, or the exercise of contractual rights up to and including termination of the master license agreement.

If the master license agreement were terminated, or any of our license rights were limited, our business, results of operations and financial condition would be materially adversely affected.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Our Board of Directors authorized an aggregate of \$2.4 billion for our share repurchase program, including its most recent increase in authorization in March 2022. The authorizations do not have an expiration date.

The following table provides information as of September 30, 2022 with respect to shares of Yum China common stock repurchased by the Company during the quarter then ended:

Period	Total Number of Shares Repurchased (thousands)	Average Price Paid Per Share	Total Number of Shares Repurchased as Part of Publicly Announced Plans or Programs (thousands)	Approximate Dollar Value of Shares that May Yet Be Repurchased under the Plans or Programs (millions)
7/1/22-7/31/22	—	-	—	\$ 1,217
8/1/22-8/31/22	—	\$ -	—	\$ 1,217
9/1/22-9/30/22	271	\$ 48.05	271	\$ 1,204
Total	271	\$ 48.05	271	\$ 1,204

Item 6. Exhibits

Exhibit Number	Description of Exhibits
31.1	<u>Certification of the Chief Executive Officer pursuant to Rule 13a-14(a) of Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*</u>
31.2	<u>Certification of the Chief Financial Officer pursuant to Rule 13a-14(a) of Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.*</u>
32.1	<u>Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*</u>
32.2	<u>Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.*</u>
101.INS	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document *
101.SCH	Inline XBRL Taxonomy Extension Schema Document *
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document *
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document *
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document *
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document *
104	Cover Page Interactive Data File - the cover page XBRL tags are embedded within the Inline XBRL document *

* Filed or furnished herewith.

** Portions of this exhibit have been redacted pursuant to Item 601(b)(10)(iv) of Regulation S-K.

SIGNATURES

Pursuant to the requirement of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Yum China Holdings, Inc.

(Registrant)

Date: November 9, 2022

/s/ Xueling Lu

Controller and Principal Accounting Officer

CERTIFICATION

I, Joey Wat, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Yum China Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant, as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2022

/s/ Joey Wat

Joey Wat
Chief Executive Officer

CERTIFICATION

I, Andy Yeung, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Yum China Holdings, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant, as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 9, 2022

/s/ Andy Yeung
Andy Yeung
Chief Financial Officer

CERTIFICATION OF CHIEF EXECUTIVE OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Yum China Holdings, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2022, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), I, Joey Wat, Chief Executive Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Periodic Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2022

/s/ Joey Wat

Joey Wat

Chief Executive Officer

A signed original of this written statement required by Section 906 has been provided to Yum China Holdings, Inc. and will be retained by Yum China Holdings, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.

CERTIFICATION OF CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Quarterly Report of Yum China Holdings, Inc. (the "Company") on Form 10-Q for the quarter ended September 30, 2022, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), I, Andy Yeung, Chief Financial Officer of the Company, hereby certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

1. The Periodic Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information contained in the Periodic Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: November 9, 2022

/s/ Andy Yeung

Andy Yeung

Chief Financial Officer

A signed original of this written statement required by Section 906 has been provided to Yum China Holdings, Inc. and will be retained by Yum China Holdings, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.
