

**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 June 30, 2018

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)

81-2421743

(I.R.S. Employer
Identification No.)

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

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

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

(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)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post 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"/> (Do not check if a small reporting company)	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 August 2, 2018 was 383,246,732 shares.

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Condensed Consolidated Statements of Income (Unaudited)

Yum China Holdings, Inc.

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

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Revenues				
Company sales	\$ 1,888	\$ 1,664	\$ 3,904	\$ 3,402
Franchise fees and income	34	33	74	69
Revenues from transactions with franchisees and unconsolidated affiliates	141	141	302	288
Other revenues	5	3	9	8
Total revenues	2,068	1,841	4,289	3,767
Costs and Expenses, Net				
Company restaurants				
Food and paper	571	483	1,165	969
Payroll and employee benefits	424	366	866	734
Occupancy and other operating expenses	607	539	1,226	1,069
Company restaurant expenses	1,602	1,388	3,257	2,772
General and administrative expenses	101	118	215	216
Franchise expenses	17	17	37	35
Expenses for transactions with franchisees and unconsolidated affiliates	138	137	298	284
Other operating costs	7	3	11	6
Closures and impairment expenses, net	17	18	16	18
Other income, net	(7)	(11)	(133)	(31)
Total costs and expenses, net	1,875	1,670	3,701	3,300
Operating Profit	193	171	588	467
Interest income, net	10	4	18	8
Income Before Income Taxes	203	175	606	475
Income tax provision	(53)	(43)	(160)	(133)
Net income – including noncontrolling interests	150	132	446	342
Net income – noncontrolling interests	7	7	15	13
Net Income – Yum China Holdings, Inc.	\$ 143	\$ 125	\$ 431	\$ 329
Weighted-average common shares outstanding (in millions):				
Basic	386	387	386	387
Diluted	398	399	400	397
Basic Earnings Per Common Share	\$ 0.37	\$ 0.32	\$ 1.12	\$ 0.85
Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31	\$ 1.08	\$ 0.83
Cash Dividends Declared Per Common Share	\$ 0.10	\$ —	\$ 0.20	\$ —

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	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Net income - including noncontrolling interests	\$ 150	\$ 132	\$ 446	\$ 342
Other comprehensive income, net of tax of nil:				
Foreign currency translation adjustments	(148)	32	(58)	47
Comprehensive income - including noncontrolling interests	2	164	388	389
Comprehensive income - noncontrolling interests	2	8	13	15
Comprehensive Income - Yum China Holdings, Inc.	\$ —	\$ 156	\$ 375	\$ 374

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	
	6/30/2018	6/30/2017
Cash Flows – Operating Activities		
Net income – including noncontrolling interests	\$ 446	\$ 342
Depreciation and amortization	235	196
Closures and impairment expenses	16	18
Gain from re-measurement of equity interest upon acquisition	(98)	—
Deferred income taxes	42	(3)
Equity income from investments in unconsolidated affiliates	(35)	(35)
Distributions received from unconsolidated affiliates	41	31
Share-based compensation	13	11
Changes in accounts receivable	(2)	12
Changes in inventories	18	(3)
Changes in prepaid expenses and other current assets	(28)	(1)
Changes in accounts payable and other current liabilities	182	46
Changes in income taxes payable	20	20
Other, net	(31)	(30)
Net Cash Provided by Operating Activities	819	604
Cash Flows – Investing Activities		
Capital spending	(230)	(204)
Purchases of short-term investments	(370)	(318)
Maturities of short-term investments	295	81
Proceeds from refranchising of restaurants	3	3
Acquisition of business, net of cash acquired	(88)	(25)
Other, net	(16)	(2)
Net Cash Used in Investing Activities	(406)	(465)
Cash Flows – Financing Activities		
Payment of capital lease obligation	(1)	(1)
Repayment of short-term borrowings assumed from acquisition	(10)	—
Repurchase of shares of common stock	(70)	(96)
Proceeds from exercise of stock options	—	4
Cash dividends paid	(77)	—
Dividends paid to noncontrolling interests	(27)	(17)
Other, net	(1)	—
Net Cash Used in Financing Activities	(186)	(110)
Effect of Exchange Rates on Cash and Cash Equivalents	(25)	12
Net Increase in Cash and Cash Equivalents	202	41
Cash and Cash Equivalents - Beginning of Period	1,059	885
Cash and Cash Equivalents - End of Period	\$ 1,261	\$ 926
Supplemental Cash Flow Data		
Cash paid for income tax	114	121

See accompanying Notes to Condensed Consolidated Financial Statements.

Condensed Consolidated Balance Sheets (Unaudited)

Yum China Holdings, Inc.

(in US\$ millions)

	6/30/2018	12/31/2017
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 1,261	\$ 1,059
Short-term investments	278	205
Accounts receivable, net	73	81
Inventories, net	276	297
Prepaid expenses and other current assets	205	160
Total Current Assets	2,093	1,802
Property, plant and equipment, net	1,657	1,691
Goodwill	276	108
Intangible assets, net	145	101
Investments in unconsolidated affiliates	53	95
Other assets	421	385
Deferred income taxes	85	105
Total Assets	\$ 4,730	\$ 4,287
LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	\$ 1,147	\$ 985
Income taxes payable	59	39
Total Current Liabilities	1,206	1,024
Capital lease obligations	27	28
Other liabilities and deferred credits	396	388
Total Liabilities	1,629	1,440
Redeemable Noncontrolling Interest	5	5
Equity		
Common stock, \$0.01 par value; 1,000 million shares authorized; 391 million shares and 389 million shares issued at June 30, 2018 and December 31, 2017, respectively; 385 million shares and 385 million shares outstanding at June 30, 2018 and December 31, 2017, respectively	4	4
Treasury stock	(221)	(148)
Additional paid-in capital	2,388	2,375
Retained earnings	751	397
Accumulated other comprehensive income	81	137
Total Equity – Yum China Holdings, Inc.	3,003	2,765
Noncontrolling interests	93	77
Total Equity	3,096	2,842
Total Liabilities, Redeemable Noncontrolling Interest and Equity	\$ 4,730	\$ 4,287

See accompanying Notes to Condensed Consolidated Financial Statements.

Notes to Condensed Consolidated Financial Statements (Unaudited)

(Tabular amounts in US\$ millions)

Note 1 – Description of the 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 separated from Yum! Brands, Inc. (“YUM” or the “Parent”) on October 31, 2016 (the “separation”), becoming an independent publicly traded company as a result of a pro rata distribution (the “distribution”) of all outstanding shares of Yum China common stock to shareholders of YUM. On October 31, 2016, YUM’s shareholders of record as of 5:00 p.m. Eastern Time on October 19, 2016 received one share of Yum China common stock for every one share of YUM common stock held as of the record date. Yum China’s common stock began trading “regular way” under the ticker symbol “YUMC” on the New York Stock Exchange on November 1, 2016.

The Company owns, franchises or has an ownership in entities that own and operate restaurants under the KFC, Pizza Hut, East Dawning, Little Sheep and Taco Bell concepts (collectively, the “Concepts”). In connection with the separation of the Company from YUM, Yum! Restaurants Asia Pte. Ltd., a wholly-owned indirect subsidiary of YUM, and Yum Restaurants Consulting (Shanghai) Company Limited (“YCCL”), a wholly-owned indirect subsidiary of Yum China, entered into a 50-year master license agreement 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, for the exclusive right to use and sub-license the use of intellectual property owned by YUM and its subsidiaries for the development and operation of the KFC, Pizza Hut and, subject to achieving certain agreed-upon milestones, Taco Bell brands and their related marks and other intellectual property rights for restaurant services in the People’s Republic of China, excluding Hong Kong, Taiwan and Macau (the “PRC” or “China”). 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 East Dawning and Little Sheep intellectual property and pay no license fee related to these concepts.

The Company also owns a controlling interest in the holding company of DAOJIA.com.cn (“Daojia”), an established online food delivery service provider in China.

Note 2 – Basis of Presentation

In connection with our separation from YUM, the direct and indirect equity interests of all of our operating subsidiaries and intermediate holding companies were transferred from YUM to Yum China, when Yum China was still one of YUM’s subsidiaries, through a series of transactions, which were completed in August 2016. The Company separated from YUM on October 31, 2016, becoming an independent publicly traded company as a result of a pro rata distribution of all outstanding shares of Yum China common stock to shareholders of YUM.

For periods prior to October 31, 2016, the combined financial statements of YUM’s China businesses and operations when Yum China was a wholly-owned subsidiary of YUM are referred to as Condensed Combined Financial Statements. For periods subsequent to October 31, 2016, the consolidated financial statements of the Company as a separate publicly traded company following its separation from YUM are referred to as Condensed Consolidated Financial Statements.

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 June 30, 2018, and the results of our operations and comprehensive income for the quarters and years to date ended June 30, 2018 and 2017, and cash flows for the years to date ended June 30, 2018 and 2017. 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 and Combined Financial Statements and notes thereto defined and included in the Company’s Annual Report on Form 10-K as filed with the SEC on February 27, 2018.

Through the acquisition of Daojia during the second quarter of 2017, 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 has the obligation to absorb substantially all of the profits and 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.

During the first quarter of 2018, the Company completed the acquisition of an additional 36% equity interest in an unconsolidated affiliate that operates KFC stores in Wuxi, China (“Wuxi KFC”), for cash consideration of approximately \$98 million, increasing the Company’s equity interest to 83%, allowing the Company to consolidate the entity. The acquisition was considered immaterial. We began consolidating Wuxi KFC upon the completion of acquisition.

Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (“FASB”) issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)* (“ASC 606”), to provide principles within a single framework for revenue recognition of transactions involving contracts with customers across all industries. The standard allows for either a full retrospective or modified retrospective transition method. In March, April and May 2016, the FASB issued the following amendments to clarify the implementation guidance: ASU No. 2016-04, *Liabilities-Extinguishments of liabilities (Subtopic 450-20): Revenue of Breakage for Certain Prepaid Stored-Value Products (a consensus of the FASB Emerging Issues Task Force)*, ASU No. 2016-08, *Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, ASU No. 2016-10 *Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing* and ASU No. 2016-12, *Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients*. The Company adopted these standards on January 1, 2018, and applied the full retrospective approach.

The new standard did not have an impact on our recognition of revenue from Company-owned restaurants or our recognition of continuing fees from franchisees and unconsolidated affiliates; however, it changed the way we account for upfront fees. Upfront fees, such as initial and renewal fees from franchisees and unconsolidated affiliates, were previously recognized as revenue when we performed substantially all initial services required by the franchise agreement, generally upon the opening of a store or when a renewal agreement with a franchisee became effective. We now recognize the upfront fees from franchisees and unconsolidated affiliates as revenue over the term of each franchise agreement as the franchise rights are accounted for as rights to access our symbolic intellectual property in accordance with the new standard. Any unamortized portion of fees received is accounted for as a contract liability.

The new standard also had an impact on certain transactions we entered into with franchisees and unconsolidated affiliates, such as sales of food and paper products and advertising services. These transactions were previously either not included or presented on a net basis in our statements of income or cash flows based on industry-specific guidance included in previous accounting guidance, which was superseded by the new standard. Under the new standard, we consider ourselves the principal in these arrangements as we have the ability to control a promised good or service before transferring that good or service to the customer. Therefore, we include such transactions in revenues and expenses on the Condensed Consolidated Statements of Income with no significant impact to Net income.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230)* (“ASU 2016-15”), which provides clarification regarding how certain cash receipts and cash payments are presented and classified in the statement of cash flows. This update addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU 2016-15 is effective for annual and interim periods beginning after December 15, 2017, with early adoption permitted. We adopted ASU 2016-15 on January 1, 2018, and such adoption did not have a material impact on our financial statements.

In October 2016, the FASB issued ASU No. 2016-16, *Income Taxes (Topic 740): Intra-Entity Transfers of Assets Other Than Inventory* (“ASU 2016-16”), which requires the recognition of the income tax consequences of an intra-entity transfer of an asset, other than inventory, when the transfer occurs. We adopted ASU 2016-16 on January 1, 2018, and such adoption did not have a material impact on our financial statements.

In November 2016, the FASB issued ASU No. 2016-18, *Statement of Cash Flows (Topic 230): Restricted Cash* (“ASU 2016-18”), which requires that entities show the changes in total cash, cash equivalents, restricted cash and restricted cash equivalents in the statement of cash flows. We adopted ASU 2016-18 on January 1, 2018, and such adoption did not have a material impact on our financial statements.

In January 2017, the FASB issued ASU No. 2017-01, *Business Combinations (Topic 805): Clarifying the Definition of a Business* (“ASU 2017-01”), which revises the definition of a business and provides new guidance in evaluating when a set of transferred assets and activities is a business. We adopted ASU 2017-01 on January 1, 2018, and such adoption did not have a material impact on our financial statements.

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

Our fiscal year ends on December 31. Effective at the beginning of fiscal year 2018, the Company changed its fiscal calendar from two months in the first quarter, three months in the second and third quarters and four months in the fourth quarter, to four three-month quarters ending on March 31, June 30, September 30 and December 31 of each year. The change was made to align with how management now measures performance internally and to facilitate the comparability of our results with peers using calendar quarters. Quarterly results of all prior financial periods presented have been recast as if they had been reported under our new fiscal calendar.

Note 3 – 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 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.

Franchise Fees and Income

Franchise fees and income primarily include upfront fees, such as initial fees and renewal fees, and continuing fees. We have determined that the services we provide in exchange for upfront fees and continuing fees are highly interrelated with the franchise right. We recognize upfront 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 in accordance with ASC 606. The franchise agreement term is generally 10 years for KFC and Pizza Hut, and five or 10 years for Little Sheep. 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.

The Company centrally purchases substantially all food and paper products from suppliers for substantially all of our restaurants, including franchisees and unconsolidated affiliates, and then sells and delivers them to the restaurants. 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. 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 support and technology support services. Advertising services and other services provided are highly interrelated to franchise right, so we do not consider them to be individually distinct and therefore account for them under ASC 606 as a single performance obligation and 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 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. 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, including an estimate of the breakage for points that members will never redeem. The Company reviews its breakage estimates at least annually based upon the latest available information regarding redemption and expiration patterns.

Accounts Receivable

Accounts receivable mainly consist of trade receivables and royalties from franchisees and unconsolidated affiliates, 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 for uncollectible receivable balances is based upon pre-defined aging criteria or upon the occurrence of other events that indicate that we may not collect the balance due. Additionally, we monitor the financial condition of our franchisees and record provisions for estimated losses on receivables when we believe it probable that our franchisees will be unable to make their required payments. 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. Trade receivables that are ultimately deemed to be uncollectible, and for which collection efforts have been exhausted, are written off against the allowance for doubtful accounts.

Costs to Obtain Contracts

Costs to obtain contracts represent the portion of upfront license 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. They meet the requirements to be capitalized as the Company expects to generate future economic benefits from such costs incurred, which allow us to enter into franchise agreements and collect fees. Such costs to obtain contracts are included in Other assets on the Condensed Consolidated Balance Sheets and are amortized over the term of the franchise agreement. Subsequent to the separation, we are no longer required to pay YUM any upfront 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 \$9 million and \$12 million at June 30, 2018 and December 31, 2017, respectively.

Contract Liabilities

Contract liabilities at June 30, 2018 and December 31, 2017 were as follows:

Contract liabilities	6/30/2018	12/31/2017
- Deferred revenue related to prepaid stored-value products	\$ 51	\$ 50
- Deferred revenue related to customer loyalty programs	22	16
- Deferred revenue related to upfront fees	37	39
Total	<u>\$ 110</u>	<u>\$ 105</u>

Contract liabilities consist of deferred revenue related to prepaid stored-value products, customer loyalty programs and upfront fees. Deferred revenue related to prepaid stored-value products and customer loyalty programs is included in Accounts payable and other current liabilities on the Condensed Consolidated Balance Sheets. Deferred revenue related to upfront 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 and deferred credits on the Condensed Consolidated Balance Sheets. Revenue recognized in the quarter and year to date ended June 30, 2018 that was included in the contract liability balance at the beginning of each period amounted to \$18 million and \$30 million, 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 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 based on certain percentage of sales, as those sales occur.

Note 4 – Earnings Per Common Share (“EPS”)

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

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Net Income – Yum China Holdings, Inc.	\$ 143	\$ 125	\$ 431	\$ 329
Weighted-average common shares outstanding (for basic calculation) (a)	386	387	386	387
Effect of dilutive share-based employee compensation (a)	10	11	11	9
Effect of dilutive warrants (b)	2	1	3	1
Weighted-average common and dilutive potential common shares outstanding (for diluted calculation)	398	399	400	397
Basic Earnings Per Common Share	\$ 0.37	\$ 0.32	\$ 1.12	\$ 0.85
Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31	\$ 1.08	\$ 0.83
Employee stock options, stock appreciation rights and warrants excluded from the diluted EPS computation (c)	1	10	1	14

(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 on shares of common stock 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 outstanding equity awards are included in the computation of diluted EPS, if there is dilutive effect.

(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 providing the right to purchase 8,200,405 shares of Yum China common stock, at an exercise price of \$31.40 and \$39.25 per share, respectively, subject to customary anti-dilution adjustments. The warrants may be exercised at any time through October 31, 2021. The outstanding warrants are included in the computation of diluted EPS, if there is dilutive effect when the average market price of Yum China common stock for the period exceeds the exercise price of the warrants.

(c) These outstanding employee stock options, stock appreciation rights and warrants were not included in the computation of diluted EPS because to do so would have been antidilutive for the quarters and years to date presented.

Note 5 – Equity

Changes in Equity and Redeemable Noncontrolling Interest

Yum China Holdings, Inc.										
	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Treasury Stock		Noncontrolling Interests	Total Equity	Redeemable Noncontrolling Interest
	Shares	Amount				Shares	Amount			
Balance at December 31, 2017	389	\$ 4	\$ 2,375	\$ 397	\$ 137	(4)	\$ (148)	\$ 77	\$ 2,842	\$ 5
Net Income				431				15	446	
Foreign currency translation adjustments					(56)			(2)	(58)	
Comprehensive income									388	
Acquisition of business								36	36	
Cash dividends declared (\$0.20 per common share)				(77)					(77)	
Dividends declared								(33)	(33)	
Repurchase of shares of common stock						(2)	(73)		(73)	
Exercise and vesting of share-based awards	2	—	—						—	
Share-based compensation			13						13	
Balance at June 30, 2018	391	\$ 4	\$ 2,388	\$ 751	\$ 81	(6)	\$ (221)	\$ 93	\$ 3,096	\$ 5

Share Repurchase Program

On February 7, 2017, we announced that our Board of Directors authorized a \$300 million share repurchase program. On October 4, 2017, the Board of Directors increased Yum China's existing share repurchase authorization from \$300 million to an aggregate of \$550 million. Under the authorization, we repurchased shares of Yum China common stock during the years to date ended June 30, 2018 and 2017 as indicated below. All amounts exclude applicable transaction fees.

