KFC Holdings Japan / 9873

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How to read a Shared Research report: This report begins with the trends and outlook section, which discusses the company's most recent earnings. First-time readers should start at the business section later in the report.

Executive summary

Core businesses

Under a master franchise agreement with Yum! Brands, Inc., KFC Holdings Japan operates Kentucky Fried Chicken brand restaurants in Japan, which mainly processes and sells fried chicken. The company also acts as a franchisor in Japan for the Kentucky Fried Chicken brand, earning royalties and other revenues.

As of end-March 2021, the company had 299 directly operated restaurants primarily in Greater Tokyo, and 839 restaurants run by franchisees, mainly in regional areas. It boasts the leading domestic market share in fried chicken fast food restaurants, and it is one of the most well-known fast food restaurant brands, alongside such names as McDonald's and Mos Burger.

Japan's fried chicken market has been relatively flat since 2000, and in 2003 major convenience stores began entering the fried chicken market. KFC is distinctive due to the brand power of its "original-recipe chicken," which it has cultivated since its launch in Japan in 1970, and procurement arrangements with major trading company Mitsubishi Corporation (TSE1: 8058; has 35.1% stake in the company) for high-quality chicken. Convenience stores primarily use imported frozen chicken 50 days old or older, while KFC's "original-recipe chicken" uses only Japan-raised chickens (about 38 days old), which are more tender and flavorsome.

Trends and outlook

- In FY03/21, the company reported revenues of JPY89.7bn (+12.6% YoY), operating profit of JPY6.4bn (+32.8% YoY), recurring profit of JPY5.5bn (+69.1% YoY), and net income of JPY2.8bn (+82.9% YoY). At its mainstay KFC business, sales at existing stores were up 13.6% YoY, store traffic rising 4.1% YoY, and average spending per customer up 9.1% YoY. Revenues and profits grew YoY aided by various initiatives, including growth in sales through its existing takeout and drive-through channels, increasing the number of stores offering home delivery service, and store remodelings aimed at maintaining and enhancing its brand image. On the minus side, the harsh operating environment in the wake of the COVID-19 pandemic weighed on its equity-method affiliates and left KFC Holdings with JPY1.3bn in losses on investments in equity-method affiliates (booked under non-operating expenses). The company also booked extraordinary losses of JPY300mn to reflect asset impairment charges taken against stores and other assets whose profitability appeared to unlikely to recover to previous levels. For FY03/21, the company will pay dividends of JPY60 per share (including a JPY10 dividend to commemorate its 50th anniversary), representing a dividend payout ratio of 47.8%.
- For FY03/22, the company forecasts revenues of JPY95.7bn (+6.7% YoY), operating profit of JPY5.8bn (-8.8% YoY), recurring profit of JPY5.0bn (-8.8% YoY), and net income of JPY2.8bn (+0.9% YoY). The company aims to boost sales at existing stores with the help of more store remodelings and increases in the number of stores offering home delivery service. It also plans to accelerate the opening of new stores. The operating profit forecast calls for a YoY decline despite the outlook for higher revenues because of an increase in expenses such as IT system investment for future growth and investment to streamline operations.
- In April 2021, the company announced its new medium-term management plan dubbed "Second Founding: Setting the Stage for Continued Growth Over the Next 50 Years." The core strategies under the new medium-term plan call for 1) promoting further growth at its KFC business, 2) further expanding the group's business portfolio and boosting the enterprise value of its capital and business alliance partners, and 3) building out its business foundation to support growth. For FY03/24, the company targets revenues of JPY107.2bn, operating profit of JPY6.3bn, and net income of JPY3.5bn.

Strengths and weaknesses

Shared Research thinks the company's strengths are brand power cultivated since its founding; a business model built on a relationship with Mitsubishi; and economies of scale. We think its weaknesses are constraints on KFC sales promotions due to using 100% domestically raised chicken and constraints imposed by franchise agreements with Yum! Brands.

Key financial data

Income statement (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.	FY03/22 Est.
Total revenues	**85,864**	**83,436**	**84,605**	**88,180**	**88,032**	**73,457**	**74,344**	**79,634**	**89,652**	**95,688**
YoY	-2.6%	-2.8%	1.4%	4.2%	-0.2%	-16.6%	1.2%	7.1%	12.6%	6.7%
Gross profit	39,656	38,460	38,206	39,364	39,887	31,604	32,037	34,959	38,698	-
YoY	-0.1%	-3.0%	-0.7%	3.0%	1.3%	-20.8%	1.4%	9.1%	10.7%	-
Gross profit margin	46.2%	46.1%	45.2%	44.6%	45.3%	43.0%	43.1%	43.9%	43.2%	-
SG&A expenses	37,261	36,638	37,536	37,352	37,328	31,127	29,831	30,173	32,344	-
YoY	-0.1%	-1.7%	2.5%	-0.5%	-0.1%	-16.6%	-4.2%	1.1%	7.2%	-
SG&A ratio	43.4%	43.9%	44.4%	42.4%	42.4%	42.4%	40.1%	37.9%	36.1%	-
Operating profit	**2,395**	**1,822**	**670**	**2,011**	**2,558**	**477**	**2,206**	**4,785**	**6,354**	**5,793**
YoY	0.2%	-23.9%	-63.2%	200.1%	27.2%	-81.4%	362.5%	116.9%	32.8%	-8.8%
Operating profit margin	2.8%	2.2%	0.8%	2.3%	2.9%	0.6%	3.0%	6.0%	7.1%	6.1%
Recurring profit	**2,506**	**1,856**	**667**	**1,866**	**2,425**	**627**	**2,975**	**3,252**	**5,498**	**5,012**
YoY	1.5%	-25.9%	-64.1%	179.8%	30.0%	-74.1%	374.5%	9.3%	69.1%	-8.8%
Recurring profit margin	2.9%	2.2%	0.8%	2.1%	2.8%	0.9%	4.0%	4.1%	6.1%	5.2%
Net income attributable to owners of the parent	**1,203**	**441**	**-524**	**730**	**1,365**	**578**	**2,055**	**1,533**	**2,805**	**2,831**
YoY	9.2%	-63.3%	-	-	87.0%	-57.7%	255.5%	-25.4%	83.0%	0.9%
Net margin	1.4%	0.5%	-0.6%	0.8%	1.6%	0.8%	2.8%	1.9%	3.1%	3.0%
Per-share data (split-adjusted; JPY)										
Shares issued (year-end; '000)	22,783	22,783	22,783	22,783	22,783	22,783	22,783	22,424	22,424	
EPS	53.64	19.69	-23.4	32.59	60.90	25.83	91.99	68.62	125.50	126.63
EPS (fully diluted)	-	-	-	-	-	-	-	-	-	
Dividend per share	50.00	50.00	50.00	50.00	50.00	50.00	50.00	50.00	60.00	50.00
Book value per share	1,034.60	1,002.93	946.18	932.24	944.43	922.83	956.80	975.69	1,056.53	
Balance sheet (JPYmn)										
Current assets	23,340	21,682	22,332	21,390	20,721	14,952	19,196	20,898	26,141	
Cash and cash equivalents	13,502	16,146	16,804	15,339	14,571	9,757	13,267	14,917	18,476	
Accounts receivable	3,544	3,701	3,546	3,855	4,007	3,562	4,269	4,386	5,751	
Inventories	729	518	397	697	450	414	486	386	406	
Other	5,565	1,317	1,585	1,499	1,693	1,219	1,174	1,209	1,405	
Fixed assets	16,968	16,301	16,085	17,902	18,762	20,793	19,223	17,113	16,553	
Tangible fixed assets	6,184	5,703	6,093	7,178	8,506	7,734	6,474	6,197	6,123	
Intangible assets	2,950	2,924	2,874	2,828	2,206	1,704	1,091	1,083	1,591	
Investments and other assets	7,834	7,674	7,118	7,896	8,050	11,354	11,658	9,832	8,838	
Total assets	40,308	37,984	38,418	39,292	39,484	35,746	38,420	38,012	42,694	
Current liabilities	13,029	11,203	13,166	13,070	13,033	10,929	13,222	12,514	15,265	
Accounts payable	6,568	5,754	5,978	6,232	5,824	5,735	6,664	5,626	6,757	
Short-term debt	211	193	187	531	618	531	519	115	87	
Other current liabilities	6,250	5,256	7,001	6,307	6,591	4,663	6,039	6,773	8,417	
Fixed liabilities	4,065	4,283	4,031	5,317	5,272	4,190	3,812	3,690	3,808	
Long-term debt	207	188	432	1,533	1,142	666	189	171	196	
Other	3,858	4,095	3,599	3,784	4,130	3,524	3,623	3,519	3,612	
Net assets	23,214	22,497	21,219	20,904	21,178	20,626	21,385	21,807	23,620	
Capital stock	7,297	7,297	7,297	7,297	7,297	7,297	7,297	7,297	7,297	
Capital surplus	10,430	10,430	10,430	10,430	10,430	10,430	10,430	9,689	9,689	
Retained earnings	6,165	5,485	4,228	3,837	4,082	3,539	4,473	4,886	6,570	
Treasury stock	-710	-722	-733	-739	-739	-887	-887	-147	-134	
Accum. other comprehensive income	31	7	-2	79	108	246	71	81	197	
Minority interests	-	-	-	-	-	-	-	-	-	
Total liabilities and equity	40,308	37,984	38,418	39,292	39,484	35,746	38,420	38,012	42,694	
Statement of cash flows (JPYmn)										
Cash flows from operating activities	3,370	1,717	4,574	1,519	4,424	1,928	5,436	3,934	7,042	
Cash flows from investing activities	-1,558	2,287	-1,556	-298	-3,679	-4,863	-265	-626	-2,246	
Cash flows from financing activities	-1,367	-1,360	-1,360	-1,686	-1,512	-1,878	-1,660	-1,657	-1,237	
Financial ratios										
Interest-bearing debt	418	381	619	2,064	1,760	1,197	708	286	283	
Net cash	13,084	15,765	16,185	13,275	12,811	8,560	12,559	14,631	18,193	
ROA (RP-based)	6.1%	4.7%	1.7%	4.8%	6.2%	1.7%	8.0%	8.5%	13.6%	
ROE	5.2%	1.9%	-2.4%	3.5%	6.5%	2.8%	9.8%	7.1%	12.3%	
Current ratio	179%	194%	170%	164%	159%	137%	145%	167%	171%	
Fixed ratio	73.1%	72.5%	75.8%	85.6%	88.6%	100.8%	89.9%	78.5%	70.1%	
Equity ratio	57.6%	59.2%	55.2%	53.2%	53.6%	57.7%	55.7%	57.4%	55.3%	

Source: Shared Research based on company data
Note: Accounts receivable figures are after deducting bad debt provisions.
Note: Figures may differ from company materials due to differences in rounding methods.

Recent updates

Highlights

On July 2, 2021, Shared Research updated the report following interviews with KFC Holdings Japan, Ltd.

On July 1, 2021, the company announced monthly sales data for June 2021; see the monthly trends section for details.

On June 1, 2021, the company announced monthly sales data for May 2021.

On May 12, 2021, the company announced earnings results for full-year FY03/21; see the results section for details.

On May 11, 2021, the company announced revisions to its full-year earnings forecast for FY03/21 and the booking of non-operating expenses and extraordinary losses.

Revised full-year FY03/21 earnings forecast

- Revenues: JPY89.7bn (previous forecast: JPY86.5bn)
- Operating profit: JPY6.4bn (JPY6.0bn)
- Recurring profit: JPY5.5bn (TBD)
- Net income attributable to owners of the parent: JPY2.8bn (TBD)
- EPS: JPY125.50 (TBD)

Reasons for revision

The company had previously left its forecast for recurring profit and net income attributable to owners of the parent as TBD due to difficulties in making reasonable earnings estimates with no sign of the COVID-19 pandemic coming to an end anytime soon. In the mainstay KFC business, the company worked on a number of initiatives, including expanding the number of stores that offered takeout, drive-through, and delivery services and store renovations aimed at enhancing its KFC brand power. As a result, in FY03/21, system sales, customer count, and customer spend at existing stores all increased YoY—by 13.6%, 4.1%, and 9.1%, respectively—and the company expects sales and operating profit to come in above its previous forecast. Note, however, that no change has been made to the year-end dividend forecast.

Booking of non-operating expenses (loss on investment in equity-method affiliates)

Earnings performance at equity-method affiliates Bamboo (Thailand) Holding Pte. Ltd. and BYO Co., Ltd. were affected by the pandemic, as evidenced by their sales declines among other factors. As a result, in FY03/21, the company expects to post an equity-method investment loss of JPY1.3bn (versus JPY1.6bn in FY03/20) as non-operating expenses.

Booking of extraordinary losses (impairment losses)

The company assessed earnings potential of stores whose profitability declined according to the Accounting Standards for Impairment of Fixed Assets, and as a result, decided to book an impairment loss of JPY300mn in FY03/21.

On May 7, 2021, the company announced monthly sales data for April 2021.

On April 14, 2021, the company announced changes in directors, including representative directors.

Details of change

Name	New position	Current position
Takayuki Hanji	Representative Director and President/CEO Representative Director and President of Kentucky Fried Chicken Japan, Ltd.	Director and Managing Executive Officer in charge of Management Strategies and SDGs Director and Managing Executive Officer in charge of Management Strategies of Kentucky Fried Chicken Japan
Masaki Kondo	Advisor	Representative Director and President/CEO Representative Director and President of Kentucky Fried Chicken Japan

Effective date of change

June 22, 2021

For previous releases and developments, please refer to the News and topics section.