Authorization Date	Shares Repurchased (thousands)		Dollar Value of Shares Repurchased (millions)		Remaining Dollar Value of Shares that may be Repurchased (millions)
	2018	2017	2018	2017	
	February 7, 2017	1,910	2,723	73	
October 4, 2017	—	—	—	—	250
Total	1,910 (a)	2,723 (b)	73 (a)	105 (b)	349

(a) Includes 0.1 million shares repurchased for \$3 million with trade dates prior to June 30, 2018 but cash settlement dates subsequent to June 30, 2018.

(b) Includes 0.2 million shares repurchased for \$9 million with trade dates prior to June 30, 2017 but cash settlement dates subsequent to June 30, 2017.

Note 6 – Items Affecting Comparability of Net Income and Cash Flows

Store Closure and Impairment Activity

Store closure income and Store impairment charges by reportable segments and All Other Segments are presented below:

	Quarter Ended				Year to Date Ended			
	6/30/2018				6/30/2018			
	Total Company	KFC	Pizza Hut	All Other Segments	Total Company	KFC	Pizza Hut	All Other Segments
Store closure income ^(a)	\$ 2	\$ 1	\$ 1	\$ —	\$ 5	\$ 2	\$ 3	\$ —
Store impairment charges	(19)	(7)	(12)	—	(21)	(8)	(13)	—
Closure and impairment expenses	<u>\$ (17)</u>	<u>\$ (6)</u>	<u>\$ (11)</u>	<u>\$ —</u>	<u>\$ (16)</u>	<u>\$ (6)</u>	<u>\$ (10)</u>	<u>\$ —</u>

	Quarter Ended				Year to Date Ended			
	6/30/2017				6/30/2017			
	Total Company	KFC	Pizza Hut	All Other Segments	Total Company	KFC	Pizza Hut	All Other Segments
Store closure income(a)	\$ 1	\$ 1	\$ —	\$ —	\$ 5	\$ 3	\$ 2	\$ —
Store impairment charges	(19)	(10)	(9)	—	(23)	(13)	(10)	—
Closure and impairment expenses	<u>\$ (18)</u>	<u>\$ (9)</u>	<u>\$ (9)</u>	<u>\$ —</u>	<u>\$ (18)</u>	<u>\$ (10)</u>	<u>\$ (8)</u>	<u>\$ —</u>

(a) Store closure income include proceeds from forced store closures, lease reserves established when we cease using a property under an operating lease and subsequent adjustments to those reserves and other facility-related expenses from previously closed stores. Remaining lease obligations for closed stores were not material at June 30, 2018 or December 31, 2017.

Note 7 – Other Income, net

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Equity income from investments in unconsolidated affiliates	\$ 12	\$ 14	\$ 35	\$ 35
Gain from re-measurement of equity interest upon acquisition(a)	—	—	98	—
Foreign exchange loss and other	(5)	(3)	—	(4)
Other income, net	<u>\$ 7</u>	<u>\$ 11</u>	<u>\$ 133</u>	<u>\$ 31</u>

(a) As a result of the acquisition of Wuxi KFC in the first quarter of 2018, as disclosed in Note 2, the Company recognized a gain of \$98 million from the re-measurement of our previously held 47% equity interest at fair value, which was not allocated to any segment for performance reporting purposes.

Note 8 – Supplemental Balance Sheet Information

<u>Accounts Receivable, net</u>	6/30/2018	12/31/2017
Accounts receivable, gross	\$ 75	\$ 83
Allowance for doubtful accounts	(2)	(2)
Accounts receivable, net	<u>\$ 73</u>	<u>\$ 81</u>

<u>Prepaid Expenses and Other Current Assets</u>	6/30/2018	12/31/2017
Prepaid rent	\$ 43	\$ 41
Receivables from payment processors and aggregators	34	38
Dividends receivable from unconsolidated affiliates	39	21
Other prepaid expenses and current assets	89	60
Prepaid expenses and other current assets	<u>\$ 205</u>	<u>\$ 160</u>

<u>Property, Plant and Equipment</u>	6/30/2018	12/31/2017
Buildings and improvements	\$ 2,169	\$ 2,184
Capital leases, primarily buildings	28	28
Machinery, equipment and construction in progress	1,208	1,204
Property, plant and equipment, gross	3,405	3,416
Accumulated depreciation	(1,748)	(1,725)
Property, plant and equipment, net	<u>\$ 1,657</u>	<u>\$ 1,691</u>

<u>Other Assets</u>	6/30/2018	12/31/2017
Land use right	\$ 136	\$ 131
VAT assets	197	176
Costs to obtain contracts	9	12
Long-term deposits	61	56
Others	18	10
Other Assets	<u>\$ 421</u>	<u>\$ 385</u>

<u>Accounts Payable and Other Current Liabilities</u>	6/30/2018	12/31/2017
Accounts payable	\$ 584	\$ 424
Accrued capital expenditures	120	142
Accrued compensation and benefits	179	233
Accrued taxes, other than income taxes	25	16
Accrued marketing expenses	81	28
Contract liabilities	80	72
Other current liabilities	78	70
Accounts payable and other current liabilities	<u>\$ 1,147</u>	<u>\$ 985</u>

<u>Other Liabilities and Deferred Credits</u>	6/30/2018	12/31/2017
Deferred escalating minimum rent	\$ 156	\$ 162
Contract liabilities	30	33
Accrued income tax payable	96	112
Deferred income tax liabilities	69	32
Other noncurrent liabilities and deferred credits	45	49
Other liabilities and deferred credits	<u>\$ 396</u>	<u>\$ 388</u>

Note 9 – 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, 2017				
Goodwill, gross	\$ 490	\$ 80	\$ 19	\$ 391
Accumulated impairment losses ^(a)	(382)	—	—	(382)
Goodwill, net	108	80	19	9
Goodwill acquired ^(b)	175	175	—	—
Effect of currency translation adjustment	(7)	(7)	—	—
Balance as of June 30, 2018				
Goodwill, gross	658	248	19	391
Accumulated impairment losses ^(a)	(382)	—	—	(382)
Goodwill, net	<u>\$ 276</u>	<u>\$ 248</u>	<u>\$ 19</u>	<u>\$ 9</u>

(a) Accumulated impairment losses represent Little Sheep goodwill impairment.

(b) Goodwill acquired in connection with the acquisition of Wuxi KFC.

Intangible assets, net as of June 30, 2018 and December 31, 2017 are as follows:

	6/30/2018			12/31/2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Definite-lived intangible assets						
Reacquired franchise rights(c)	\$ 156	\$ (94)	\$ 62	\$ 100	\$ (87)	\$ 13
Daojia platform	17	(2)	15	18	(1)	17
Customer-related assets	12	(7)	5	12	(6)	6
Other	19	(11)	8	19	(10)	9
	<u>\$ 204</u>	<u>\$ (114)</u>	<u>\$ 90</u>	<u>\$ 149</u>	<u>\$ (104)</u>	<u>\$ 45</u>
Indefinite-lived intangible assets						
Little Sheep trademark	\$ 55	\$ —	\$ 55	\$ 56	\$ —	\$ 56
	<u>\$ 259</u>	<u>\$ (114)</u>	<u>\$ 145</u>	<u>\$ 205</u>	<u>\$ (104)</u>	<u>\$ 101</u>

(c) Increase in gross carrying amount of reacquired franchise rights during the year to date ended June 30, 2018 primarily resulted from the acquisition of Wuxi KFC.

Amortization expense of definite-lived intangible assets was \$7 million and \$3 million for the quarters ended June 30, 2018 and 2017, respectively, and \$13 million and \$6 million for the years to date ended June 30, 2018 and 2017, respectively. As of June 30, 2018, expected amortization expense for the unamortized definite-lived intangible assets is approximately \$14 million for the remainder of 2018, \$20 million in 2019, \$15 million in 2020, \$15 million in 2021 and \$15 million in 2022.

Note 10 – Fair Value Measurements

As of June 30, 2018, the carrying values of cash and cash equivalents, short-term investments, accounts receivable and accounts payable approximated their fair values because of the short-term nature of these instruments.

In addition, certain of the Company's assets, such as property, plant and equipment, goodwill and intangible assets, are measured at fair value on a non-recurring basis, if determined to be impaired.

During the quarter and year to date ended June 30, 2018, we recorded restaurant-level impairment (Level 3) of \$13 million and \$13 million, respectively. During the quarter and year to date ended June 30, 2017, we recorded restaurant-level impairment (Level 3) of \$16 million and \$19 million, respectively. The remaining net book value of the assets measured at fair value as of June 30, 2018, subsequent to these impairments, was not significant.

Note 11 – Income Taxes

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Income tax provision	\$ 53	\$ 43	\$ 160	\$ 133
Effective tax rate	26.0%	24.3%	26.4%	27.9%

The higher effective tax rate for the quarter was primarily due to less excess tax benefit driven by the exercise of share-based awards, offset by less estimated repatriation of current year earnings outside of China. The lower year-to-date effective tax rate was primarily due to less estimated repatriation of current year earnings outside of China.