Trends and outlook

Monthly trends

		FY03/11	FY03/12	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19	FY03/20	FY03/21
Average system sales per store		5.7%	-2.6%	-5.0%	-3.3%	3.5%	7.4%	-0.9%	-1.7%	5.2%	9.0%	11.8%
Sales at directly operated comparable stores		4.2%	-3.5%	-4.1%	-3.4%	2.9%	8.8%	-0.8%	-1.4%	3.7%	10.1%	13.6%
	Customer count	3.7%	-2.5%	-1.5%	-4.0%	0.2%	1.6%	-2.5%	-4.2%	2.3%	10.1%	4.1%
	Spend per customer	0.5%	-0.9%	-2.7%	0.6%	2.6%	7.1%	1.7%	3.0%	1.4%	-0.0%	9.1%

		Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	FY
FY03/16	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY**
Average monthly sales	All stores	6.77	8.26	8.05	8.60	9.77	7.51	7.74	8.61	13.29	9.07	7.36	8.85	8.66
	Directly operated stores	7.82	9.27	8.88	9.69	10.67	8.62	8.98	9.70	15.11	10.25	8.60	9.90	9.79
	Franchised stores	6.39	7.89	7.76	8.20	9.45	7.12	7.30	8.23	12.65	8.65	6.93	8.49	8.26
YoY	All stores	-7.8%	20.2%	9.5%	14.5%	16.9%	-10.1%	12.1%	7.9%	4.5%	7.3%	6.6%	10.6%	7.4%
	Directly operated comp. stores	-5.6%	18.4%	8.3%	13.3%	19.6%	-5.8%	13.5%	9.2%	6.7%	10.7%	6.7%	13.1%	8.8%
	Customer count	-9.4%	6.6%	-1.2%	3.9%	10.1%	-7.2%	6.6%	0.3%	0.2%	3.5%	2.9%	4.0%	1.6%
	Spend per customer	4.2%	11.1%	9.6%	9.1%	8.6%	1.5%	6.5%	8.8%	6.4%	7.0%	3.7%	8.8%	7.1%
FY03/17	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY**
Average monthly sales	All stores	7.14	7.53	7.21	9.34	8.66	8.21	8.34	8.58	13.57	8.84	6.89	8.21	8.55
	Directly operated stores	8.34	8.64	8.29	10.60	9.69	9.18	9.50	9.83	15.52	9.89	7.92	9.14	9.72
	Franchised stores	6.73	7.16	6.84	8.91	8.31	7.88	7.95	8.16	12.91	8.48	6.55	7.90	8.15
YoY	All stores	6.2%	-8.1%	-9.9%	9.1%	-10.7%	9.8%	8.2%	-0.2%	2.1%	-2.7%	-6.3%	-7.2%	-0.9%
	Directly operated comp. stores	6.4%	-7.0%	-7.2%	8.8%	-9.6%	6.0%	6.3%	1.4%	2.2%	-3.9%	-4.9%	-7.9%	-0.8%
	Customer count	3.1%	-5.2%	-3.9%	3.7%	-8.5%	0.6%	0.1%	-1.4%	-1.7%	-6.2%	-5.6%	-4.6%	-2.5%
	Spend per customer	3.3%	-1.9%	-3.4%	4.8%	-1.3%	5.4%	6.2%	2.8%	4.0%	2.5%	0.7%	-3.5%	1.7%
FY03/18	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY**
Average monthly sales	All stores	7.43	7.24	7.81	8.44	8.49	8.75	8.00	8.23	13.45	8.54	6.38	7.93	8.40
	Directly operated stores	8.54	8.35	8.85	9.70	9.42	9.84	9.19	9.45	15.33	9.66	7.57	9.08	9.61
	Franchised stores	7.05	6.87	7.47	8.03	8.17	8.38	7.57	7.79	12.76	8.14	5.97	7.55	7.99
YoY	All stores	4.3%	-3.7%	8.2%	-9.5%	-2.1%	6.5%	-4.0%	-4.0%	-0.9%	-3.4%	-7.5%	-3.4%	-1.7%
	Directly operated comp. stores	2.6%	-2.8%	6.9%	-8.3%	-2.8%	6.6%	-3.7%	-4.1%	-1.3%	-2.5%	-4.4%	-0.9%	-1.4%
	Customer count	0.7%	-4.5%	0.5%	-11.2%	-7.1%	3.2%	-6.2%	-4.4%	-4.7%	-4.6%	-6.2%	-4.9%	-4.2%
	Spend per customer	1.9%	1.8%	6.3%	3.3%	4.6%	3.3%	2.6%	0.3%	3.6%	2.2%	1.9%	4.1%	3.0%
FY03/19	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY**
Average monthly sales	All stores	7.03	6.94	7.58	9.28	9.86	9.14	8.38	8.09	14.28	9.04	7.58	9.04	8.84
	Directly operated stores	8.19	8.11	8.68	10.56	10.62	10.26	9.64	9.23	16.18	10.13	8.77	10.13	10.04
	Franchised stores	6.60	6.51	7.19	8.83	9.60	8.75	7.95	7.69	13.62	8.66	7.18	8.68	8.44
YoY	All stores	-6.4%	-5.1%	-3.5%	9.0%	15.4%	3.3%	4.8%	-1.5%	6.1%	5.9%	19.3%	14.5%	5.2%
	Directly operated comp. stores	-5.5%	-4.2%	-2.7%	7.6%	11.4%	3.6%	3.8%	-3.0%	4.7%	4.2%	14.7%	10.7%	3.7%
	Customer count	-8.5%	-8.1%	-5.5%	4.8%	9.0%	1.0%	5.1%	-2.0%	4.3%	6.4%	16.7%	6.6%	2.3%
	Spend per customer	3.4%	4.2%	2.9%	2.7%	2.1%	2.6%	-1.2%	-1.0%	0.4%	-2.1%	-1.7%	3.9%	1.4%
FY03/20	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY**
Avg. monthly sales	All stores (SR estimates)	8.09	8.09	9.40	9.58	10.51	9.54	9.08	9.46	14.82	9.68	8.84	9.76	9.75
YoY	All stores	13.6%	15.7%	22.8%	3.2%	5.9%	5.0%	5.3%	16.0%	3.4%	5.7%	15.5%	5.7%	9.0%
	Comparable stores	15.1%	16.5%	24.1%	3.6%	6.9%	4.8%	8.3%	17.6%	4.4%	8.5%	12.8%	8.2%	10.1%
	Customer count	16.2%	18.4%	24.4%	5.1%	6.1%	8.0%	7.1%	19.1%	7.1%	6.3%	6.4%	3.2%	10.1%
	Spend per customer	-1.0%	-1.6%	-0.2%	-1.4%	0.8%	-3.0%	1.1%	-1.2%	-2.5%	2.1%	6.0%	4.9%	-0.0%
FY03/21	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY***
Avg. monthly sales	All stores (SR estimates)	10.68	11.04	9.33	12.22	11.99	10.02	10.22	11.29	15.03	10.74	9.30	11.37	10.90
YoY	All stores	20.6%	22.2%	-2.0%	26.0%	12.9%	3.5%	13.2%	18.9%	1.8%	10.9%	5.1%	16.5%	11.8%
	Comparable stores	33.1%	37.6%	-1.0%	27.3%	13.6%	4.8%	12.2%	18.7%	0.8%	10.5%	7.6%	14.5%	13.6%
	Customer count	7.3%	6.5%	-7.3%	13.3%	6.1%	-2.2%	8.1%	5.3%	-2.3%	1.9%	0.2%	14.8%	4.1%
	Spend per customer	24.0%	29.2%	6.8%	12.3%	7.1%	7.1%	3.7%	12.7%	3.2%	8.5%	7.4%	-0.2%	9.1%
FY03/22	**(JPYmn)**	**Apr**	**May**	**Jun**	**Jul**	**Aug**	**Sep**	**Oct**	**Nov**	**Dec**	**Jan**	**Feb**	**Mar**	**FY***
Avg. monthly sales	All stores (SR estimates)	10.59	12.60	10.23										11.73
YoY	All stores	-0.9%	14.2%	9.6%										7.6%
	Comparable stores	-9.1%	4.4%	8.2%										1.0%
	Customer count	4.7%	16.8%	9.3%										10.2%
	Spend per customer	-13.3%	-10.6%	-1.1%										-8.4%

Source: Shared Research based on company data
Note: FY growth is on a year-to-date basis from April.
Note: Figures may differ from company materials due to differences in rounding methods.

Quarterly trends and results

Cumulative (JPYmn)	FY03/20 Q1	FY03/20 Q2	FY03/20 Q3	FY03/20 Q4	FY03/21 Q1	FY03/21 Q2	FY03/21 Q3	FY03/21 Q4	FY03/22 FY Est.
Revenues	17,717	38,052	60,895	79,634	19,762	43,287	68,480	89,652	95,688
YoY	14.9%	8.5%	7.3%	7.1%	11.5%	13.8%	12.5%	12.6%	6.7%
Gross profit	7,777	16,727	26,694	34,959	8,594	18,883	29,557	38,693	
YoY	18.6%	11.9%	9.9%	9.1%	10.5%	12.9%	10.7%	10.7%	
Gross profit margin	43.9%	44.0%	43.8%	43.9%	43.5%	43.6%	43.2%	43.2%	
SG&A expenses	6,826	14,260	22,439	30,173	7,305	15,485	23,811	32,344	
YoY	-3.5%	-1.4%	1.3%	1.1%	7.0%	8.6%	6.1%	7.2%	
SG&A ratio	38.5%	37.5%	36.8%	37.9%	37.0%	35.8%	34.8%	36.1%	
Operating profit	951	2,466	4,255	4,785	1,289	3,397	5,745	6,354	5,793
YoY	-	408.5%	97.8%	116.9%	35.5%	37.8%	35.0%	32.8%	-8.8%
Operating profit margin	5.4%	6.5%	7.0%	6.0%	6.5%	7.8%	8.4%	7.1%	6.1%
Recurring profit	1,039	2,766	4,551	3,252	545	2,883	4,691	5,498	5,012
YoY	-	405.7%	102.3%	9.3%	-47.5%	4.2%	3.1%	69.1%	-8.8%
Recurring profit margin	5.9%	7.3%	7.5%	4.1%	2.8%	6.7%	6.9%	6.1%	5.2%
Net income	701	1,896	2,988	1,533	82	1,602	2,454	2,805	2,831
YoY	-	416.6%	103.3%	-25.4%	-88.3%	-15.5%	-17.9%	83.0%	0.9%
Net margin	4.0%	5.0%	4.9%	1.9%	0.4%	3.7%	3.6%	3.1%	3.0%

Quarterly (JPYmn)	FY03/20 Q1	FY03/20 Q2	FY03/20 Q3	FY03/20 Q4	FY03/21 Q1	FY03/21 Q2	FY03/21 Q3	FY03/21 Q4
Revenues	17,717	20,335	22,843	18,739	19,762	23,525	25,193	21,172
YoY	14.9%	3.5%	5.4%	6.4%	11.5%	15.7%	10.3%	13.0%
Gross profit	7,777	8,950	9,967	8,265	8,594	10,289	10,674	9,136
YoY	18.6%	6.6%	6.7%	6.8%	10.5%	15.0%	7.1%	10.5%
Gross profit margin	43.9%	44.0%	43.6%	44.1%	43.5%	43.7%	42.4%	43.2%
SG&A expenses	6,826	7,434	8,179	7,734	7,305	8,180	8,326	8,533
YoY	-3.5%	0.6%	6.5%	0.7%	7.0%	10.0%	1.8%	10.3%
SG&A ratio	38.5%	36.6%	35.8%	41.3%	37.0%	34.8%	33.0%	40.3%
Operating profit	951	1,515	1,789	530	1,289	2,108	2,348	609
YoY	-	51.5%	7.4%	863.6%	35.5%	39.1%	31.2%	14.9%
Operating profit margin	5.4%	7.5%	7.8%	2.8%	6.5%	9.0%	9.3%	2.9%
Recurring profit	1,039	1,727	1,785	-1,299	545	2,338	1,808	807
YoY	-	73.7%	4.8%	-	-47.5%	35.4%	1.3%	-
Recurring profit margin	5.9%	8.5%	7.8%	-6.9%	2.8%	9.9%	7.2%	3.8%
Net income	701	1,195	1,092	-1,455	82	1,520	852	351
YoY	-	72.9%	-1.0%	-	-88.3%	27.2%	-22.0%	-
Net margin	4.0%	5.9%	4.8%	-7.8%	0.4%	6.5%	3.4%	1.7%

System sales Cumulative (JPYmn)	FY03/20 Q1	FY03/20 Q2	FY03/20 Q3	FY03/20 Q4	FY03/21 Q1	FY03/21 Q2	FY03/21 Q3	FY03/21 Q4	FY03/22 FY Est.
Total system sales	28,394	61,313	97,997	128,755	32,035	69,608	109,861	143,998	152,100
YoY	17.5%	10.3%	9.1%	9.0%	12.8%	13.5%	12.1%	11.8%	5.6%
Directly operated stores	8,140	17,427	27,815	36,433	8,699	19,117	30,147	39,400	41,900
YoY	10.0%	6.1%	5.3%	5.4%	6.9%	9.7%	8.4%	8.1%	6.3%
Franchised stores	20,253	43,886	70,182	92,321	23,335	50,491	79,714	104,598	110,200
YoY	20.8%	12.0%	10.7%	10.5%	15.2%	15.1%	13.6%	13.3%	5.4%

System sales Quarterly (JPYmn)	FY03/20 Q1	FY03/20 Q2	FY03/20 Q3	FY03/20 Q4	FY03/21 Q1	FY03/21 Q2	FY03/21 Q3	FY03/21 Q4
Total system sales	28,394	32,919	36,684	30,758	32,035	37,573	40,253	34,137
YoY	17.5%	4.7%	7.2%	8.6%	12.8%	14.1%	9.7%	11.0%
Directly operated stores	8,140	9,287	10,388	8,618	8,699	10,418	11,030	9,253
YoY	10.0%	3.0%	3.8%	5.9%	6.9%	12.2%	6.2%	7.4%
Franchised stores	20,253	23,633	26,296	22,139	23,335	27,156	29,223	24,884
YoY	20.8%	5.4%	8.7%	9.7%	15.2%	14.9%	11.1%	12.4%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.
Note: Revenues and operating profit tend to peak in Q3, which includes Christmas season.
Note: Starting in Q1 FY03/19, KFC transitioned to a single reporting segment of KFC business, and segment information disclosures have been omitted accordingly.

Full-year FY03/21 results (out May 12, 2021)

Results summary

- In FY03/21, the company reported revenues of JPY89.7bn (+12.6% YoY), operating profit of JPY6.4bn (+32.8% YoY), recurring profit of JPY5.5bn (+69.1% YoY), and net income of JPY2.8bn (+82.9% YoY). Net income was a record high since the company's listing. In FY03/21, system sales (total for directly operated and franchised stores) were JPY144.0bn (+11.8% YoY). Sales at existing stores were up 13.6% YoY, store traffic rising 4.1% YoY, and average spending per customer up 9.1% YoY. As of end-FY03/21, the company had 1,138 stores in operation. During FY03/21, it opened 22 stores (three directly operated stores and 19 franchised stores) and remodeled 233 stores (59 directly operated stores and 174 franchised stores). At end-FY03/21, the number of stores providing home delivery service grew to 376 (up 156 stores versus end-March 2020).
- At its mainstay KFC business, the company undertook various initiatives aimed at capturing more demand from the many families eating at home (rather than at restaurants) in the wake of the pandemic. In addition to its traditional strengths of takeout and drive-through options, the company worked to increase the number of stores offering home delivery service and also expanded its set meal menu. As part of its overall effort to protect customers and employees from infections, the company stepped up initiatives to provide contactless service. It installed equipment to facilitate the use of QR codes to pay for orders at all stores and, on an experimental basis, also installed store pickup lockers at some stores to allow delivery service staff and customers to pick up products ordered online without having to directly interface with store staff. On the minus side, the ongoing uncertainty as to when the COVID-19 pandemic will come to an end coupled with the harsh operating environment faced by equity-method affiliates, Bamboo (Thailand) Holding Pte. Ltd. and BYO Co., Ltd., left KFC Holdings with JPY1.3bn in losses on investments in equity-method affiliates (recorded under non-operating expenses). The company also booked extraordinary losses of JPY300mn to reflect asset impairment charges taken against stores whose profitability appeared to unlikely to recover to previous levels. For FY03/21, the company will pay dividends of JPY60 per share (including a JPY10 per share dividend to commemorate its 50th anniversary), representing a dividend payout ratio of 47.8%.