In December 2017, the U.S. enacted the *Tax Cuts and Jobs Act* (the "Tax Act"), which included a broad range of tax reforms, including, but not limited to, the establishment of a flat corporate income tax rate of 21%, the elimination or reduction of certain business deductions and the imposition of tax on deemed repatriation of accumulated undistributed foreign earnings. The Tax Act impacted Yum China in two material aspects: (1) all of the foreign-source dividends received by Yum China from its foreign subsidiaries will be exempted from taxation starting from the tax year beginning after December 31, 2017 and (2) Yum China recorded additional income tax expense in the fourth quarter of 2017, including an estimated one-time transition tax on its deemed repatriation of accumulated undistributed foreign earnings and additional tax related to revaluation of certain deferred tax assets.

The Tax Act requires a U.S. shareholder be subject to tax on Global Intangible Low Taxed Income (“GILTI”) earned by foreign subsidiaries. The Company has not determined its accounting policy with respect to whether to record deferred taxes for basis differences expected to reverse as a result of the GILTI provisions in future periods or use the period cost method. We have, however, included the 2018 estimate of current year GILTI as a period cost and included as part of the estimated annual effective tax rate.

As we collect and prepare necessary data, and interpret the Tax Act and any additional guidance issued by the U.S. Treasury Department, the Internal Revenue Service (“IRS”), and other standard-setting bodies, we may make adjustments to the provisional amounts. We continue to expect to complete our analysis within the measurement period not exceeding one year from the enactment date.

Note 12 – Reportable Operating Segments

We have two reportable segments: KFC and Pizza Hut. We also have four operating segments, East Dawning, Little Sheep, Taco Bell and Daojia, which are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in the aggregate.

Revenues	Quarter Ended 6/30/2018						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 1,400	\$ 528	\$ 17	\$ 123	2,068	\$ —	\$ 2,068
Inter-segment revenue	—	—	1	—	1	(1)	—
Total	<u>\$ 1,400</u>	<u>\$ 528</u>	<u>\$ 18</u>	<u>\$ 123</u>	<u>\$ 2,069</u>	<u>\$ (1)</u>	<u>\$ 2,068</u>

Revenues	Quarter Ended 6/30/2017						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated(d)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 1,206	\$ 498	\$ 16	\$ 121	1,841	\$ —	\$ 1,841
Inter-segment revenue	—	—	—	—	—	—	—
Total	<u>\$ 1,206</u>	<u>\$ 498</u>	<u>\$ 16</u>	<u>\$ 121</u>	<u>\$ 1,841</u>	<u>\$ —</u>	<u>\$ 1,841</u>

Revenues	Year to Date Ended 6/30/2018						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 2,898	\$ 1,093	\$ 37	\$ 261	4,289	\$ —	\$ 4,289
Inter-segment revenue	—	—	1	—	1	(1)	—
Total	<u>\$ 2,898</u>	<u>\$ 1,093</u>	<u>\$ 38</u>	<u>\$ 261</u>	<u>\$ 4,290</u>	<u>\$ (1)</u>	<u>\$ 4,289</u>

Revenues	Year to Date Ended 6/30/2017						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated(a)	Combined	Elimination	Consolidated
Revenue from external customers	\$ 2,456	\$ 1,026	\$ 39	\$ 246	3,767	\$ —	\$ 3,767
Inter-segment revenue	—	—	—	—	—	—	—
Total	<u>\$ 2,456</u>	<u>\$ 1,026</u>	<u>\$ 39</u>	<u>\$ 246</u>	<u>\$ 3,767</u>	<u>\$ —</u>	<u>\$ 3,767</u>

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Operating Profit				
KFC(b)	\$ 199	\$ 182	\$ 495	\$ 427
Pizza Hut	20	39	54	119
All Other Segments	(7)	(3)	(11)	(2)
Unallocated revenues from transactions with franchisees and unconsolidated affiliates(a)	122	121	259	246
Unallocated Other revenues(a)	1	—	2	—
Unallocated expenses from transactions with franchisees and unconsolidated affiliates(a)	(120)	(118)	(257)	(243)
Unallocated Other operating costs(a)	(1)	—	(2)	—
Unallocated and corporate G&A expenses(a)	(19)	(50)	(52)	(81)
Unallocated Other income (loss)(a)(c)	(2)	—	100	1
Operating Profit	\$ 193	\$ 171	\$ 588	\$ 467
Interest income, net(a)	10	4	18	8
Income Before Income Taxes	\$ 203	\$ 175	\$ 606	\$ 475

	Identifiable Assets	
	6/30/2018	12/31/2017
KFC(d)	\$ 1,760	\$ 1,544
Pizza Hut	615	668
All Other Segments	137	144
Corporate and Unallocated(e)	2,218	1,931
	\$ 4,730	\$ 4,287

	Long-Lived Assets(f)	
	6/30/2018	12/31/2017
KFC	\$ 1,384	\$ 1,152
Pizza Hut	529	580
All Other Segments	109	114
Corporate and Unallocated	56	54
	\$ 2,078	\$ 1,900

- (a) Amounts have not been allocated to any segment for performance reporting purposes.
- (b) Includes equity income from investments in unconsolidated affiliates of \$12 million and \$14 million for the quarters ended June 30, 2018 and 2017, respectively, and \$35 million and \$35 million for the years to date ended June 30, 2018 and 2017, respectively.
- (c) Amounts mainly include gain from re-measurement of previously held equity interest in connection with the acquisition of Wuxi KFC. See Note 2.
- (d) Includes investments in the unconsolidated affiliates.
- (e) Primarily includes cash and cash equivalents, short-term investments and inventories that are centrally managed.
- (f) Includes property, plant and equipment, goodwill and intangible assets, net.

Note 13 – Contingencies

Indemnification of China Tax on Indirect Transfers of Assets

In February 2015, the Chinese State Administration of Taxation (“SAT”) 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 distribution. However, given how recently Bulletin 7 was promulgated, 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 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

From time to time we have guaranteed certain lines of credit and loans of franchisees and unconsolidated affiliates. As of June 30, 2018, we have provided guarantees of approximately \$2 million on behalf of franchisees and no guarantees were outstanding for unconsolidated affiliates.

Legal Proceedings

From time to time, the Company is subject to various lawsuits covering a variety of allegations. 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 14 – Subsequent Events

On August 1, 2018, the Company announced that the Board of Directors declared a cash dividend of \$0.10 per share on Yum China’s common stock, payable as of the close of business on September 19, 2018, to stockholders of record as of the close of business on August 29, 2018. Total estimated cash dividend payable is approximately \$38 million.

On August 1, 2018, the Company entered into an agreement for an offshore credit facility of \$100 million. This credit facility has a term of three years and bears interest based on the prevailing rate stipulated by the London Interbank Offered Rate (LIBOR) administered by the ICE Benchmark Administration. As of the date of this report, the full amount of borrowing was available to us under this credit facility.

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 retail tax structure reform and the potential effects thereof, our growth plans, future capital resources to fund our operations and anticipated capital expenditures, share repurchases, our ability to pay 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, with over 8,100 restaurants as of June 30, 2018. Our growing restaurant base consists of China’s leading restaurant brands and concepts, primarily KFC, Pizza Hut, East Dawning, Little Sheep and Taco Bell. Following our separation from YUM, we have had the exclusive right to operate and sub-license the KFC, Pizza Hut and, subject to achieving certain agreed-upon milestones, Taco Bell brands in China, excluding Hong Kong, Taiwan and Macau (the “PRC” or “China”), and we own the East Dawning and Little Sheep marks outright. We were the first major global restaurant brand when we entered China in 1987 and we have developed deep operating experience in the market. We have since grown to become one of China’s largest restaurant developers with locations in over 1,200 cities as of June 30, 2018.

KFC is the leading Quick-Service Restaurant (“QSR”) brand in the PRC in terms of system sales and number of restaurants. As of June 30, 2018, KFC operated over 5,600 restaurants in over 1,200 cities across China. Measured by number of restaurants, we believe KFC has a two-to-one lead over the nearest Western QSR competitor in China, and KFC has continued to grow in both large and small cities. During the first quarter of 2018, the Company completed the acquisition of an additional 36% interest in an unconsolidated affiliate that operates KFC stores in Wuxi, China (“Wuxi KFC”), increasing equity interest to 83% and allowing the Company to consolidate the entity.

During the second quarter of 2017, we integrated the business of Pizza Hut Casual Dining and Pizza Hut Home Service as Pizza Hut. Segment financial information for prior periods has been recast to align with this change in segment reporting. After the integration, Pizza Hut continues to be the leading Casual Dining Restaurant (“CDR”) brand in China as measured by system sales and number of restaurants. We believe Pizza Hut has a four-to-one lead in terms of number of restaurants over its nearest Western CDR competitor in China. As of June 30, 2018, Pizza Hut operated over 2,200 restaurants in over 500 cities.

Separation from YUM

The Company separated from YUM on October 31, 2016, becoming an independent publicly traded company as a result of a pro rata distribution of all outstanding shares of Yum China common stock to shareholders of YUM. On October 31, 2016, YUM’s shareholders of record as of 5:00 p.m. Eastern Time on October 19, 2016 received one share of Yum China common stock for every one share of YUM common stock held as of the record date. Yum China’s common stock began trading “regular way” under the ticker symbol “YUMC” on the New York Stock Exchange on November 1, 2016.