Q4 FY3/21 results (January–March 2021)

In Q4 FY03/21, the company reported revenues of JPY21.2bn (+13.0% YoY), operating profit of JPY609mn (+14.9% YoY), and net income of JPY351mn (JPY1.5bn net loss in Q4 FY03/20). Market conditions remain severe in the food-service industry as a result of a second state of emergency declared in January 2021 and associated order to reduce opening hours. Amid the trend of more families eating at home, the company worked to capture demand by offering takeout, drive-through, and delivery services, and stepped up sales of new products and set menu meals. The number of stores at end-Q4 was 1,138. The company opened five new stores in Q4 (two directly operated and three franchised stores) and remodeled 71 stores (20 directly operated and 51 franchised stores).

In Q4 FY03/21, system sales (total for directly operated and franchised stores) were JPY34.1bn (+11.0% YoY). System sales at existing stores were up 10.5% YoY in January, up 7.6% YoY in February, and up 14.5% YoY in March. With monthly sales growth trending above 8% YoY in Q4 FY03/20, the company posted higher YoY system sales in Q4 FY03/21 as well. The company ran promotional campaigns for new products Ginger Hot Chicken in January, Ii Tokodori (set menu) in February, and Share Box in March 2021. Menus representing good value and new products that stimulate regular consumption proved successful, helped by more families eating at home.

Gross profit was JPY9.1bn (up 10.6% from JPY8.3bn in Q4 FY03/20), SG&A expenses were JPY8.5bn (up 10.3% YoY from JPY7.7bn), operating profit was JPY609mn (up 14.9% from JPY530mn), and the OPM was 2.9% (little changed from 2.8%). The main SG&A expense increases were in personnel and remodeling expenses. Personnel expenses were up, because the company paid bonuses to employees (including temporary employees) who continued to work amid the pandemic. The company also exceeded its initial budget for remodeling directly operated stores, because it decided to do more remodeling than planned in response to sales through Q3 trending ahead YoY. Commissions paid to food delivery services such as Uber Eats also increased, because more KFC stores began offering home delivery.

The company has two equity-method affiliates, Bamboo (Thailand) Holding Pte. Ltd. and BYO Co., Ltd. Bamboo (Thailand) Holding, which runs franchised KFC stores in Thailand, posted sales and profit declines amid the COVID-19 pandemic and political unrest. BYO runs Japanese restaurants and fast-food stores as well as Japanese-style gastropub En Washoku Sake, with roughly 50% of stores in buildings near stations in Tokyo. Earnings have deteriorated under the state of emergency, because stores cannot serve alcohol and had to shorten opening hours. Consequently, in Q4 KFC Holdings recorded JPY144mn in losses on investments in equity-method affiliates (recorded under non-operating expenses; JPY1.3bn over the full year). The company also booked extraordinary losses of JPY100mn in Q4 (JPY300mn over the full year) to reflect asset impairment charges taken against KFC stores in Greater Tokyo whose sales continue to decline because of people staying at home and teleworking. Accordingly, net income was JPY351mn in Q4 (net loss of JPY1.5bn in Q4 FY03/20).

Full-year FY3/21 results

In FY03/21, the company reported revenues of JPY89.7bn (+12.6% YoY), operating profit of JPY6.4bn (+32.8% YoY), recurring profit of JPY5.5bn (+69.1% YoY), and net income of JPY2.8bn (+82.9% YoY).

Revenues

FY03/21 system sales (total for directly operated and franchised stores) were a record JPY144.0bn (+11.8% YoY) and monthly system sales at existing stores were JPY11.1mn (+13.6% YoY), also a record high. The number of stores at end-FY03/21 was 1,138 (+5 YoY), of which 233 stores were remodeled (+21 YoY), and 376 offered home delivery services (+156 YoY). System sales reached a record high despite some stores being forced to close because of the pandemic and the average number of stores in operation falling from a year earlier to 1,040.

In FY03/21, customer count at existing stores grew 4.1% YoY and spending per customer was up 9.1% YoY. Customer traffic increased at KFC stores, which attracted customers in all age groups as a result of developing a new children’s menu and expanding its lunch menu to attract younger customers under age 30. Spending per customer also went up, because sales of large volume takeout items increased, likely for family dinners at home.

Most restaurants whose main business is eating in were unable to open in April and May 2020 because of the pandemic. The company was able to attract demand, because it has always been known for its takeout service (takeout accounts for around 70% of total sales) and offers a drive-through option with minimal contact. Since June 2020, however, many restaurants reopened with restrictions, gradually increasing opportunities for consumers to dine out while taking steps to prevent infection. The company thinks that comparable store sales trended higher YoY throughout FY03/21 (except in June 2020) because of its keenly priced meals that encourage regular purchases and a product development and menu strategy that delivers fun and surprise.

Gross profit

Gross profit at 43.2% in FY03/21 was little changed from 43.9% in FY03/20. The company has continued efforts to make sales forecast more precise and to reduce losses from food disposal, which contributed toward keeping GPM at a high level. GPM has been stable at 43% or higher every fiscal year.

SG&A expenses

SG&A expenses were JPY32.3bn in FY03/21 (+7.2% YoY) with an SG&A expense ratio of 36.1% (-1.8pp YoY). The SG&A expense ratio fell as a result of higher revenues. The company continues to optimize headquarters expenses.

Commissions paid to food delivery services such as Uber Eats also increased, because more KFC stores began offering home delivery. At end-March 2021, home delivery services were available at 376 out of 1,138 stores (an increase of 156 stores from end-March 2020) to respond to the growing demand for delivery services. Although the company also has its own delivery system, most deliveries are via food delivery services. The company remodeled 233 stores (20.5% of the total), in part to respond to home delivery demand. Modifications include split counters that separate takeout and delivery traffic from eat-in traffic and a dedicated entrance and exist for food delivery service staff. The company is also trialing store pickup lockers where delivery service staff and customers can pick up products ordered online on a non-contact basis.

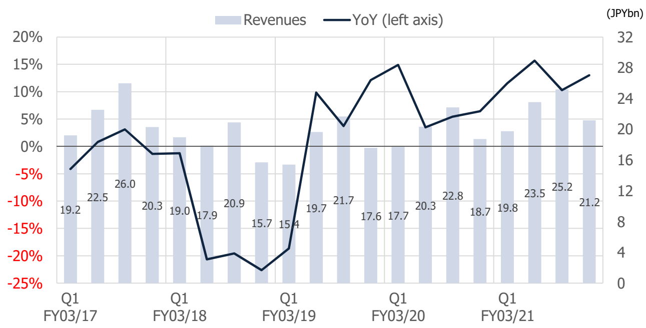
Equity-method affiliates

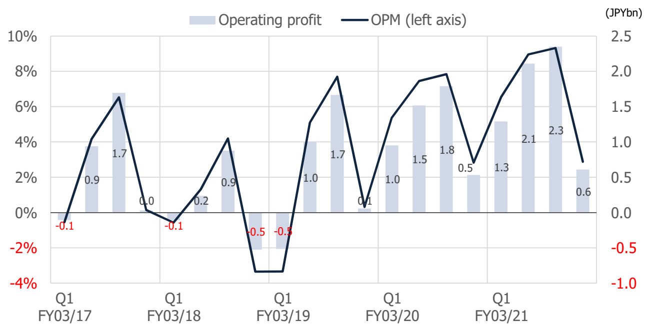
Market conditions remain severe for the company's two equity-method affiliates, Bamboo (Thailand) Holding Pte. Ltd. and BYO Co., Ltd., resulting in KFC Holdings recording JPY1.3bn in losses on investments in equity-method affiliates (recorded under non-operating expenses) in FY03/21.

Bamboo (Thailand) Holding recorded JPY530mn in losses on investments in equity-method affiliates (under non-operating expenses). Earnings deteriorated amid the COVID-19 pandemic and political unrest. Thailand is a major tourism center whose tourism revenue accounts for around 20% of GDP. Tourism revenue fell 80% in 2020. We assume that franchised KFC stores run by Bamboo (Thailand) Holding was negatively impacted by fewer tourists visiting stores and loss of revenue source of customers employed in tourism. Although Bamboo (Thailand) Holding is trying to expand earnings opportunities by increasing the number of stores that offer a delivery service, the company thinks earnings recovery at the affiliate will take some time.

BYO recorded JPY744mn in losses on investments in equity-method affiliates (under non-operating expenses). It runs Japanese restaurants and fast-food stores as well as Japanese-style gastropub En Washoku Sake, with roughly 50% of stores in buildings near stations in Tokyo. The market environment remains challenging under the state of emergency, because stores cannot serve alcohol and have to shorten opening hours.

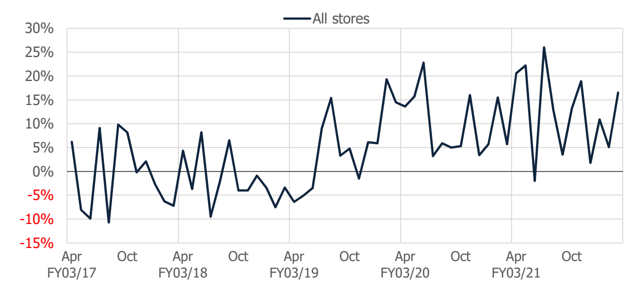
Quarterly performance

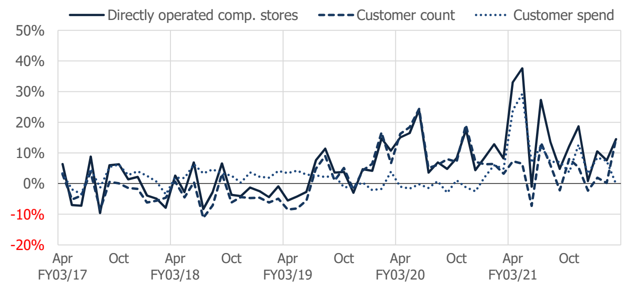




Source: Shared Research based on company data
Note: Revenues and operating profit tend to peak in Q3, which includes Christmas season.

KFC business monthly sales





Source: Shared Research based on company data

For details on previous results, please refer to the Historical performance section.

Company forecast for FY03/22

	FY03/20			FY03/21			FY03/22
(JPYmn)	1H	2H	FY	1H	2H	FY	FY Est.
Total revenues	**38,052**	**41,582**	**79,634**	**43,287**	**46,365**	**89,652**	**95,688**
YoY	8.5%	5.9%	7.1%	13.8%	11.5%	12.6%	6.7%
Gross profit	16,727	18,232	34,959	18,883	18,883	38,698	
YoY	11.9%	6.7%	9.1%	12.9%	3.6%	10.7%	
Gross profit margin	44.0%	43.8%	43.9%	43.6%	40.7%	43.2%	
SG&A expenses	14,260	15,913	30,173	15,485	16,859	32,344	
YoY	-1.4%	3.6%	1.1%	8.6%	5.9%	7.2%	
SG&A ratio	37.5%	38.3%	37.9%	35.8%	36.4%	36.1%	
Operating profit	**2,466**	**2,319**	**4,785**	**3,397**	**2,957**	**6,354**	**5,793**
YoY	408.5%	34.7%	116.9%	37.8%	27.5%	32.8%	-8.8%
Operating profit margin	6.5%	5.6%	6.0%	7.8%	6.4%	7.1%	6.1%
Recurring profit	**2,766**	**486**	**3,252**	**2,883**	**2,615**	**5,498**	**5,012**
YoY	405.7%	-80.0%	9.3%	4.2%	438.1%	69.1%	-8.8%
Recurring profit margin	7.3%	1.2%	4.1%	6.7%	5.6%	6.1%	5.2%
Net income attributable to owners of the parent	**1,896**	**-363**	**1,533**	**1,602**	**1,203**	**2,805**	**2,831**
YoY	416.6%	-	-25.4%	-15.5%	-	83.0%	0.9%
Net margin	5.0%	-0.9%	1.9%	3.7%	2.6%	3.1%	3.0%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

System sales	FY03/20			FY03/21			FY03/22
(JPYmn)	1H	2H	FY	1H	2H	FY	FY
Total system sales	**61,313**	**67,442**	**128,755**	**69,608**	**74,390**	**143,998**	**152,100**
YoY	10.3%	7.8%	9.0%	13.5%	10.3%	11.8%	5.6%
Directly operated stores	17,427	19,006	36,433	19,117	20,283	39,400	41,900
YoY	6.1%	4.8%	5.4%	9.7%	6.7%	8.1%	6.3%
% of total	28.4%	28.2%	28.3%	27.5%	27.3%	27.4%	27.5%
Franchised stores	43,886	48,435	92,321	50,491	54,107	104,598	110,200
YoY	12.0%	9.1%	10.5%	15.1%	11.7%	13.3%	5.4%
% of total	71.6%	71.8%	71.7%	72.5%	72.7%	72.6%	72.5%

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

For FY03/22, the company projects revenues of JPY95.7bn (+6.7% YoY), operating profit of JPY5.8bn (-8.8% YoY), recurring profit of JPY5.0bn (-8.8% YoY), and net income of JPY2.8bn (+0.9% YoY). The company aims to boost system sales at existing stores with the help of 50 new store openings, more store remodelings, and increases in the number of stores offering home delivery service. The forecast assumes total system sales of JPY152.1bn (+5.6% YoY) with the average existing store generating monthly sales of JPY11.3mn (up JPY210,000 YoY), a year-end store count of 1,161 (+23 YoY), the remodeling of 220 stores (-13 YoY), and the addition of delivery service to another 79 stores to bring the total number of stores offering home delivery service to 455.

In January 2021, the Japanese government issued a second state of emergency declaration that covered the Tokyo metropolitan area and the Kansai region. The declaration was lifted in March, but the government issued a third emergency declaration in April, covering Tokyo, Osaka, and several other prefectures. In this relation, restrictions are still keeping people at home and forcing some of the company's stores to keep shorten operating hours. The company said its estimates for FY03/22 assume the COVID-19 pandemic and related restrictions will affect earnings in FY03/22 and beyond. For 03/22, the company plans to pay dividends of JPY50 per share.

Revenues

In FY03/22, the company forecasts revenues of JPY95.7bn (+6.7% YoY) and system sales of JPY152.1bn (+5.6% YoY), assuming an increased store count and higher system sales at existing stores. The company plans to open 50 new stores (net increase of 23 after closing 27 stores) versus 1,138 at end-FY03/21.

KFC Holdings forecasts an increase in average monthly sales at existing stores from JPY11.1mn in FY03/21 to JPY11.3mn in FY03/22 by expanding menus and remodeling. System sales at existing stores fell 9.1% YoY in April 2021 (customer traffic up 4.7% and spending per customer down 13.3% YoY). The company commented that this was likely a reaction to the 33.1% surge in sales at existing stores in April 2020 and in line with its assumptions. In FY03/22, it will continue to offer menus that encourage customers to purchase regularly, such as attracting lunchtime demand, to increase customer traffic YoY. To this end, the company plans to step up sales of items other than fried chicken (including sandwiches on sale for a limited period) as part of its menu strategy, as well as run a campaign to promote further efforts to improve the taste of the mainstay original-recipe chicken. Remodeling of 220 stores is planned, with an increase in the number of stores offering home delivery to 455 (+79 YoY).

The company plans to open 50 new stores in FY03/22, more than double the 22 new stores opened in FY03/21. Over the past 15 years, the company closed more unprofitable stores than open new ones. The store count peaked at 1,180 at end-March 2013 and gradually declined to 1,138 (down 42 stores) at end-March 2021. The company has been unable to increase the store count, because most of its store are in downtown areas where potential for new stores is limited. However, it plans to open stores in areas that it had not considered in the past (including suburban drive-through stores), because working from home has become the norm amid the pandemic and demand has grown in residential areas. The company is also seeking opportunities to open new stores in premises that are already fitted out, because many restaurants are closing in downtown areas. It plans an aggressive new store opening program by developing new formats and modify layouts such as small properties for takeout-only stores and smaller stores offering a drive-through option.

Operating profit

KFC Holdings forecasts operating profit of JPY5.8bn (-8.8% YoY) in FY03/22 despite the outlook for 5.6% YoY revenue growth. This is because the company expects higher expenses to streamline operations and plans to invest for growth, such as opening and remodeling stores, promoting digitalization, system development for stores, and promoting use of the cloud. An example is investment in improving the convenience of online orders.

In FY03/21, stores were mainly remodeled to handle takeout and delivery orders. The company expects demand for takeout and delivery services to persist even if the pandemic ends, and will thus continue its remodeling program. At the same time, it expects an increase in customers eating in after the pandemic is over.

Net income

The net income forecast is little changed from FY03/21 at JPY2.8bn (+0.9% YoY), because the company expects lingering uncertainty of outlook regarding the impact of the pandemic and foresees an ongoing negative impact on its two equity-method affiliates for some time after FY03/22.

Historical results vs. estimates

Results vs. Initial Est. (JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Total revenues (Initial Est.)	90,000	92,000	89,100	85,000	90,000	92,000	77,400	73,000	74,400	85,000
Total revenues (Results)	88,124	85,864	83,436	84,605	88,180	88,032	73,457	74,344	79,634	9,468
Results vs. Initial Est.	**-2.1%**	**-6.7%**	**-6.4%**	**-0.5%**	**-2.0%**	**-4.3%**	**-5.1%**	**1.8%**	**7.0%**	**-88.9%**
Operating profit (Initial Est.)	2,600	2,800	2,410	1,600	1,500	2,500	1,200	1,000	1,500	5,000
Operating profit (Results)	2,390	2,395	1,822	670	2,011	2,558	477	2,206	4,785	6,354
Results vs. Initial Est.	**-8.1%**	**-14.5%**	**-24.4%**	**-58.1%**	**34.1%**	**2.3%**	**-60.3%**	**120.6%**	**219.0%**	**27.1%**
Recurring profit (Initial Est.)	2,700	2,900	2,550	1,700	1,600	2,400	1,000	1,100	1,400	1,400
Recurring profit (Results)	2,469	2,506	1,856	667	1,866	2,425	627	2,975	3,252	5,498
Results vs. Initial Est.	**-8.6%**	**-13.6%**	**-27.2%**	**-60.8%**	**16.6%**	**1.0%**	**-37.3%**	**170.5%**	**132.3%**	**292.7%**
Net income attributable to owners of the parent (Initial Est.)	1,400	1,600	1,350	700	600	1,300	1,500	700	1,000	1,000
Net income attributable to owners of the parent (Results)	1,102	1,203	441	-524	730	1,365	578	2,055	1,533	2,805
Results vs. Initial Est.	**-21.3%**	**-24.8%**	**-67.3%**	**-**	**21.7%**	**5.0%**	**-61.5%**	**193.6%**	**53.3%**	**180.5%**

Source: Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Medium-term management plan

Medium-term management plan

With the company having reached its 50-year anniversary in 2020, KFC Holdings announced its new medium-term management plan on April 14, 2021. Dubbed "Second Founding: Setting the Stage for Continued Growth Over the Next 50 Years" and running from FY03/22 to FY03/24, the new plan is aimed at pursing further growth as a group providing comprehensive food service with KFC at its core business. Under its guiding principle of "Creating delicious meals and happiness," the company is also looking to maintain the flexibility and capabilities to response quickly to changes in the operating environment. The core strategies under the new medium-term plan call for 1) promoting further growth at its KFC business, 2) further expanding the group's business portfolio and boosting the enterprise value of its capital and business alliance partners, and 3) building out its business foundation to support growth. The company implemented a range of menu strategies under the previous medium-term plan (FY03/19–FY03/21) targeting recovery and growth of customer traffic. They had the effect of increasing revenues and operating profit as a result of increased customer count. The new medium-term plan targets further increase in new store openings and system sales at existing stores while expanding investment to augment its foundation for business growth.

For FY03/24, the company targets revenues of JPY1.1bn (+19.5% versus FY03/21), operating profit of JPY6.3bn (flat), and net income of JPY3.5bn (+25%). The company expects growth in revenues as a result of higher system sales at existing KFC stores and opening new stores. At the same time, it anticipates flat operating profit because of increased expenses for store opening and remodeling and system development. The company projects net income to grow, factoring in earnings improvement at equity-method affiliates.

Promote further growth of KFC business

KFC Holdings targets system sales of JPY170.0bn through growth of existing store sales and opening 129 new stores (net increase of 70 stores). The company aims to grow revenues by leveraging the KFC brand in Japan, established over 50 years, and further refining it. The following three measures are designed to increase revenues.

Making KFC an everyday brand

A challenge for the company is that many consumers associate KFC with Christmas and special occasions, not with casual, everyday meals. The company aims to encourage customers to purchase more regularly by providing products and services that fit the needs of diverse settings and times of day. Initiatives include making its products more appealing (i.e., further improving the tastiness of original-recipe chicken and other mainstay items), expanding lunchtime menus, and increasing the number of stores that offer a home delivery service.

More local and convenient

KFC Holdings is ramping up its store opening and remodeling program. Under the new medium-term plan, the company targets 129 new stores in three years (net increase of 70 stores) and remodeling around 200 stores per year. It plans to increase the number of stores offering a home delivery service from 376 at end-FY03/21 to 553 at end-FY03/24. The plan's targets for FY03/22, the first year of the medium-term plan, are opening 50 new stores (and closing 27 stores for a net increase of 23), remodeling 220 stores, and increasing the number of stores offering a home delivery service to 455.

The company has been unable to increase the store count, because most of its store are in downtown areas where potential for opening new stores is limited. However, it plans to open stores in areas that it had not considered in the past (including suburban drive-through stores), because working from home has become the norm amid the COVID-19 pandemic and demand has grown in residential areas. The company also plans to open new format stores in downtown areas such as takeout-only stores, actively seeking opportunities to take over stores that are already fitted out, because many restaurants are closing because of the pandemic.

Remodeling features split counters that separate takeout and delivery traffic from eat-in traffic and a dedicated entrance and exist for food delivery staff. The company is also trialing store pickup lockers where food delivery staff and customers can pick up products ordered online on a non-contact basis. Other improvements to prevent the spread of COVID-19 include units that display ready-to-collect order numbers and self-checkouts in addition to strict infection control procedures. Through these remodelings, the company aims to create a pleasant interior.

Safe, secure, and tasty food

KFC Holdings is renewing its commitment to the fundamentals of food service abbreviated as “QSC x H,” representing quality, service, and cleanliness combined with hospitality. The company breeds chickens at 200 KFC-registered farms in Japan and processes the poultry at approved “KFC cut chicken production facilities” that meet the company’s safety and quality control standards. Its integrated production system from chicken farming to delivery and instore cooking processes is safe and secure, with hygiene management in place throughout. The company will further strengthen this system.

Expand group business portfolio and enhance corporate value of capital and business alliance partners

Market condition remain severe for equity-method affiliates, Bamboo (Thailand) Holding Pte. Ltd. and BYO Co., Ltd., because of the COVID-19 pandemic.

Turning around earnings performance of these two affiliates is a management priority for KFC Holdings in FY03/22, thus the company is not planning new acquisitions. However, the company may invest to move into a food-service business other than fast food during the new medium-term plan period after reviewing the allocation of management resources. The company commented that if it were to enter into a capital or business alliance, it would be in a food-related business where it can harness its strengths.

Expand foundations for business growth

KFC Holdings is strengthening its digital and IT strategies to improve customer convenience and comfort, promote work style reforms for employees, and offer a pleasant workplace environment. It revamped the Kentucky official app in February 2021, adding features such as member registration and loyalty points, as well as coupon delivery. The company is focusing on system improvements and data marketing to make effective use of customer data. It will invest in projects such as developing a new POS system and promoting digitalization, in the order of priority.

Business

Overview

Under a franchise agreement with Yum! Brands, Inc., KFC Holdings Japan operates KFC restaurants in Japan. It also acts as a franchisor for the KFC brand and earns royalties and other revenues.

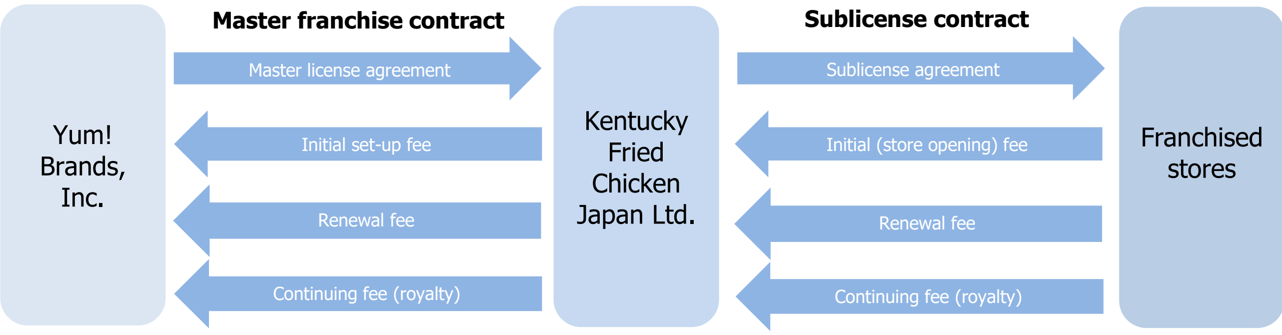
> Yum! Brands, Inc.
> Yum! Brands, Inc. is a major global fast food chain operator, with the restaurant brands including KFC, Pizza Hut, and Taco Bell. The company was established via a spinoff from major soft drink manufacturer PepsiCo in 1997 (at that time the company name was Tricon Global Restaurants, Inc.). The KFC brand was acquired by PepsiCo Inc. in 1986 after a series of M&A deals following the sale of franchise rights by its founder, Colonel Harland Sanders in 1964.

Master franchises and sublicenses

KFC Holdings Japan has both master franchise and sublicense agreements. It is a master franchisee of KFC Restaurants Asia Pte Ltd. (member of the Yum Brands, Inc. group). The company pays initial setup fees to the Yum! Brands group for opening restaurants, as well as renewal fees and ongoing royalties.

In turn, KFC Holdings Japan provides sublicensing rights to franchisees in Japan and receives initial setup payments when restaurants are opened, as well as renewal payments and ongoing royalties. (For details refer to discussion of business models for KFC).

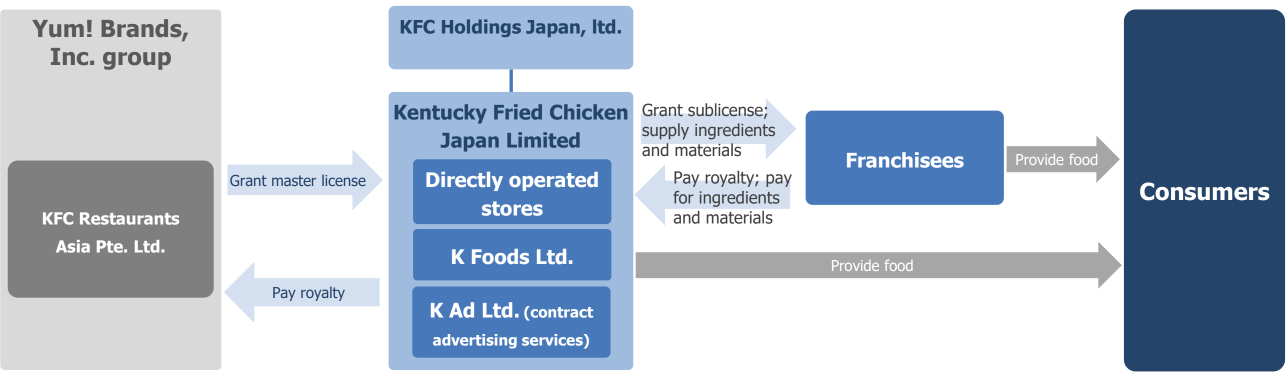
Two layers of franchise agreements



Source: Shared Research based on company data
Note: FY03/10 was a 16-month period due to balance date change. Data not disclosed for FY03/15 onward.

In April 2014, KFC Holdings Japan moved to a holding company structure to maximize the corporate value of the group. Under the management of KFC Holdings Japan, restaurants are operated by Kentucky Fried Chicken Japan, Ltd. Advertising for each company is handled by K Ad, Ltd. K Foods, Ltd. is a wholly owned subsidiary of Kentucky Fried Chicken Japan, Ltd. and operates stores in Osaka, Shikoku, and Kanto areas.

Business organization

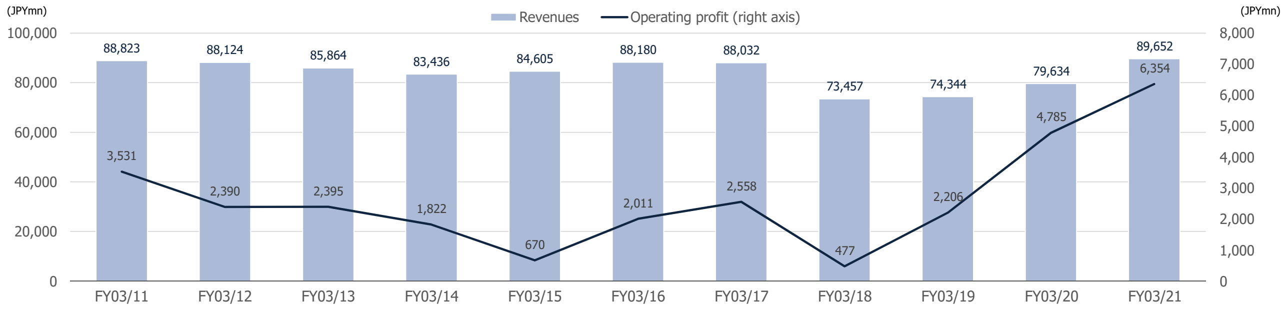


Source: Shared Research based on company data

KFC Japan's operating profit declined from a peak of JPY3.5bn in FY03/11 to JPY670mn in FY03/15 due to increases in ingredient and personnel costs, but recovered to JPY2.6bn (+27.2% YoY) in FY03/17 thanks to cost cutting in the Pizza Hut business. In

FY03/18, operating profit decreased to JPY477mn as a result of the sale of the Pizza Hut business, but in FY03/20 it had recovered to JPY4.8bn and to JPY6.4bn in FY03/21 thanks to measures to promote everyday patronage. The company was able to generate steady operating profit and avoid losses despite tough operating conditions. This is partly due to its consistent efforts to improve system sales and customer traffic, and optimize companywide expenses.