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 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 a rate of approximately 6% of system sales. Franchise and unconsolidated affiliate restaurant sales are not included in Company sales on 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. 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, 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. Prior periods have been adjusted accordingly.
- 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.
- In addition to the results provided in accordance with GAAP throughout this MD&A, the Company provides measures adjusted for Special Items, which include Adjusted Operating Profit, Adjusted Diluted Earnings Per Common Share, Adjusted Effective Tax Rate and Adjusted EBITDA, which we define as net income including noncontrolling interests adjusted for income tax, interest income, depreciation, amortization and other items, including store impairment charges. The Special Item for the year to date ended June 30, 2018 represents a gain recognized from the re-measurement of our previously held equity interest in Wuxi KFC at fair value upon acquisition, as described in Note 2. 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 income tax, interest income, depreciation, amortization and other items, including store impairment charges. 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.

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.

Effective at the beginning of fiscal 2018, the Company changed its fiscal calendar from two months in the first quarter, three months in the second and third quarters and four months in the fourth quarter, to four three-month quarters ending on March 31, June 30, September 30 and December 31 of each year. Prior periods have been recast as if they had been reported under the new fiscal calendar.

Quarters and years to date ended June 30, 2018 and 2017

Results of Operations

Summary

The Company has two reportable segments: KFC and Pizza Hut. Our remaining operating segments, including the operations of East Dawning, Little Sheep, Taco Bell and Daojia, are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in the aggregate.

Quarterly highlights:

	% Change				
	System Sales(a)	Same-Store Sales(a)	Net New Units	Operating Profit (Reported)	Operating Profit (Ex F/X)
KFC	+5	+0	+7	+10	+2
Pizza Hut	(1)	(4)	+4	(49)	(52)
All Other Segments(b)	(21)	(10)	+14	(80)	(78)
Total	+3	(1)	+6	+13	+5

Year to Date highlights:

	% Change				
	System Sales(a)	Same-Store Sales(a)	Net New Units	Operating Profit (Reported)	Operating Profit (Ex F/X)
KFC	+7	+3	+7	+16	+8
Pizza Hut	(1)	(5)	+4	(55)	(58)
All Other Segments(b)	(27)	(7)	+14	NM	NM
Total	+5	+1	+6	+26	+16

NM refers to changes over 100%, from negative to positive amounts or from zero to an amount.

- (a) System Sales and Same-Store Sales percentages as shown in tables exclude the impact of F/X.
- (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 June 30, 2018, the Company operated over 8,100 units, predominately KFC and Pizza Hut restaurants, which are the leading QSR and CDR brand, respectively, in mainland China. Given our strong competitive position, a growing economy and a population of approximately 1.4 billion in mainland China, the Company has rapidly added KFC and Pizza Hut restaurants.

As compared to the second quarter of 2017, Company sales in the second quarter of 2018 increased 13%, or 6% if excluding the impact of F/X. The increase in Company sales during the quarter, excluding the impact of F/X, was driven by net unit growth, partially offset by same-store sales decline. Company sales for the year to date ended June 30, 2018 increased 15%, or 6% if excluding the impact of F/X. The year to date increase in Company sales, excluding the impact of F/X, was driven by net unit growth and same-store sales growth.

The decrease in Restaurant profit for the quarter, excluding the impact of F/X, was driven by higher promotion and product upgrade costs and wage inflation, partially offset by net unit growth. The year to date decrease in Restaurant profit, excluding the impact of F/X, was driven by higher promotion and product upgrade costs and wage inflation, partially offset by same-store sales leverage and net unit growth.

The Consolidated Results of Operations for the quarters and years to date ended June 30, 2018 and 2017 are presented below:

	Quarter Ended		% B/(W) (a)		Year to Date Ended		% B/(W) (a)	
	6/30/2018	6/30/2017	Reported	Ex F/X	6/30/2018	6/30/2017	Reported	Ex F/X
Company sales	\$ 1,888	\$ 1,664	13	6	\$ 3,904	\$ 3,402	15	6
Franchise fees and income	34	33	2	(5)	74	69	7	(1)
Revenues from transactions with franchisees and unconsolidated affiliates	141	141	—	(6)	302	288	5	(2)
Other revenues	5	3	79	70	9	8	15	10
Total revenues	\$ 2,068	\$ 1,841	12	5	\$ 4,289	\$ 3,767	14	5
Restaurant profit	\$ 286	\$ 276	3	(4)	\$ 647	\$ 630	3	(5)
Restaurant Margin %	15.1%	16.6%	(1.5) ppts.	(1.5) ppts.	16.6%	18.5%	(1.9) ppts.	(1.9) ppts.
Operating Profit	\$ 193	\$ 171	13	5	\$ 588	\$ 467	26	16
Interest income, net	10	4	NM	NM	18	8	NM	96
Income tax provision	(53)	(43)	(24)	(16)	(160)	(133)	(21)	(13)
Net Income - including noncontrolling interests	150	132	13	5	446	342	30	19
Net Income - noncontrolling interests	7	7	(2)	(9)	15	13	10	2
Net Income - Yum China Holdings, Inc.	\$ 143	\$ 125	14	6	\$ 431	\$ 329	31	20
Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31	16	6	\$ 1.08	\$ 0.83	30	19
Effective tax rate	26.0%	24.3%			26.4%	27.9%		
Adjusted Operating Profit	\$ 193	\$ 171			\$ 490	\$ 467		
Adjusted Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31			\$ 0.89	\$ 0.83		
Adjusted Effective Tax Rate	26.0%	24.3%			26.6%	27.9%		
Adjusted EBITDA	\$ 329	\$ 290			\$ 746	\$ 686		

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

Performance Metrics

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
System Sales Growth	11%	2%	13%	—%
System Sales Growth, excluding F/X	3%	7%	5%	6%
Same-Store Sales (Decline) Growth	(1)%	3%	1%	2%

<u>Unit Count</u>	6/30/2018	6/30/2017	% Increase (Decrease)
Company-owned	6,626	6,113	8
Unconsolidated affiliates	784	863	(9)
Franchisees	788	728	8
	8,198	7,704	6

Special Items

Special Items, along with the reconciliation to the most comparable GAAP financial measure, are presented below.

Detail of Special Items	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Gain from re-measurement of equity interest upon acquisition ^(a)	\$ —	\$ —	\$ 98	\$ —
Special Items Income - Operating Profit	—	—	98	—
Tax Expenses on Special Items ^(b)	—	—	(24)	—
Special Items Income, net of tax - including noncontrolling interests	—	—	74	—
Special Items Expense, net of tax - noncontrolling interests	—	—	—	—
Special Items Income, net of tax - Yum China Holdings, Inc.	\$ —	\$ —	\$ 74	\$ —
Weighted-average diluted shares outstanding	398	399	400	397
Special Items Diluted Earnings Per Common Share	\$ —	\$ —	\$ 0.19	\$ —
Reconciliation of Operating Profit to Adjusted Operating Profit				
Operating Profit	\$ 193	\$ 171	\$ 588	\$ 467
Special Items Income - Operating Profit	—	—	98	—
Adjusted Operating Profit	\$ 193	\$ 171	\$ 490	\$ 467
Reconciliation of EPS to Adjusted EPS				
Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31	\$ 1.08	\$ 0.83
Special Items Diluted Earnings Per Common Share	—	—	0.19	—
Adjusted Diluted Earnings Per Common Share	\$ 0.36	\$ 0.31	\$ 0.89	\$ 0.83
Reconciliation of Effective Tax Rate to Adjusted Effective Tax Rate				
Effective Tax Rate (See Note 11)	26.0%	24.3%	26.4%	27.9%
Impact on Effective Tax Rate as a result of Special Items ^(b)	—%	—%	(0.2)%	—%
Adjusted Effective Tax Rate	26.0%	24.3%	26.6%	27.9%

(a) As a result of the acquisition of Wuxi KFC in the first quarter of 2018, as disclosed in Note 2, the Company recognized a gain of \$98 million from the re-measurement of our previously held 47% equity interest at fair value, which was not allocated to any segment for performance reporting purposes.

(b) The tax expense was determined based upon the nature, as well as the jurisdiction, of each Special Item at the applicable tax rate.