Consolidated results



Source: Shared Research based on company data
Note: Results up to June 2017 include the Pizza Hut business.

KFC business

Business model

Overview

Under a holding company structure, Kentucky Fried Chicken Japan runs the KFC business. As of end-March 2021, it had a total of 1,138 restaurants (299 directly operated restaurants primarily in Greater Tokyo, and 839 restaurants run by franchisees, mainly in regional areas).

Breakdown of system sales

Out of total system sales (total for directly operated and franchised restaurants) of JPY144.0bn in FY03/21, JPY39.4bn came from directly operated stores and JPY104.6bn came from franchised stores. Sales at directly operated stores accounted for 27.4% of total system sales, while the remaining 72.6% came from franchised stores.

Franchise agreement

The master license agreement between the company and KFC Restaurants Asia Pte. Ltd. covers the following:

- Use trademarks relating to the KFC business in restaurants.
- Selling products using methods and trade secrets disclosed by the licensor that meet the licensor's quality standards.
- The above rights and conditions may be sublicensed to restaurants.

Compensation under the master franchise and sublicense agreements with franchisees is as shown below.

Compensation under franchise agreements in KFC business

	Master franchise agreement	Sublicense agreement
Initial (store opening) fee	JPY1.5mn/store*	JPY2.5mn/store*
Renewal fee July 11, 2004–November 30, 2014 December 1, 2014–November 30, 2019 December 1, 2019–November 30, 2024	Per store renewed JPY250,000 JPY360,000 JPY180,000	Per store renewed No charge JPY180,000 JPY180,000
Continuing fee July 11, 2004–November 30, 2005 December 1, 2005–November 30, 2011 December 1, 2011–November 30, 2014 December 1, 2014–November 30, 2019 December 1, 2019–November 30, 2024	Share of total sales 2.3% +0.1pp p.a. from Dec. 1, 2005 3.0% 5.0% 6.0%	Share of total sales 4.0% 4.0% 4.0% 5.0% 6.0%
Store certification period July 11, 2004–November 30, 2014 December 1, 2014–November 30, 2019 December 1, 2019–November 30, 2024	For directly operated stores Seven-year contract period Ten-year contract period Five-year contract period	For franchised stores Two-year contract period Five-year contract period Five-year contract period
Contributions for advertising	Contributions of a minimum of 4% of total sales to the KFC Advertising Association, an organization formed by the company and franchisees, (outsourced to 100% subsidiary K Ad) to create nationwide ad campaigns	

Source: Shared Research based on company data
Note: Adjusted for inflation starting from December 1, 2014
Note: Continuing fee under sublicense agreements (% share of total sales) includes portion retained by KFC Japan.

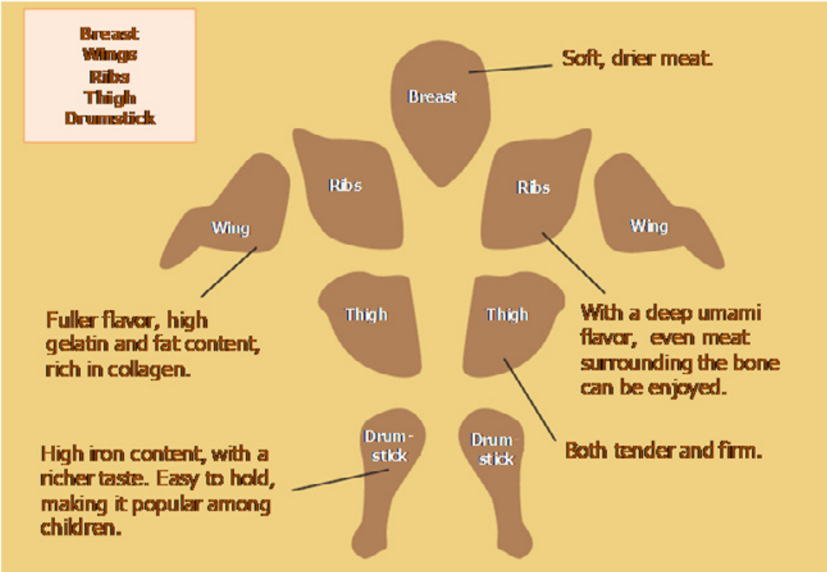
The approval of the master franchisor, Yum! Brands, is required for all aspects of franchise agreements including products, ingredients, restaurants, and equipment.

Mainstay product: "original-recipe chicken"

KFC's mainstay "original-recipe chicken" is made from chicken raised in Japan on feed mixed with herbs that mask certain chicken odors, and accounts for roughly 40% of KFC's system sales.

Once a chick has hatched and has undergone a health check, the chicken is raised at one of 200 KFC-registered farms nationwide, which all meet strict standards for equipment, animal breeding methods, feed, and health management. The chickens are slaughtered and cut into nine pieces using KFC's original nine-cut method when they are about 38 days old. They are slaughtered in the morning and shipped to individual stores in the shortest time possible.

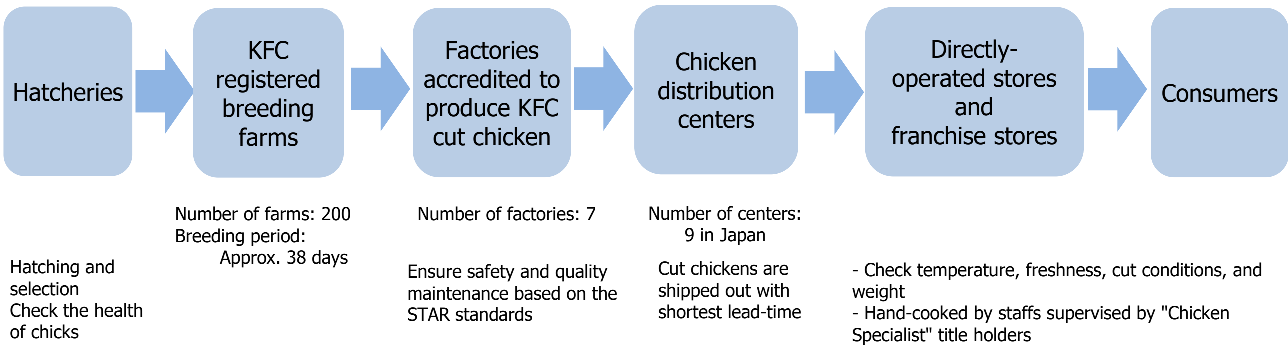
KFC's original nine-cut chicken cutting method



Source: Shared Research based on company data

Employees conduct further quality checks of the poultry in the restaurants, assessing temperature, freshness, and whether any feathers remain, preparing only the chickens that meet stringent standards. "Original-recipe chicken" is prepared by staff accredited as "chicken specialists" under the company's certification system.

Distribution chart for herb-fed chickens used for "original-recipe chicken"



Source: Shared Research based on company data

> Supplier Tracking Assessment and Recognition (STAR) standards
> Global food safety and quality management standards for KFC set by the US headquarters of Yum! Brands, Inc. In Japan, factories accredited to produce KFC cut chicken must reach a certain level of STAR standards to fulfill the company's safety and quality maintenance requirements. The standards cover a wide scope, including facility equipment, machinery, and surrounding environment, conditions, organization, and management structure.

Customer demographic

Some 70% of KFC's customers are women in their 30s through 50s. Around 70% of customers order takeout such as "original-recipe chicken" meals, and the remaining 30% dine in, ordering sets such as chicken fillet sandwiches or chicken cutlet sandwiches that come with a soft drink. Customers in their 40s and 50s are familiar with the taste of KFC since their younger days, and tend to be big KFC fans. Since 2013, when convenience stores entered the fried chicken market, it appears that customers in their 20s, who are more accustomed to convenience stores, have become less frequent at KFC.

Spending per customer

At directly operated restaurants in Greater Tokyo, average spending per customer is JPY900–1,000, whereas in regional areas it is JPY1,200–1,300. Average spending per customer is lower in the Tokyo area due to the trend toward smaller, nuclear families. The all-store average figure is around JPY1,000. Around lunchtime, the average customer spends less than JPY900 due to value sets of JPY500–700 featuring items such as chicken fillet sandwiches and chicken cutlet sandwiches. At dinnertime, many people purchase "packs" and other large volume packages of "original-recipe chicken" to take home to their families for dinner, so spending per customer average JPY1,200–1,500. Although for most of the year spending per customer averages JPY1,000, Q3 (October–December) is the peak season with spending per customer reaching nearly JPY1,200, as it includes Christmas (when it has become common in Japan to eat fried chicken).

Restaurant openings and closures

Directly operated restaurants

Store openings are primarily in the Kanto and Kansai regions, and consider the scope for new openings and trends in commercial areas. Locations also take into account profit and loss simulations based on restaurant format, i.e., stores in busy shopping areas, drive-through stores, or shopping center stores.

Restaurants with negative operating cash flow are designated as closure candidates. For restaurants where performance does not recover, the closure method and timing are based on overall expenses, such as the costs of restoring premises to their original condition.

Franchise restaurants

The company makes recommendations regarding franchise restaurant openings based on the scope for new openings and trends in commercial areas. The final decision is made by individual franchisees, who receive support from KFC Holdings Japan.

Regarding closures, supervisors who are part of the company's sales division provide management advice for underperforming restaurants, with the final decision left up to the franchisee.

Distinctive elements of KFC business

Brand power underpinned by tasty food prepared on-site

KFC is a global brand, with a presence in more than 135 countries worldwide and roughly 23,000 restaurants as of June 2021. The KFC brand is sustained by its mainstay product, "original-recipe chicken," developed by Colonel Harland Sanders in 1939. It is prepared using 11 secret herbs and spices, and fried with pure vegetable oil in a pressure cooker.

The 11 secret herbs and spices are shrouded in mystery and attract much attention. The *Chicago Tribune* in August 2016 published an article stating that a memo with the secret recipe had been discovered. According to the company, even internally information on the 11 herbs and spices is closely guarded so that no individual knows the secret combination.

First mover advantage gives KFC high market share

KFC was established in Japan in 1970 and opened its first location in Nagoya, one year before McDonald's Corporation established McDonald's Japan. Subsequently, the KFC brand spread, along with statues of Colonel Sanders. In much of the world the custom is to eat turkey at Christmas, but in Japan chicken is the typical Christmas dinner. The company's successful marketing has established a culture of eating fried chicken at Christmas. KFC Holdings Japan is the only company that has succeeded in establishing a fast-food chain specialized in fried chicken.

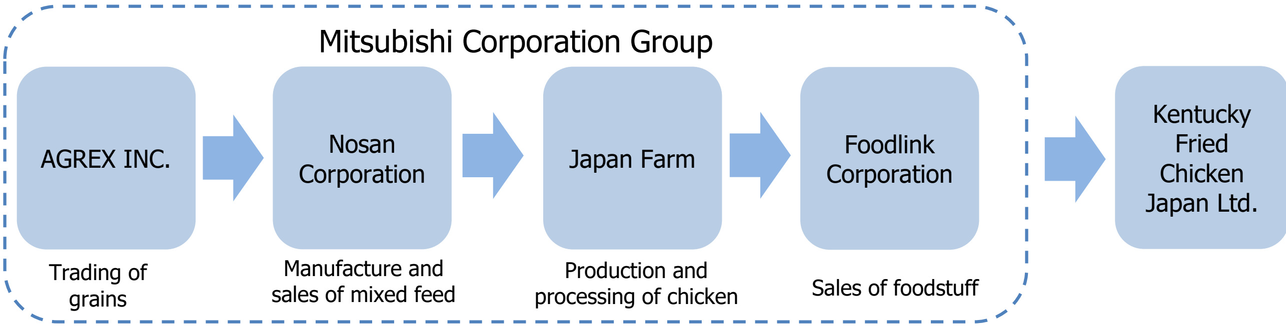
Steady, large-volume supplies of chicken raised in Japan

All of the company's chicken is raised in Japan. At about 38 days old, these young birds are juicy, tender, and indispensable for making KFC's original-recipe chicken. In contrast, convenience stores primarily use frozen imported chicken over 50 days old for their fried chicken.

The company is able to obtain a steady, large (more than 200mn pieces per annum) supply of chicken by virtue of the feed and livestock value chain created by Mitsubishi Corporation, its major shareholder. Mitsubishi was the first company in Japan to introduce the end-to-end chicken farming system prevalent in the US that encompasses production, treatment, processing, and sales. Mitsubishi also built a value chain for chicken feed from procuring the grains used such as corn.

In the Mitsubishi Corporation group, Agrex, Inc. procures grain and Nosan Corporation uses the grain to make formula feed. Japan Farm (the first factory accredited to produce KFC cut chicken) produces chicken. The processed chicken produced by Japan Farm is sold to subsidiary Kentucky Fried Chicken Japan, Ltd. (KFC Japan) via Foodlink Corporation. In this manner the feed and livestock value chain run by the Mitsubishi group supports KFC's restaurants.

Mitsubishi group's feed and livestock value chain



Source: Shared Research based on Nikkei Business materials

Takeout accounts for 70%

Around 70% of sales of the company's mainstay "original-recipe chicken" is takeout, reflecting growth in prepared meal demand accompanying the trend toward nuclear families.

KFC earnings

In FY03/21, revenues in the KFC business were JPY89.7bn (+12.6% YoY) and operating profit was JPY6.4bn (+32.8% YoY). System sales (total for directly operated and franchised stores) of JPY144.0bn were up 11.8% YoY, with directly operated stores generating sales of JPY39.4bn (+8.1% YoY) and franchised stores generating sales of JPY104.6bn (+13.3% YoY).

System sales

System sales (directly operated store sales plus at franchises) for KFC declined continuously from FY03/12 to FY03/14. This was due to the impact of economic stagnation such as declining wages and the launch of fried chicken prepared on-site by convenience stores. However, system sales rose for two consecutive fiscal years starting in FY03/15 due to a recovery in wages and a 4.2% price bump for "original-recipe chicken" on March 25, 2015 (from JPY240 to JPY250 including tax). In both FY03/17 and FY03/18, the company saw increases in average spending per customer but system sales still finished down in both years due to a drop in store traffic. The increase in system sales in FY03/19 was driven in large part by the jump in traffic sparked by the company's successful two-tiered marketing approach that made use of everyday value set menus and the periodic addition of new menu items. System sales continued to rise in FY03/20, on the back of measures to promote everyday use and periodically launch new menu items. System sales reached a record high in FY03/21 as the company attracted demand for its traditional strengths of takeout, drive-thorough, and home delivery services amid the trend of more families eating at home. The company also pushed forward with measures to promote everyday patronage and roll out new products.

Operating profit

The operating profit margin of 7.1% in FY03/21 was the highest the company has recorded since FY03/11. The SG&A expense ratio fell because of higher revenues.