Adjusted EBITDA

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

Reconciliation of Net Income to Adjusted EBITDA	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
Net Income — Yum China Holdings, Inc.	\$ 143	\$ 125	\$ 431	\$ 329
Net Income — noncontrolling interests	7	7	15	13
Income tax provision	53	43	160	133
Interest income, net	(10)	(4)	(18)	(8)
Operating Profit	193	171	588	467
Depreciation and amortization	117	100	235	196
Store impairment charges	19	19	21	23
Special Items Income – Operating Profit	—	—	(98)	—
Adjusted EBITDA	\$ 329	\$ 290	\$ 746	\$ 686

Segment Results

KFC

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	6/30/2018	6/30/2017	Reported	Ex F/X	6/30/2018	6/30/2017	Reported	Ex F/X
Company sales	\$ 1,352	\$ 1,159	17	9	\$ 2,796	\$ 2,358	19	10
Franchise fees and income	33	32	1	(7)	70	66	5	(3)
Revenues from transactions with franchisees and unconsolidated affiliates	15	15	(1)	(7)	32	32	—	(5)
Total revenues	<u>\$ 1,400</u>	<u>\$ 1,206</u>	16	8	<u>\$ 2,898</u>	<u>\$ 2,456</u>	18	9
Restaurant profit	\$ 227	\$ 203	12	4	\$ 528	\$ 452	17	8
Restaurant margin %	16.8%	17.5%	(0.7) ppts.	(0.7) ppts.	18.9%	19.2%	(0.3) ppts.	(0.3) ppts.
G&A expenses	\$ 45	\$ 38	(13)	(5)	\$ 91	\$ 77	(16)	(7)
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 15	\$ 15	1	7	\$ 32	\$ 32	—	6
Closure and impairment expenses, net	\$ 6	\$ 9	43	46	\$ 6	\$ 10	44	48
Other income, net	\$ (7)	\$ (11)	(40)	(43)	\$ (30)	\$ (30)	(2)	(8)
Operating Profit	\$ 199	\$ 182	10	2	\$ 495	\$ 427	16	8

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
System Sales Growth	12%	3%	15%	—%
System Sales Growth, excluding F/X	5%	8%	7%	5%
Same-Store Sales Growth	—%	4%	3%	2%

Unit Count	6/30/2018	6/30/2017	% Increase (Decrease)
	Company-owned	4,421	3,991
Unconsolidated affiliates	784	863	(9)
Franchisees	491	470	4
	<u>5,696</u>	<u>5,324</u>	7

Company Sales and Restaurant Profit

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

Income (Expense)	Quarter Ended				
	6/30/2017	Store Portfolio Actions	Other	F/X	6/30/2018
Company sales	\$ 1,159	\$ 86	\$ 12	\$ 95	\$ 1,352
Cost of sales	(348)	(28)	(7)	(30)	(413)
Cost of labor	(241)	(21)	(7)	(20)	(289)
Occupancy and other	(367)	(27)	1	(30)	(423)
Restaurant profit	<u>\$ 203</u>	<u>\$ 10</u>	<u>\$ (1)</u>	<u>\$ 15</u>	<u>\$ 227</u>

Income (Expense)	Year to Date Ended				
	6/30/2017	Store Portfolio Actions	Other	F/X	6/30/2018
Company sales	\$ 2,358	\$ 151	\$ 79	\$ 208	\$ 2,796
Cost of sales	(701)	(48)	(25)	(63)	(837)
Cost of labor	(482)	(36)	(21)	(43)	(582)
Occupancy and other	(723)	(46)	(17)	(63)	(849)
Restaurant profit	\$ 452	\$ 21	\$ 16	\$ 39	\$ 528

The quarter and year to date increases in Company sales and Restaurant profit associated with store portfolio actions, excluding the impact of F/X, were driven by net unit growth. Significant other factors impacting Company sales and Restaurant profit were the Company same-store sales growth, partially offset by higher labor costs mainly due to wage inflation of 6% and higher promotion costs.

Franchise Fees and Income

The quarter and year to date decreases in Franchise fees and income, excluding the impact of F/X, were primarily driven by the acquisition of Wuxi KFC, partially offset by same-store sales growth of unconsolidated affiliates and net unit growth.

G&A Expenses

The quarter and year to date increases in G&A expenses, excluding the impact of F/X, were primarily driven by higher compensation costs due to merit increases.

Operating Profit

The quarter and year to date increases in Operating Profit, excluding the impact of F/X, were primarily driven by the Company same-store sales growth and net unit growth, partially offset by higher restaurant operating costs and higher G&A expenses.

Pizza Hut

	Quarter Ended				Year to Date Ended			
	6/30/2018	6/30/2017	% B/(W)		6/30/2018	6/30/2017	% B/(W)	
			Reported	Ex F/X			Reported	Ex F/X
Company sales	\$ 528	\$ 497	6	(1)	\$ 1,092	\$ 1,024	7	(1)
Franchise fees and income	—	—	23	15	1	1	24	15
Revenues from transactions with franchisees and unconsolidated affiliates	—	1	5	(1)	—	1	(1)	(6)
Total revenues	\$ 528	\$ 498	6	(1)	\$ 1,093	\$ 1,026	7	(1)
Restaurant profit	\$ 58	\$ 74	(20)	(26)	\$ 118	\$ 178	(34)	(39)
Restaurant margin %	11.2%	14.9%	(3.7) ppts.	(3.7) ppts.	10.8%	17.4%	(6.6) ppts.	(6.6) ppts.
G&A expenses	\$ 28	\$ 26	(6)	2	\$ 56	\$ 51	(10)	(2)
Expenses for transactions with franchisees and unconsolidated affiliates	\$ —	\$ 1	(5)	2	\$ —	\$ 1	1	6
Closure and impairment expenses, net	\$ 11	\$ 9	(34)	(25)	\$ 10	\$ 8	(22)	(14)
Other income, net	\$ (1)	\$ —	NM	NM	\$ (2)	\$ —	NM	NM
Operating Profit	\$ 20	\$ 39	(49)	(52)	\$ 54	\$ 119	(55)	(58)

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
System Sales Growth	7%	1%	7%	2%
System Sales (Decline) Growth, excluding F/X	(1)%	6%	(1)%	7%
Same-Store Sales (Decline) Growth	(4)%	—%	(5)%	1%

Unit Count	6/30/2018	6/30/2017	% Increase
Company-owned	2,179	2,094	4
Franchisees	30	28	7
	<u>2,209</u>	<u>2,122</u>	4

Company Sales and Restaurant Profit

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

Income (Expense)	Quarter Ended				
	6/30/2017	Store Portfolio Actions	Other	F/X	6/30/2018
Company sales	\$ 497	\$ 16	\$ (21)	\$ 36	\$ 528
Cost of sales	(132)	(5)	(8)	(11)	(156)
Cost of labor	(122)	(4)	3	(10)	(133)
Occupancy and other	(169)	(5)	5	(12)	(181)
Restaurant profit	<u>\$ 74</u>	<u>\$ 2</u>	<u>\$ (21)</u>	<u>\$ 3</u>	<u>\$ 58</u>

Income (Expense)	Year to Date Ended				
	6/30/2017	Store Portfolio Actions	Other	F/X	6/30/2018
Company sales	\$ 1,024	\$ 37	\$ (49)	\$ 80	\$ 1,092
Cost of sales	(261)	(12)	(26)	(24)	(323)
Cost of labor	(246)	(10)	(3)	(21)	(280)
Occupancy and other	(339)	(11)	6	(27)	(371)
Restaurant profit	<u>\$ 178</u>	<u>\$ 4</u>	<u>\$ (72)</u>	<u>\$ 8</u>	<u>\$ 118</u>

The decreases in Company sales and Restaurant profit for the quarter, excluding the impact of F/X, were driven by Company same-store sales decline, higher promotion and product upgrade costs, and higher labor costs mainly attributable to wage inflation of 7%, partially offset by net unit growth and labor efficiency.

The year to date decreases in Company sales and Restaurant profit, excluding the impact of F/X, were driven by Company same-store sales decline, higher promotion and product upgrade costs, and higher labor costs mainly attributable to wage inflation of 6%, partially offset by net unit growth and labor efficiency.

G&A Expenses

The decrease in G&A expenses for the quarter, excluding the impact of F/X, was primarily driven by less performance-based compensation.

The year to date increase in G&A expenses, excluding the impact of F/X, was primarily driven by higher compensation costs due to merit increases, partially offset by less performance-based compensation.

Operating Profit

The quarter and year to date decreases in Operating Profit, excluding the impact of F/X, were primarily driven by same-store sales decline and higher restaurant operating costs mainly attributable to promotion and product upgrade costs and wage inflation.

All Other Segments

All Other Segments includes East Dawning, Little Sheep, Taco Bell and Daojia.

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	6/30/2018	6/30/2017	Reported	Ex F/X	6/30/2018	6/30/2017	Reported	Ex F/X
Company sales	\$ 8	\$ 8	(14)	(20)	\$ 16	\$ 20	(21)	(27)
Franchise fees and income	1	1	52	41	3	2	58	45
Revenues from transactions with franchisees and unconsolidated affiliates	4	4	16	7	11	9	18	9
Other revenues	5	3	66	60	8	8	(0)	(4)
Total revenues	<u>\$ 18</u>	<u>\$ 16</u>	11	5	<u>\$ 38</u>	<u>\$ 39</u>	(4)	(10)
Restaurant profit	\$ —	\$ (1)	(5)	2	\$ —	\$ —	NM	NM
Restaurant margin %	-8.5%	-6.9%	(1.6) ppts.	(1.6) ppts.	-2.8%	2.2%	(5.0) ppts.	(5.0) ppts.
G&A expenses	\$ 9	\$ 4	NM	NM	\$ 16	\$ 7	NM	NM
Expenses for transactions with franchisees and unconsolidated affiliates	\$ 3	\$ 3	5	11	\$ 9	\$ 8	(6)	1
Operating Loss	\$ (7)	\$ (3)	(80)	(78)	\$ (11)	\$ (2)	NM	NM

	Quarter Ended		Year to Date Ended	
	6/30/2018	6/30/2017	6/30/2018	6/30/2017
	(10)%	(2)%	(7)%	(9)%
Same-Store Sales Decline				

The quarter and year to date decreases in Company sales, excluding the impact of F/X, were primarily driven by unit closures and refranchising of Little Sheep units.