KFC business KPIs

KFC business KPI	FY03/13 Act.	FY03/14 Act.	FY03/15 Act.	FY03/16 Act.	FY03/17 Act.	FY03/18 Act.	FY03/19 Act.	FY03/20 Act.	FY03/21 Act.
System sales (JPYmn)	**111,405**	**107,618**	**109,860**	**116,150**	**114,854**	**113,210**	**118,129**	**128,755**	**143,998**
Directly operated store sales	33,072	31,809	32,197	34,279	33,762	33,762	34,561	36,433	39,400
Franchised store sales	78,333	75,809	77,663	81,871	81,091	79,447	83,568	92,321	104,598
System sales (YoY)	**-3.5%**	**-3.4%**	**2.1%**	**5.7%**	**-1.1%**	**-1.4%**	**4.3%**	**9.0%**	**11.8%**
Directly operated store sales (YoY)	-4.8%	-3.8%	1.2%	6.5%	-1.5%	0.0%	2.4%	5.4%	8.1%
Franchised store sales (YoY)	-3.0%	-3.2%	2.4%	5.4%	-1.0%	-2.0%	5.2%	10.5%	13.3%
% of system sales									
Directly operated store sales	29.7%	29.6%	29.3%	29.5%	29.4%	29.8%	29.3%	28.3%	27.4%
Franchised store sales	70.3%	70.4%	70.7%	70.5%	70.6%	70.2%	70.7%	71.7%	72.6%
Number of stores	**1,180**	**1,171**	**1,155**	**1,144**	**1,149**	**1,153**	**1,132**	**1,133**	**1,138**
Number of directly operated store	329	329	330	316	326	329	306	306	299
Number of franchised store	851	842	825	828	823	824	826	827	839
Number of stores (YoY)	**1.2%**	**-0.8%**	**-1.4%**	**-1.0%**	**0.4%**	**0.3%**	**-1.8%**	**0.1%**	**0.4%**
Number of directly operated stores (YoY)	-0.3%	0.0%	0.3%	-4.2%	3.2%	0.9%	-7.0%	0.0%	-2.3%
Number of franchised stores (YoY)	1.8%	-1.1%	-2.0%	0.4%	-0.6%	0.1%	0.2%	0.1%	1.5%
Sales per store (JPYmn)	**94**	**92**	**95**	**102**	**100**	**98**	**104**	**114**	**127**
Directly operated stores	101	97	98	108	104	103	113	119	132
Franchised stores	92	90	94	99	99	96	101	112	125
Sales per store (YoY)	**-4.7%**	**-2.7%**	**3.5%**	**6.7%**	**-1.5%**	**-1.8%**	**6.3%**	**8.9%**	**11.3%**
Directly operated stores (YoY)	-4.5%	-3.8%	0.9%	11.2%	-4.5%	-0.9%	10.1%	5.4%	10.7%
Franchised stores (YoY)	-4.7%	-2.2%	4.6%	5.0%	-0.4%	-2.1%	4.9%	10.3%	11.7%

Source: Shared Research based on company materials
Note: Figures may differ from company materials due to differences in rounding methods.

Earnings structure

Earnings structure (consolidated) (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Total revenues	**85,864**	**83,436**	**84,605**	**88,180**	**88,032**	**73,457**	**74,344**	**79,634**	**89,652**
YoY	-2.6%	-2.8%	1.4%	4.2%	-0.2%	-16.6%	1.2%	7.1%	12.6%
Sales	78,010	75,937	77,138	80,254	79,962	66,565	67,695	72,114	80,184
YoY	-2.9%	-2.7%	1.6%	4.0%	-0.4%	-16.8%	1.7%	6.5%	11.2%
% of total revenues	90.9%	91.0%	91.2%	91.0%	90.8%	90.6%	91.1%	90.6%	89.4%
Other revenues	7,853	7,499	7,467	7,925	8,069	6,891	6,649	7,519	9,468
YoY	1.3%	-4.5%	-0.4%	6.1%	1.8%	-14.6%	-3.5%	13.1%	25.9%
% of total revenues	9.1%	9.0%	8.8%	9.0%	9.2%	9.4%	8.9%	9.4%	10.6%
Cost of revenues	46,207	44,976	46,399	48,816	48,144	41,852	42,306	44,674	50,954
YoY	-4.6%	-2.7%	3.2%	5.2%	-1.4%	-13.1%	1.1%	5.6%	14.1%
% of total revenues	53.8%	53.9%	54.8%	55.4%	54.7%	57.0%	56.9%	56.1%	56.8%
Cost of sales	40,457	39,753	41,234	43,418	42,717	37,250	38,111	39,732	44,761
YoY	-4.1%	-1.7%	3.7%	5.3%	-1.6%	-12.8%	2.3%	4.3%	12.7%
% of total revenues	47.1%	47.6%	48.7%	49.2%	48.5%	50.7%	51.3%	49.9%	49.9%
Cost of other revenues	5,750	5,222	5,165	5,397	5,427	4,602	4,195	4,942	6,192
YoY	-8.1%	-9.2%	-1.1%	4.5%	0.6%	-15.2%	-8.8%	17.8%	25.3%
% of total revenues	6.7%	6.3%	6.1%	6.1%	6.2%	6.3%	5.6%	6.2%	6.9%
Gross profit	39,656	38,460	38,206	39,364	39,887	31,604	32,037	34,959	38,698
YoY	-0.1%	-3.0%	-0.7%	3.0%	1.3%	-20.8%	1.4%	9.1%	10.7%
Gross profit margin	46.2%	46.1%	45.2%	44.6%	45.3%	43.0%	43.1%	43.9%	43.2%
SG&A expenses	37,261	36,638	37,536	37,352	37,328	31,127	29,831	30,173	32,344
YoY	-0.1%	-1.7%	2.5%	-0.5%	-0.1%	-16.6%	-4.2%	1.1%	7.2%
SG&A ratio	43.4%	43.9%	44.4%	42.4%	42.4%	42.4%	40.1%	37.9%	36.1%
Salaries and allowances	14,941	15,098	14,879	14,767	14,799	12,022	11,246	11,421	-
YoY	-0.7%	1.1%	-1.5%	-0.8%	0.2%	-18.8%	-6.5%	1.6%	-
% of total revenues	17.4%	18.1%	17.6%	16.7%	16.8%	16.4%	15.1%	14.3%	-
Rents	4,255	4,181	4,151	4,130	4,274	3,680	3,565	3,524	-
YoY	-1.4%	-1.7%	-0.7%	-0.5%	3.5%	-13.9%	-3.1%	-1.2%	-
% of total revenues	5.0%	5.0%	4.9%	4.7%	4.9%	5.0%	4.8%	4.4%	-
Advertising	4,373	3,779	4,558	4,254	3,681	3,128	2,782	2,445	-
YoY	4.3%	-13.6%	20.6%	-6.7%	-13.5%	-15.0%	-11.1%	-12.1%	-
% of total revenues	5.1%	4.5%	5.4%	4.8%	4.2%	4.3%	3.7%	3.1%	-
Depreciation	2,106	2,088	2,206	2,226	2,288	1,929	1,889	1,558	-
YoY	3.0%	-0.9%	5.7%	0.9%	2.8%	-15.7%	-2.1%	-17.5%	-
% of total revenues	2.5%	2.5%	2.6%	2.5%	2.6%	2.6%	2.5%	2.0%	-
Other SG&A expenses	11,586	11,492	11,742	11,975	12,286	10,368	10,349	11,225	32,344
YoY	-1.0%	-0.8%	2.2%	2.0%	2.6%	-15.6%	-0.2%	8.5%	188.1%
% of total revenues	13.5%	13.8%	13.9%	13.6%	14.0%	14.1%	13.9%	14.1%	36.1%
Operating profit	2,395	1,822	670	2,011	2,558	477	2,206	4,785	6,354
YoY	0.2%	-23.9%	-63.2%	200.1%	27.2%	-81.4%	362.5%	116.9%	32.8%
Operating profit margin	2.8%	2.2%	0.8%	2.3%	2.9%	0.6%	3.0%	6.0%	7.1%

Source: Source: Shared Research based on company data

Revenues

About 90% of the company's total revenues come from directly operated restaurants and sales of ingredients and other products to franchisees. The remaining 10% comes from royalties for sublicensing to franchisees, rental revenues from POS systems and other restaurant fixtures, and ad revenues from franchisees.

Cost of revenues

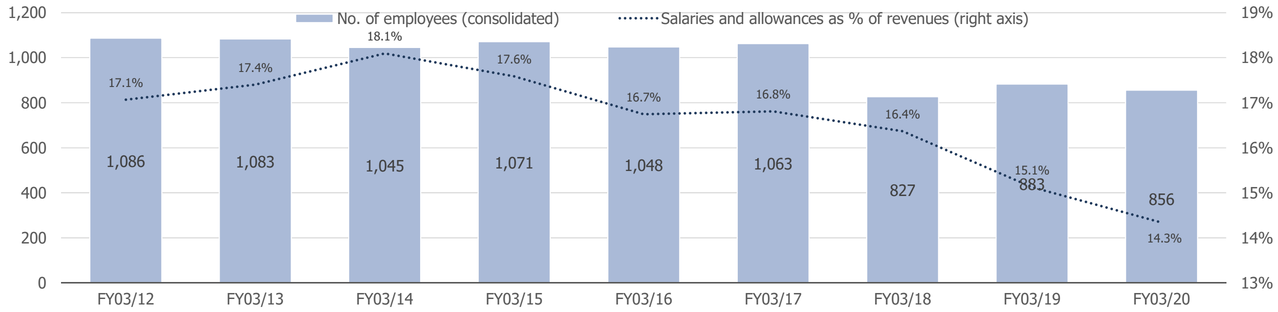
The total cost of revenues ratio in FY03/21 was 56.8%, consisting of the cost of sales and other cost of revenues. The cost of sales was 49.9%, comprising ingredients and materials such as 100% made-in-Japan chicken and flour. The remaining 6.9% under other cost of revenues was the cost of procuring POS systems and other store fixtures.

The cost of sales ratio has trended between 47% and 52%.

SG&A expenses

The SG&A expenses were 36.1% of total revenues in FY03/21. In FY03/20, SG&A expenses consisted mainly of salaries and allowances (14.3% of total revenues), rents (4.4%), and advertising expenses (3.1%). The company was able to lower the ratio of salaries and allowances to total revenues from 17.4% in FY03/13 to 14.3% in FY03/20.

Ratio of salaries and allowances to total revenues, consolidated employee numbers



Source: Shared Research based on company materials

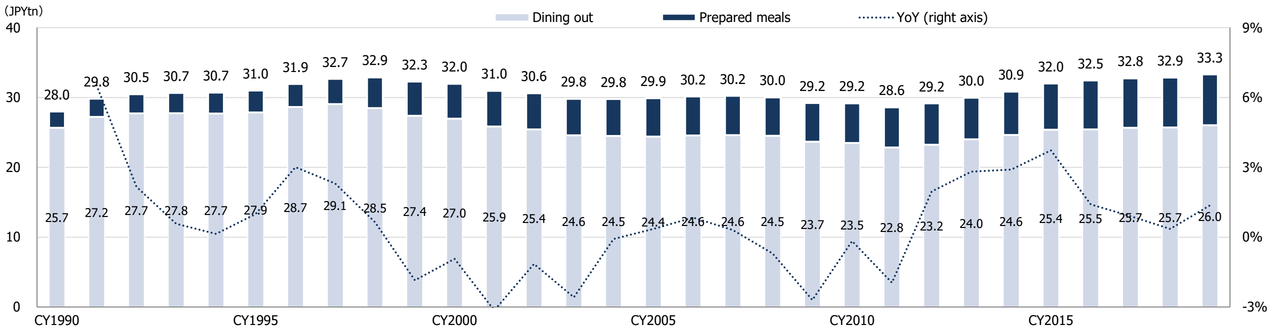
Market and value chain

Trends in restaurant and prepared meals market

Restaurant market (broad definition)

According to the Japan Food Service Association, in the broadly defined restaurant market, which includes both dining out and prepared meal markets, was worth JPY33.3tn (+1.4% YoY) in 2019. After peaking at JPY32.9tn in 1998, it continued to shrink amid contracting demand due to the decline and aging of the population and shift toward lower prices driven by growing price-consciousness among consumers. However, the dining out and prepared meal markets started to recover in 2012 and the overall market has been growing. One of the factors contributing to growth of the dining out market was demand from foreign tourists to Japan. The growth of the prepared meal market has been fueled by the higher number of people eating alone due to an increase in single-person households and working couples, changing social conditions such as the rise of nuclear families, and a wide range of prepared food products offered by convenience stores and supermarkets. The prepared meal market has expanded every year since 1976 with the exception of 2008, when it contracted 2.2% YoY.

Japan's dining-out and prepared meal markets

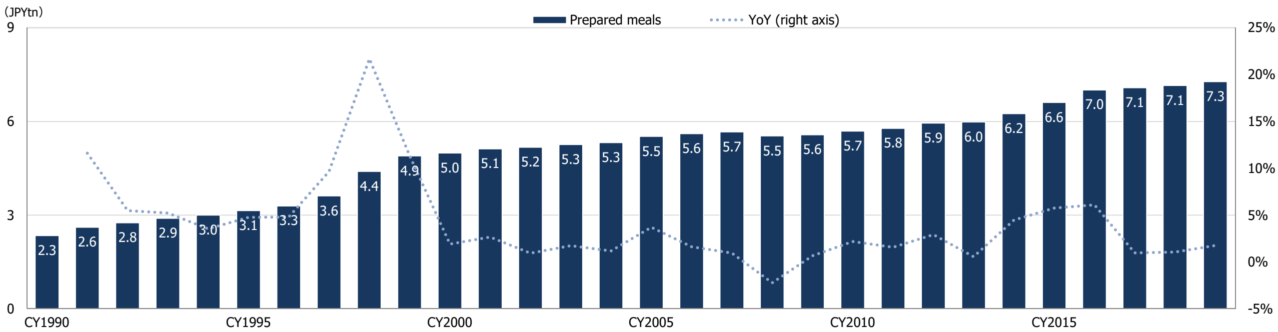


Source: Shared Research based on Japan Food Service Association materials

Prepared meal market

KFC Holdings' traditional strengths are in takeout and drive-through services, with takeout accounting for 70–80% of the total. The prepared meal market, which includes takeout and delivery food and beverage services, grew by1.7% YoY to JPY7.3tn in 2020.

Japan's prepared meal market

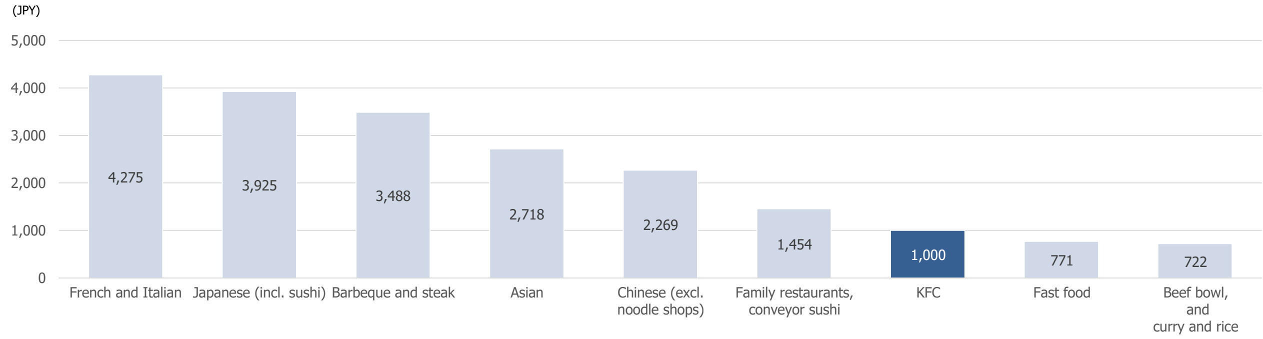


Source: Shared Research based on Teikoku Databank materials

Restaurant meal price comparison

According to FY2019 data from Recruit Lifestyle, spending per customer in fast food restaurants averaged JPY771, and family restaurants, JPY1,454, with KFC in the middle at JPY1,000.