The quarter and year to date increases in G&A expenses were primarily due to G&A expenses incurred by Daojia, which was acquired by the Company during the second quarter of 2017.

Corporate and Unallocated

	Quarter Ended				Year to Date Ended			
			% B/(W)				% B/(W)	
	6/30/2018	6/30/2017	Reported	Ex F/X	6/30/2018	6/30/2017	Reported	Ex F/X
Revenues from transactions with franchisees and unconsolidated affiliates	\$ 122	\$ 121	—	(6)	\$ 259	\$ 246	5	(3)
Other revenue	1	—	NM	NM	2	—	NM	NM
Expenses for transactions with franchisees and unconsolidated affiliates	120	118	(2)	5	257	243	(6)	2
Other operating costs	1	—	NM	NM	2	—	NM	NM
Corporate G&A expenses	19	50	62	64	52	81	35	39
Other expenses (income) (See Note 12)	2	—	NM	NM	(100)	(1)	NM	NM
Interest income, net	10	4	NM	NM	18	8	NM	96
Income tax provision (See Note 11)	(53)	(43)	(24)	(16)	(160)	(133)	(21)	(13)
Effective tax rate (See Note 11)	26.0%	24.3%	(1.7)%	(1.8)%	26.4%	27.9%	1.5%	1.2%

Revenues from Transactions with Franchisees and Unconsolidated Affiliates

The quarter and year to date decreases in Revenues from transactions with franchisees and unconsolidated affiliates, excluding the impact of F/X, were primarily driven by the acquisition of Wuxi KFC, partially offset by system sales growth of unconsolidated affiliates and franchisees.

G&A Expenses

The quarter and year to date decreases in G&A expenses, excluding the impact of F/X, were driven by higher government incentives, less employee benefits and less professional service fees, partially offset by higher compensation costs due to merit increases.

Interest Income, Net

The quarter and year to date increases in interest income, net were driven by higher returns on larger balances of short-term investments and time deposits.

Income Tax Provision

Our income tax provision includes tax on our earnings at the Chinese statutory tax rate of 25%, a 10% withholding tax on repatriation of earnings outside of China and U.S. corporate income tax, if any. Our effective tax rate was 26.0% and 24.3% for the quarters ended June 30, 2018 and 2017, respectively, and 26.4% and 27.9% for the year to date ended June 30, 2018 and 2017, respectively. The higher effective tax rate for the quarter was primarily due to less excess tax benefit driven by the exercise of share-based awards recognized, offset by less estimated repatriation of current year earnings outside of China. The lower year-to-date effective tax rate was primarily due to less estimated repatriation of current year earnings outside of China.

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

The Tax Act

In December 2017, the U.S. enacted the Tax Act, which included a broad range of tax reforms, including, but not limited to, the establishment of a flat corporate income tax rate of 21%, the elimination or reduction of certain business deductions and the imposition of tax on deemed repatriation of accumulated undistributed foreign earnings. The Tax Act has impacted Yum China in two material aspects: (i) all of the foreign-source dividends received by Yum China from its foreign subsidiaries will be exempted from taxation starting from the tax year beginning after December 31, 2017 and (ii) Yum China recorded, in the fourth quarter of 2017, an additional income tax expense of \$163.9 million, which includes an estimated one-time transition tax of \$129.8 million on the deemed repatriation of accumulated undistributed foreign earnings, \$4.5 million primarily related to the re-measurement of certain deferred tax assets based on the rates at which they are expected to reverse in the future, and the valuation allowance of \$29.6 million for certain deferred tax assets.

The Tax Act requires complex computations with significant estimates to be performed, significant judgments to be made in interpretation of the provisions, and the preparation and analysis of information not previously relevant or regularly produced. The U.S. Treasury Department, the IRS, the SEC and other standard-setting bodies could interpret or issue guidance on how provisions of the Tax Act will be applied or otherwise administered that is different from our current interpretation. As we complete our analysis of the Tax Act, collect and prepare necessary data, and interpret any additional guidance, we may make adjustments to provisional amounts that we have recorded that may materially impact our provision for income taxes in the period in which the adjustments are made. We expect to complete our analysis within the measurement period not exceeding one year from the enactment date.

Tax Examination on Transfer Pricing

We are subject to reviews, examinations and audits by Chinese tax authorities, the IRS and other taxing authorities with respect to income and non-income based taxes. Currently we are under a national audit on transfer pricing by the SAT in China regarding our related party transactions for the period from 2006 to 2015. It is reasonably possible that there could be significant developments within the next 12 months. The ultimate assessment will depend upon further review of the information provided and ongoing discussions with the SAT and in-charge local tax authorities, and therefore it is not possible to reasonably estimate the potential impact. We will continue to defend our transfer pricing position. However, if the SAT 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, the Chinese government implemented reform to its retail tax structure, which is intended to be a progressive and positive shift to more closely align with a more modern service-based economy. Under this reform, a 6% output VAT replaced the 5% business tax previously applied to certain restaurant sales. VAT rates imposed on goods and services included 17%, 13%, 11% and 6%. Input VAT would be creditable to the aforementioned 6% output VAT.

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 an input VAT credit 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 input VAT credit asset for recoverability based on its forecasted operating results. We evaluate the recoverability of the net VAT credit asset based on our estimated operating results and capital spending, which inherently includes significant assumptions that are subject to change.

As of June 30, 2018, an input VAT credit asset of \$197 million and payable of \$10 million were recorded in Other assets and other current liabilities, respectively, on the Condensed Consolidated Balance Sheets. The Company has not made an allowance for the recoverability of the input VAT credit asset, as the balance is expected to be utilized to offset against net VAT payables more than one year from June 30, 2018. Any input VAT credit asset would be classified as Prepaid expenses and other current assets if the Company expected to use the credit within one year.

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.

Effective from July 1, 2017, the 13% VAT rate primarily applicable to certain agricultural products was reduced to 11%. Effective from May 1, 2018, the VAT rates of 17% and 11% were lowered to 16% and 10%, respectively. 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.

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.

Consolidated Cash Flows

Our cash flows for the years to date ended June 30, 2018 and 2017 were as follows:

Net cash provided by operating activities was \$819 million in 2018 as compared to \$604 million in 2017. The increase was primarily driven by higher Net income and timing of payments for inventory.

Net cash used in investing activities was \$406 million in 2018 as compared to \$465 million in 2017. The decrease was primarily driven by cash inflow generated by short-term investment activities, partially offset by the acquisition of Wuxi KFC.

Net cash used in financing activities was \$186 million in 2018 as compared to \$110 million in 2017. The increase was primarily driven by cash dividends paid to stockholders.

Liquidity and Capital Resources

Historically we have funded our operations through cash generated from the operation of our Company-owned stores and from our franchise operations and dividend payments from our unconsolidated affiliates.

Our ability to fund our future operations and capital needs will 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, capital expenditures and any distributions to our stockholders or share repurchases we may make. We believe that our future cash from operations, together with our access to funds on hand and capital markets, will provide adequate resources to fund these uses of cash and that our existing cash and net cash from operations 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 or absence of a credit rating;
- the liquidity of the overall capital markets; and
- the state of the Chinese, U.S. and global economies.

There can be no assurance, particularly as a relatively new company that currently has no credit rating, 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.

Dividends and Share Repurchases

On February 7, 2017, we announced that our Board of Directors authorized a \$300 million share repurchase program. On October 4, 2017, the Board of Directors increased Yum China's existing share repurchase authorization from \$300 million to an aggregate of \$550 million. 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. During the year to date ended June 30, 2018, the Company repurchased \$73 million, or 1.9 million shares, of common stock under the repurchase program.

Our ability to declare and pay any dividends on our stock may be restricted by 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.

On February 6, 2018, the Board of Directors declared a cash dividend of \$0.10 per share. The cash dividend totaling \$39 million was paid to stockholders in March 2018.

On May 1, 2018, the Board of Directors declared a cash dividend of \$0.10 per share. The cash dividend totaling \$38 million was paid to stockholders in June 2018.

On August 1, 2018, the Company announced that the Board of Directors declared a cash dividend of \$0.10 per share on Yum China's common stock, payable as of the close of business on September 19, 2018, to stockholders of record as of the close of business on August 29, 2018. Total estimated cash dividend payable is approximately \$38 million.

Borrowing Capacity

As of June 30, 2018, the Company had credit facilities of RMB 2,162 million (approximately \$327 million), including onshore credit facilities of RMB1,500 million (approximately \$227 million) in the aggregate and an offshore credit facility of \$100 million.

The credit facilities have terms ranging from one to three years. Each credit facility bears interest based on the prevailing rate stipulated by the People's Bank of China or London Interbank Offered Rate (LIBOR) administered by the ICE Benchmark Administration. 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 financial covenants including, among other things, limitations on certain additional indebtedness and liens, and certain other transactions specified in the respective agreement. Interest on any outstanding borrowings is due at least monthly. As of June 30, 2018, the full amount of borrowings was available to us under each facility.

On August 1, 2018, the Company entered into an agreement for an offshore credit facility of \$100 million. This credit facility has a term of three years and bears interest based on the prevailing rate stipulated by the London Interbank Offered Rate (LIBOR) administered by the ICE Benchmark Administration. As of the date of this report, the full amount of borrowing was available to us under this credit facility.