Average spending per customer by restaurant format and KFC Holdings Japan meal prices (Greater Tokyo, Kansai, and Tokai regions: FY2019)



Source: Shared Research based on Recruit Lifestyle and company materials

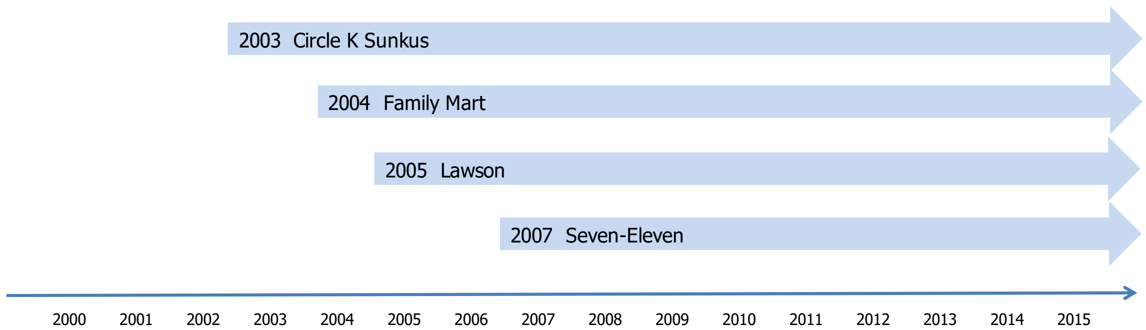
Japan's fried chicken market

Japan's fried chicken market has trended more or less flat since 2000. Competitors include hamburger chains such as McDonald's and Mos Burger, as well as supermarkets and convenience stores that offer prepared meals. Since 2003, major convenience store operators have entered the fried chicken market.

KFC's point of difference is the powerful "original-recipe chicken" brand fostered in Japan since the company was founded in 1970 and optimal chicken procurement arrangements with major trading company Mitsubishi Corporation (TSE1: 8058). Convenience stores primarily use imported frozen chicken 50 days old or older, while KFC's original-recipe chicken uses only Japan-raised chickens (about 38 days old), which are more tender and delicious, but make stable procurement difficult.

As shown in the data on average spending per customer by restaurant format, customer spend in KFC restaurants is higher than that in hamburger chains and other fast food restaurants.

Entrants in the fried chicken market in Japan



Source: Shared Research based on company materials

Peer group

KFC Holdings Japan operates fried chicken chains, and no competitor has the same portfolio. In the KFC business, there is no fast-food competitor who specializes in fried chicken.

Below are overviews of listed companies that are similar to KFC Holdings Japan.

McDonald's Holdings Company Japan Ltd. (TSE JASDAQ: 2702)

McDonald's is a global hamburger chain with a presence in over 100 countries and over 38,000 restaurants as of June 2021. The Japanese subsidiary was established in 1971, and McDonald's is the leading hamburger chain in Japan. Products made from chicken includes Chicken McNuggets (chicken nuggets), Shaka Chicken (fried chicken), Chicken Filet-O (hamburger), and Chicken Crisp (hamburger). McDonald's Holding Company Japan mainly imports chicken from Thailand (as of June 2021). The company posted a double-digit revenue decline and operating losses in FY12/14 and FY12/15. Its financial woes stemmed from a

2014 scandal involving expired poultry imported from China, as well as a 2015 incident involving foreign objects found in food. After mounting a turnaround in FY12/16, McDonald's Japan all-store sales and operating profit recovered to a record high in FY12/20, driven by drive-through and delivery services amid the growing trend of eating at home.

Mos Food Services, Inc. (TSE1: 8153)

Specialist hamburger franchise chain established in 1972, it has the second-largest market share in Japan after McDonald's. The company has produced unique hit products using Japanese flavors including teriyaki burgers using miso and soy sauce and the rice-based Mos Rice Burger. The side menu features Mos Chicken with the price set at JPY270 (as of June 2021), similar to KFC's JPY250 for its original-recipe chicken. Chicken used in Mos Chicken is produced in China (as of June 2021). During the three-year period ending in FY03/18, Mos Food Services reported an operating profit margin of more than 5%, giving it one of the highest operating profit margins in Japan's fast-food industry. In FY03/19, sales and earnings took a sharp turn for the worse with sales dropping 7.2% YoY following a food poisoning incident in August 2018. In FY03/20, though, performance recovered.

Comparison with listed peer companies

Comparison of key financial data (JPYmn)	FY11-12	FY12-13	FY13-14	FY14-15	FY15-16	FY16-17	FY17-18	FY18-19	FY20-21
KFC Holdings Japan (9873)	**FY03/13 Cons.**	**FY03/14 Cons.**	**FY03/15 Cons.**	**FY03/16 Cons.**	**FY03/17 Cons.**	**FY03/18 Cons.**	**FY03/19 Cons.**	**FY03/20 Cons.**	**FY03/21 Cons.**
Total revenues	85,864	83,436	84,605	88,180	88,032	73,457	74,344	79,634	89,652
YoY	-2.6%	-2.8%	1.4%	4.2%	-0.2%	-16.6%	1.2%	7.1%	12.6%
Gross profit	39,656	38,460	38,206	39,364	39,887	31,604	32,037	34,959	38,698
Gross profit margin	46.2%	46.1%	45.2%	44.6%	45.3%	43.0%	43.1%	43.9%	43.2%
Operating profit	2,395	1,822	670	2,011	2,558	477	2,206	4,785	6,354
Operating profit margin	2.8%	2.2%	0.8%	2.3%	2.9%	0.6%	3.0%	6.0%	7.1%
Net income attrib. to parent company shareholders	1,203	441	-524	730	1,365	578	2,055	1,533	2,805
Shareholders' equity	23,214	22,497	21,219	20,904	21,178	20,626	21,385	21,807	23,620
ROE	5.2%	1.9%	-2.4%	3.5%	6.5%	2.8%	9.8%	7.1%	12.3%
Number of employees	1,083	1,045	1,071	1,048	1,063	827	883	856	862
Revenues per employee	79	80	79	84	83	89	84	93	104
McDonald's Holdings Japan (2702)	**FY12/12 Cons.**	**FY12/13 Cons.**	**FY12/14 Cons.**	**FY12/15 Cons.**	**FY12/16 Cons.**	**FY12/17 Cons.**	**FY12/18 Cons.**	**FY12/19 Cons.**	**FY12/20 Cons.**
Revenue	294,710	260,441	222,319	189,473	226,646	253,640	272,257	281,763	288,332
YoY	-2.5%	-11.6%	-14.6%	-14.8%	19.6%	11.9%	7.3%	3.5%	2.3%
Gross profit	60,117	38,188	19,834	1,807	31,348	45,528	53,198	56,096	58,256
Gross profit margin	20.4%	14.7%	8.9%	1.0%	13.8%	17.9%	19.5%	19.9%	20.2%
Operating profit	24,780	11,524	-6,714	-23,440	6,930	18,912	25,045	28,018	31,290
Operating profit margin	8.4%	4.4%	-3.0%	-12.4%	3.1%	7.5%	9.2%	9.9%	10.9%
Net income attrib. to parent company shareholders	12,870	5,138	-21,843	-34,951	5,366	24,024	21,939	16,885	20,186
Shareholders' equity	170,571	171,720	147,559	108,666	110,000	129,690	146,226	159,295	175,081
ROE	7.7%	3.0%	-13.7%	-27.3%	4.9%	20.0%	15.9%	11.1%	12.1%
Number of employees	2,775	2,764	2,679	2,419	2,239	2,194	2,145	2,085	2,083
Revenue per employee	106	94	83	78	101	116	127	135	138
MOS FOOD SERVICES (8153)	**FY03/13 Cons.**	**FY03/14 Cons.**	**FY03/15 Cons.**	**FY03/16 Cons.**	**FY03/17 Cons.**	**FY03/18 Cons.**	**FY03/19 Cons.**	**FY03/20 Cons.**	**FY03/21 Cons.**
Sales	62,371	65,330	66,310	71,114	70,929	71,387	66,264	68,985	71,972
YoY	-0.5%	4.7%	1.5%	7.2%	-0.3%	0.6%	-7.2%	4.1%	4.3%
Gross profit	29,869	31,400	31,653	35,362	36,318	35,592	32,665	34,231	34,170
Gross profit margin	47.9%	48.1%	47.7%	49.7%	51.2%	49.9%	49.3%	49.6%	47.5%
Operating profit	1,889	2,157	1,555	3,824	4,664	3,734	517	1,060	1,422
Operating profit margin	3.0%	3.3%	2.3%	5.4%	6.6%	5.2%	0.8%	1.5%	2.0%
Net income attrib. to parent company shareholders	1,521	1,744	673	2,285	3,050	2,385	-907	365	997
Shareholders' equity	39,690	41,242	42,295	43,714	45,969	47,767	45,294	44,907	45,128
ROE	3.9%	4.3%	1.6%	5.3%	6.8%	5.1%	-1.9%	0.8%	2.2%
Number of employees	1,166	1,250	1,319	1,375	1,335	1,372	1,384	1,351	-
Sales per employee	53	52	50	52	53	52	48	51	-

Source: Shared Research based on company materials

Strengths and weaknesses

Strengths

Brand power nurtured since establishment

The company opened its first restaurant in Nagoya in 1970. Since then, the KFC brand with its statues of Colonel Sanders and fried chicken prepared on site with a secret recipe of 11 herbs and spices has spread throughout Japan. In addition, it was the company to instill the custom of eating fried chicken at Christmas time in Japan. KFC Japan is a well-known, leading chain in the fast-food industry in Japan, and Shared Research thinks it has built a unique brand among fried chicken fast food restaurant chains.

Business model built on support from Mitsubishi

The company's establishment was the fruit of four years of negotiations between Mitsubishi Corporation (stake: 35.12% as of March 31, 2021) and KFC founder Colonel Harland Sanders. The base for the original-recipe chicken is meat from approximately 38-day-old chicks raised in Japan (convenience stores use frozen imported poultry). KFC Japan obtains a steady supply through Mitsubishi using a value chain that extends from the corn and other grains for chicken feed through delivery of the pre-cut meat. In this manner, the company's operations are built on the support by Mitsubishi. Shared Research thinks that it would be difficult for other companies to create a similar business model offering fast food that matches the quality of KFC Japan.

Scale economies

Because KFC Japan's "original-recipe chicken" uses approximately 38-day-old quality chickens raised in Japan, procurement costs are relatively high compared with imported frozen poultry (which are older). Still, the company is able to keep costs low by obtaining volume discounts due to bulk procurements, leveraging its dominant position as the leading domestic fried chicken restaurant chain. Shared Research thinks that this is a barrier to entry for competitors, especially convenience stores, which use imported frozen poultry. We think economies of scale in obtaining materials and advertising are another barrier to entry for companies attempting to enter the market as fast-food chicken specialists.

Weaknesses

Constraints imposed by the franchise agreements with Yum! Brands

Approval from master franchisor Yum! Brands is needed for all aspects of the business under the franchise agreement, including products, ingredients, restaurants, and equipment. Shared Research thinks that constraints under the franchise agreement hinder the company's ability to nimbly respond to changes in consumer demand.

Constraints on sales promotion due to using domestically raised chicken (approximately 38-day-old chicks)

KFC Japan uses 100% domestically raised chicken (approximately 38-day-old chicks). When conducting an intensive sales campaign, other fast-food companies and convenience stores can adjust their schedules quickly because they mostly use frozen imported poultry. However, KFC Japan lacks this flexibility as it uses raised-to-order domestic chicken (38-day-old chicks). Shared Research thinks that this limitation is one of the company's weaknesses.

Financial statements

Income statement

Income statement (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.	FY03/22 Est.
Total revenues	**85,864**	**83,436**	**84,605**	**88,180**	**88,032**	**73,457**	**74,344**	**79,634**	**89,652**	**95,688**
YoY	-2.6%	-2.8%	1.4%	4.2%	-0.2%	-16.6%	1.2%	7.1%	12.6%	6.7%
Cost of revenue	46,208	44,976	46,399	48,816	48,144	41,852	42,306	44,674	50,954	
Cost ratio	53.8%	53.9%	54.8%	55.4%	54.7%	57.0%	56.9%	56.1%	56.8%	
Gross profit	**39,656**	**38,460**	**38,206**	**39,364**	**39,887**	**31,604**	**32,037**	**34,959**	**38,698**	
YoY	-0.1%	-3.0%	-0.7%	3.0%	1.3%	-20.8%	1.4%	9.1%	10.7%	
Gross profit margin	46.2%	46.1%	45.2%	44.6%	45.3%	43.0%	43.1%	43.9%	43.2%	
SG&A expenses	37,261	36,638	37,536	37,352	37,328	31,127	29,831	30,173	32,344	
YoY	-0.1%	-1.7%	2.5%	-0.5%	-0.1%	-16.6%	-4.2%	1.1%	7.2%	
SG&A ratio	43.4%	43.9%	44.4%	42.4%	42.4%	42.4%	40.1%	37.9%	36.1%	
Operating profit	**2,395**	**1,822**	**670**	**2,011**	**2,558**	**477**	**2,206**	**4,785**	**6,354**	
YoY	0.2%	-23.9%	-63.2%	200.1%	27.2%	-81.4%	362.5%	116.9%	32.8%	-
Operating profit margin	2.8%	2.2%	0.8%	2.3%	2.9%	0.6%	3.0%	6.0%	7.1%	-
Non-operating income	111	34	-3	-145	-133	150	769	-1,533	-856	
Rents income	222	143	177	148	161	227	241	230	230	
Rents expenses	99	73	145	161	169	184	166	161	173	
Other	-12	-36	-35	-132	-125	107	694	-1,602	-913	
Recurring profit	**2,506**	**1,856**	**667**	**1,866**	**2,425**	**627**	**2,975**	**3,252**	**5,498**	
YoY	1.5%	-25.9%	-64.1%	179.8%	30.0%	-74.1%	374.5%	9.3%	69.1%	-
Recurring profit margin	2.9%	2.2%	0.8%	2.1%	2.8%	0.9%	4.0%	4.1%	6.1%	-
Extraordinary gains (losses)	-164	-588	-512	-391	-96	840	173	137	-376	
Income taxes	1,138	826	680	744	964	889	1,092	1,854	2,316	
Implied tax rate	48.6%	65.1%	438.7%	50.4%	41.4%	60.6%	34.7%	54.7%	45.2%	
Net income attrib. to owners of the parent	**1,203**	**441**	**-524**	**730**	**1,365**	**578**	**2,055**	**1,533**	**2,805**	
YoY	9.2%	-63.3%	-	-	87.0%	-57.7%	255.5%	-25.4%	83.0%	-
Net margin	1.4%	0.5%	-0.6%	0.8%	1.6%	0.8%	2.8%	1.9%	3.1%	-

Source: Shared Research based on company data
Note: Figures may differ from company materials due to differences in rounding methods.