Off-Balance Sheet Arrangements

See the Guarantees section of Note 13 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 February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)* (“ASU 2016-02”), which increases transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. In July 2018, the FASB issued amendments allowing an optional transition method, which recognizes a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption rather than in the earliest period presented as prescribed in ASU 2016-02. We are currently evaluating which transition method we will utilize. We currently plan to use the package of practical expedients that allows us to not reassess: (1) whether any expired or existing contracts are or contain leases, (2) lease classification for any expired or existing leases and (3) initial direct costs for any expired or existing leases. We also plan to elect the hindsight practical expedient to determine the reasonably certain lease term for existing leases. We expect this standard will have a material effect on our financial statements. While we are continuing to assess the effect of adoption, we currently believe the most significant changes relate to the recognition and measurement of right-of-use assets and lease liabilities on our balance sheet for operating leases of the land and/or building of our restaurants and office space. At June 30, 2018, we operated more than 6,600 restaurants, leasing the underlying land and/or building, with our commitments expiring within 20 years from the inception of the lease. The amount of our future minimum lease payments under operating leases was approximately \$3 billion as of June 30, 2018. We anticipate continuing to add more restaurants and increase our leasing activity between now and adoption. We are also implementing software to meet the reporting requirements of the new standard, and identifying changes to our business processes and controls to support the adoption of the new standard.

In June 2016, the FASB issued ASU No. 2016-13, *Financial Instruments – Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments* (“ASU 2016-13”), which requires measurement and recognition of expected versus incurred credit losses for financial assets held. ASU 2016-13 is effective for the Company from January 1, 2020, with early adoption permitted beginning from January 1, 2019. We are currently evaluating the impact the adoption of this standard will have on our financial statements.

In May 2017, the FASB issued ASU No. 2017-09, *Compensation – Stock Compensation (Topic 718): Scope of Modification Accounting* (“ASU 2017-09”), which clarifies that modification accounting is required only if the fair value, the vesting conditions, or the classification of the award (as equity or liability) changes as a result of the changes in terms or conditions. ASU 2017-09 is effective for the Company from January 1, 2019, with early adoption permitted. We are currently evaluating the impact the adoption of this standard will have on our financial statements.

In February 2018, the FASB issued ASU 2018-02, *Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income* (“ASU 2018-02”). The new guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act and will improve the usefulness of information reported to financial statement users. ASU 2018-02 is effective for the Company from January 1, 2019, with early adoption permitted. We are currently evaluating the impact the adoption of this standard will have on our financial statements.

In June 2018, the FASB issued ASU 2018-07, *Compensation – Stock Compensation (Topic 718) - Improvements to Nonemployee Share-Based Payment Accounting* (“ASU 2018-07”). The new guidance largely aligns the accounting for share-based awards issued to employees and nonemployees. Existing guidance for employee awards will apply to nonemployee share-based transactions with limited exceptions. The new guidance also clarifies that any share-based payment awards issued to customers should be evaluated under ASC 606, *Revenue from Contracts with Customers*. ASU 2018-07 is effective for the Company from January 1, 2019, with early adoption permitted. We are currently evaluating the impact the adoption of this standard will 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,” “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 food-borne illness concerns, (b) significant failure to maintain effective quality control 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 diseases, (e) the fact that we derive substantially all of our revenue from our operations in China, (f) the fact that the operation of our restaurants is subject to the terms of the master license agreement with YUM, (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 and other supplies, (i) our inability to attain our target development goals and the potential cannibalization of existing sales by aggressive development, (j) fluctuation of raw materials prices, (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, delivery aggregators, internet infrastructure operators and internet service providers, (s) failure to provide timely and reliable delivery services by our restaurants, (t) our inability to integrate Daojia successfully and the anticipated benefits of the acquisition may not be realized in a timely manner or at all, (u) the Chinese government may determine that the VIE structure of Daojia does not comply with Chinese laws on foreign investment in restricted industries, (v) our inability or failure to recognize, respond to and effectively manage the accelerated impact of social media, (w) litigation and failure to comply with anti-bribery or anti-corruption laws, (x) U.S. federal income taxes, changes in tax rates, disagreements with taxing authorities and imposition of new taxes, (y) changes in consumer discretionary spending and general economic conditions, (z) competition in the retail food industry, (aa) loss or failure to obtain or renew any or all of the approvals, licenses and permits to operate our business, (bb) our inability to adequately protect the intellectual property we own or have the right to use, (cc) YUM's failure to protect its intellectual property, (dd) seasonality and certain major events in China, (ee) our failure to detect, deter and prevent all instances of fraud or other misconduct committed by our employees, customers or other third parties, (ff) changes in accounting standards and subjective assumptions, estimates and judgments by management related to complex accounting matters, (gg) failure of our insurance policies to provide adequate coverage for claims associated with our business operations, (hh) failure by us to maintain effective disclosure controls and procedures and internal control over financial reporting in accordance with the rules of the SEC and (ii) unforeseeable business interruptions;

- Risks related to doing business in China, such as (a) changes in Chinese political policies and economic and social policies or conditions, (b) changes in laws and regulations, (c) uncertainties with respect to the interpretation and enforcement of Chinese laws, rules and regulations, (d) fluctuation in the value of the Chinese Renminbi, (e) limitations on our ability to utilize our cash balances effectively due to governmental control of currency conversion and payments of foreign currency, (f) reliance on distributions by our operating subsidiaries in China to fund offshore cash requirements, (g) potential unfavorable tax consequences resulting from our classification as a China resident enterprise for Chinese enterprise income tax purposes, (h) uncertainty regarding indirect transfers of equity interests and enhanced scrutiny by Chinese tax authorities, (i) inability to use properties due to defects caused by non-registration of lease agreements related to certain properties, (j) risk in relation to unexpected land acquisitions, building closures or demolitions, (k) potential fines for failure to comply with law and (l) 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;
- Risks related to the separation and related transactions, such as (a) not achieving all of the anticipated benefits, (b) 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, (c) 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, (d) limitations on our ability to engage in strategic transactions as a result of the separation, (e) our inability to satisfy financial reporting and other requirements to which we are subject as an independent publicly traded company, (f) limited experience of our management in managing a public company, (g) inability to access capital markets on acceptable terms, (h) increased administrative and other costs incurred by virtue of our status as an independent public company, (i) limitations on our ability to compete with YUM and other restrictions on our operations contained in the master license agreement, (j) failure by YUM to perform its obligations under the transaction agreements that we entered into with it as part of the separation, (k) potential indemnification liabilities owing to YUM pursuant to the separation and distribution agreement and there being no assurance that the indemnity provided by YUM with respect to certain liabilities in connection with the separation will be sufficient to insure us against the full amount of such liabilities, (l) the possibility that a court would require that we assume responsibility for obligations allocated to YUM under the separation and distribution agreement, (m) potential liabilities due to fraudulent transfer considerations and (n) actual or potential conflicts of interest of certain of our executive officers and directors because of their previous positions at YUM.

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 Securities and Exchange Commission (including the information set forth under the captions "Forward-Looking Statements" and "Risk Factors" included in the Company's Annual Report on Form 10-K for the year ended December 31, 2017) 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 June 30, 2018, the Company's Operating Profit would have decreased approximately \$18 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.

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 or in other factors that materially affected, or are reasonably likely to materially affect, internal control over financial reporting during the quarter ended June 30, 2018.

PART II – Other Information

Item 1. Legal Proceedings

Information regarding legal proceedings is incorporated by reference from Note 13 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. There have been no material changes from the risk factors disclosed in Part I, Item 1A. “Risk Factors” in our Annual Report on Form 10-K for the year ended December 31, 2017, which was filed with the SEC on February 27, 2018.

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

On February 7, 2017, we announced that our Board of Directors authorized a \$300 million share repurchase program. On October 4, 2017, the Board of Directors increased Yum China’s existing share repurchase authorization from \$300 million to an aggregate of \$550 million. The authorizations do not have an expiration date.

The following table provides information as of June 30, 2018 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)
4/1/18-4/30/18	39	\$ 38.68	39	\$ 420
5/1/18-5/31/18	1,471	\$ 38.20	1,471	\$ 364
6/1/18-6/30/18	400	\$ 39.18	400	\$ 349
Total	1,910	\$ 38.41	1,910	\$ 349

Item 6. Exhibits

<u>Exhibit Number</u>	<u>Description of Exhibits</u>
3.1	<u>Amended and Restated Certificate of Incorporation of Yum China Holdings, Inc. (incorporated by reference to Exhibit 3.1 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).</u>
3.2	<u>Amended and Restated Bylaws of Yum China Holdings, Inc. (incorporated by reference to Exhibit 3.2 to Yum China Holdings, Inc.'s Current Report on Form 8-K filed on November 1, 2016).</u>
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 *
101.SCH	XBRL Taxonomy Extension Schema Document *
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document *
101.LAB	XBRL Taxonomy Extension Label Linkbase Document *
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document *
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document *

* Filed or furnished herewith.

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: August 8, 2018

/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: August 8, 2018

/s/ Joey Wat

Joey Wat

Chief Executive Officer

CERTIFICATION

I, Jacky Lo, 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: August 8, 2018

/s/ Jacky Lo

Jacky Lo

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 June 30, 2018, 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: August 8, 2018

/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 June 30, 2018, as filed with the Securities and Exchange Commission on the date hereof (the "Periodic Report"), I, Jacky Lo, 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: August 8, 2018

/s/ Jacky Lo

Jacky Lo

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.