Balance sheet

Balance sheet (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Current assets	**23,340**	**21,682**	**22,332**	**21,390**	**20,721**	**14,952**	**19,196**	**20,898**	**26,141**
Cash and deposits	13,502	16,146	16,804	15,339	14,571	9,757	13,267	14,917	18,476
Accounts receivable	3,544	3,701	3,546	3,855	4,007	3,562	4,269	4,386	5,751
Inventory assets	729	518	397	697	450	414	486	386	406
Other	5,565	1,317	1,585	1,499	1,693	1,219	1,174	1,209	1,405
Noncurrent assets	16,968	16,301	16,085	17,902	18,762	20,793	19,223	17,113	16,553
Tangible fixed assets	6,184	5,703	6,093	7,178	8,506	7,734	6,474	6,197	6,123
Intangible assets	2,950	2,924	2,874	2,828	2,206	1,704	1,091	1,083	1,591
Investments and other assets	7,834	7,674	7,118	7,896	8,050	11,354	11,658	9,832	8,838
Total assets	**40,308**	**37,984**	**38,418**	**39,292**	**39,484**	**35,746**	**38,420**	**38,012**	**42,694**
Current liabilities	**13,029**	**11,203**	**13,166**	**13,070**	**13,033**	**10,929**	**13,222**	**12,514**	**15,265**
Accounts payable	6,568	5,754	5,978	6,232	5,824	5,735	6,664	5,626	6,757
Short-term debt	211	193	187	531	618	531	519	115	87
Other current liabilities	6,250	5,256	7,001	6,307	6,591	4,663	6,039	6,773	8,417
Fixed liabilities	**4,065**	**4,283**	**4,031**	**5,317**	**5,272**	**4,190**	**3,812**	**3,690**	**3,808**
Long-term debt	207	188	432	1,533	1,142	666	189	171	196
Other	3,858	4,095	3,599	3,784	4,130	3,524	3,623	3,519	3,612
Total liabilities	**17,094**	**15,486**	**17,197**	**18,387**	**18,305**	**15,120**	**17,034**	**16,204**	**19,073**
Net assets	**23,214**	**22,497**	**21,219**	**20,904**	**21,178**	**20,626**	**21,385**	**21,807**	**23,620**
Capital stock	7,297	7,297	7,297	7,297	7,297	7,297	7,297	7,297	7,297
Capital surplus	10,430	10,430	10,430	10,430	10,430	10,430	10,430	9,689	9,689
Retained earnings	6,165	5,485	4,228	3,837	4,082	3,539	4,473	4,886	6,570
Treasury stock	-710	-722	-733	-739	-739	-887	-887	-147	-134
Accum. other comprehensive income	31	7	-2	79	108	246	71	81	197
Minority interests	-	-	-	-	-	-	-	-	-
Total liabilities and equity	**40,308**	**37,984**	**38,418**	**39,292**	**39,484**	**35,746**	**38,420**	**38,012**	**42,694**
Working capital	-2,295	-1,535	-2,035	-1,680	-1,367	-1,759	-1,909	-854	-600
Total interest-bearing debt	418	381	619	2,064	1,760	1,197	708	286	283
Net cash	13,084	15,765	16,185	13,275	12,811	8,560	12,559	14,631	18,193
Days in accounts receivable	15	16	16	15	16	19	19	20	21
Days in inventory	6	5	4	4	4	4	4	4	3
Days in accounts payable	56	50	46	46	46	50	53	50	44
Cash conversion cycle (days)	-35	-29	-27	-26	-25	-28	-30	-27	-21
Current ratio	179%	194%	170%	164%	159%	137%	145%	167%	171%
Fixed ratio	73.1%	72.5%	75.8%	85.6%	88.6%	100.8%	89.9%	78.5%	70.1%
Equity ratio	57.6%	59.2%	55.2%	53.2%	53.6%	57.7%	55.7%	57.4%	55.3%

Source: Source: Shared Research based on company data
Note: Accounts receivable figures are after deducting bad debt provisions.
Note: Figures may differ from company materials due to differences in rounding methods.

Cash and deposits

Cash and deposits were the largest component of the company’s total assets. The share of cash and deposits increased to 43.3% in FY03/21. The increase in investment and other assets in FY03/17 and FY03/18 can be seen as coming from the acquisition of shares in Bamboo Holding Pte. Ltd. and BYO Co., Ltd.

Working capital

Working capital was negative because accounts payable were greater than the combined total of accounts receivable and inventories. Accounts receivable rose with growth in franchisee sales.

Cash flow statement

Cash flow statement (JPYmn)	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
Cash flows from operating activities (1)	3,370	1,717	4,574	1,519	4,424	1,928	5,436	3,934	7,042
Pre-tax profit	2,342	1,268	155	1,475	2,330	1,467	3,148	3,388	5,121
Depreciation	2,394	2,325	2,404	2,649	2,747	2,355	2,291	1,955	1,477
Impairment losses	209	609	599	243	125	197	335	101	300
Amortization of goodwill	-	-	-	-	-	-	-	-	-
Change in working capital	-786	-550	487	-403	-186	779	117	-846	-281
Income taxes	-584	-1,228	-519	-695	-978	-675	-199	-2,183	-1,853
Other	-205	-707	1,448	-1,750	386	-2,195	-256	1,519	2,278
Cash flows from investing activities (2)	-1,558	2,287	-1,556	-298	-3,679	-4,863	-265	-626	-2,246
Acquisition of tangible/intangible fixed assets	-1,783	-1,932	-2,938	-2,057	-2,641	-2,257	-1,291	-1,057	-2,402
Proceeds from sale of tangible/intangible fixed assets	-	-	-	404	10	3	543	197	81
Payments for lease and guarantee deposits	-106	-107	-219	-127	-405	-211	-51	-28	-76
Proceeds from collection of lease and guarantee deposits	238	268	565	242	190	364	257	174	100
Proceeds from sale of stores	127	128	200	316	93	93	510	107	74
Other	-34	3,930	836	924	-926	-2,855	-233	-19	-23
FCF (1+2)	1,812	4,004	3,018	1,221	745	-2,935	5,171	3,308	4,796
Cash flows from financing activities	-1,367	-1,360	-1,360	-1,686	-1,512	-1,878	-1,660	-1,657	-1,237
Change in short-term borrowings	-	-	-	-	80	-80	-	-	-
Change in long-term borrowings	-	-	-	-	-	-	-	-	-
Issuance and redemption of corporate bonds	-	-	-	-	-	-	-	-	-
Acquisition of treasury stock	-26	-12	-10	-	-	-147	-	-	-
Dividends paid	-1,127	-1,126	-1,124	-1,123	-1,116	-1,119	-1,122	-1,121	-1,125
Other	-240	-234	-236	-563	-476	-679	-538	-536	-112
Cash and cash equivalents	444	2,644	1,657	-465	-767	-4,813	3,510	1,649	3,558
Cash and cash equivalents (year-end)	11,502	14,146	15,804	1,539	14,571	9,757	13,267	14,917	18,476
Depreciation (A)	2,394	2,325	2,404	2,649	2,747	2,355	2,291	1,955	1,477
Capital expenditures (B)	-1,783	-1,932	-2,938	-1,653	-2,631	-2,254	-748	-860	-2,321
Change in working capital (C)	-786	-550	487	-403	-186	779	117	-846	-281
Simple FCF (NI+A+B-C)	3,739	2,211	-866	2,874	2,632	789	4,574	5,329	4,558

Source: Shared Research based on company data
Figures may differ from company materials due to differences in rounding methods

Cash flows from operating activities

In FY03/21, operating cash inflows were JPY7.0bn. This was mainly because of JPY5.1bn in pre-tax profit and JPY1.5bn in depreciation.

Cash flows from investing activities

In FY03/21, cash outflows from investing activities were JPY2.2bn. A large amount (JPY2.4bn) was spent for the acquisition of tangible and intangible fixed assets, including investment in stores. In FY03/17, there were outlays of JPY831mn, and in FY03/18 outlays of JPY4.0bn, for the acquisition of investment securities (likely in Bamboo Holding Pte. Ltd. and BYO Co., Ltd).

Cash flows from financing activities

In FY03/21, cash outflows from financing activities were JPY1.2bn, primarily reflecting JPY1.1bn in dividends paid.

ROE, ROA, ROIC

(JPYmn)	FY03/12 Cons.	FY03/13 Cons.	FY03/14 Cons.	FY03/15 Cons.	FY03/16 Cons.	FY03/17 Cons.	FY03/18 Cons.	FY03/19 Cons.	FY03/20 Cons.	FY03/21 Cons.
ROE	**4.7%**	**5.2%**	**1.9%**	**-2.4%**	**3.5%**	**6.5%**	**2.8%**	**9.8%**	**7.1%**	**12.3%**
Net margin	1.3%	1.4%	0.5%	-0.6%	0.8%	1.6%	0.8%	2.8%	1.9%	3.1%
Total asset turnover	2.14	2.10	2.13	2.21	2.27	2.23	1.95	2.00	2.08	2.22
Financial leverage (equity multiplier)	1.77	1.76	1.71	1.75	1.84	1.87	1.80	1.77	1.77	1.78
ROA (RP-based)	**6.0%**	**6.1%**	**4.7%**	**1.7%**	**4.8%**	**6.2%**	**1.7%**	**8.0%**	**8.5%**	**13.6%**
ROIC	**6.0%**	**6.3%**	**4.9%**	**1.9%**	**6.0%**	**7.7%**	**1.5%**	**7.0%**	**15.0%**	**19.2%**
NOPAT	1,418	1,485	1,129	431	1,346	1,769	330	1,531	3,320	4,408
Net assets + Interest-bearing debt	23,761	23,669	23,255	22,358	22,403	22,953	22,381	21,958	22,093	22,998
ROIC (before tax)	10.1%	10.1%	7.8%	3.0%	9.0%	11.1%	2.1%	10.0%	21.7%	27.6%
Operating profit margin	2.7%	2.8%	2.2%	0.8%	2.3%	2.9%	0.6%	3.0%	6.0%	7.1%
Revenues / Invested capital	3.71	3.63	3.59	3.78	3.94	3.84	3.28	3.39	3.60	3.90

Source: Shared Research based on company data

Historical performance

Cumulative Q3 FY03/21 results (out February 10, 2021)

Results summary

- Cumulative Q3 FY03/21 results: Cumulative Q3 FY03/21 revenues were JPY68.5bn (+12.5% YoY), operating profit was JPY5.7bn (+35.0% YoY), and net income was JPY2.5bn (-17.9% YoY). With the reimposition of the state of emergency in January 2021, the government request for shortened business hours, the suspension of sales of Go To Eat premium meal tickets by some local governments, and a decline in demand for restaurants due to teleworking, the restaurant industry faces a challenging operating environment. Amid the rise in at-home dining, the company's forte of takeout and drive-through services drove higher revenues and operating profit. System sales at existing stores were up 14.4% YoY. On the other hand, it is unclear when the COVID19 outbreak might end and equity-method affiliates (Bamboo [Thailand] Holding Pte. Ltd. and BYO Co., Ltd.) continued to face a harsh business climate, so the company recorded a JPY1.1bn loss on investment in equity-method affiliates as non-operating expenses. In addition, an impairment loss of JPY200mn was recorded for restaurants where profitability has declined. As a result, net income fell YoY.
- System sales: In cumulative Q3 FY03/21, system sales (including franchises) were JPY109.9bn (+12.1% YoY). The combination of value measures to promote daily use (in the form of reasonably-priced set menus) and product measures to deliver pleasant surprise and enjoyment was successful. Popular menu items include a JPY500 lunch set that became a regular menu item in January 2020, as well as limited-time offerings such as Boneless Chicken JPY1000/JPY1500 Pack and Winter Pack. Limited-time new products included Truffle-scented Creamy Rich Sandwich, Chicken Cream Pot Pie (winter classic product) and Red Hot Chicken. As part of a set of measures to prevent the spread of infection, QR code payment was introduced at all stores, and various contactless initiatives were implemented, such as a trial of store pickup lockers where customers can pick up products ordered online on a non-contact basis. System sales at existing stores remained positive, with up 12.2% YoY in October, up 18.7% YoY in November, up 0.8% YoY in December, and up 10.5% YoY in January, resulting in a 14.4% YoY increase in cumulative Q3 FY03/21. As of end-December 2020, delivery services were offered at 341 stores (+121 stores versus end-March 2020). The 2020 KFC "Christmas Campaign" ran for seven days from December 19th to 25th, the peak demand period. System sales reached JPY6.9bn, while those from December 20th to 25th in 2019 were JPY7.1bn. The company implemented various health and safety measures to avoid the "Three Cs" in stores, including the promotion of advance reservations and the suspension of sales at booths outside stores.
- Full-year FY03/21 forecast: Full-year FY03/21 forecast has remained unchanged since announced on November 11, 2020. It calls for revenues of JPY86.5bn (+8.6% YoY) and operating profit of JPY6.0bn (+25.4%). The progress rate versus the full-year forecast is ahead of the previous year at 79.2% for sales (76.5% in Q3 FY03/20) and 95.8% for operating profit (88.9%). However, given that uncertainty over when the COVID-19 pandemic will end still remains, with the second state of emergency declared in January 2021 and shortened business hours accordingly requested, the company says it is difficult to make rational forecasts for recurring profit and net income, which have therefore been left undetermined. A dividend of JPY60 per share is planned for FY03/21 (ordinary dividend of JPY50 per share and commemorative dividend of JPY10 per share for the 50th anniversary), compared with JPY50 per share in FY03/20. The company will also provide additional shareholder benefits in commemoration of the 50th anniversary of its founding.

Q3 FY03/21 results

Q3 FY03/21 results: Q3 revenues were JPY25.2bn (+10.3% YoY), operating profit was JPY2.3bn (+31.2% YoY), and net income was JPY852mn (-22.0% YoY). The average spend per customer increased supported by takeout, likely for at-home family dining.

GPM was 42.4%, down from 43.6% in Q3 FY03/20, but SG&A expenses amounted to JPY8.3bn, up only 1.8% YoY, and the company's SG&A expense ratio improved to 33.0% (versus 35.8% in Q3 FY03/20). Meanwhile, OPM was 9.3%, up from 7.8% in Q3 FY03/20. SG&A expenses rose due primarily to costs associated with renovations at (18) directly operated stores and delivery agent fees stemming from expansion in the number of stores providing delivery services. However, this increase in SG&A expenses was limited primarily by a decline in utility expenses incurred at stores that shortened their business hours.

The company recorded an equity-method investment loss of JPY764mn in Q1, a profit of JPY 208mn in Q2, and a loss of JPY574 in Q3. Performance continued to be particularly tough at BYO Co., Ltd., which operates a variety of Japanese food businesses, including Japanese-style bars. In September, BYO opened a new location in Nihonbashi and began providing services such as pre-order sales and delivery of traditional Japanese New Year cuisine, but these services could not compensate for impact from the consumer tendency to remain indoors during the COVID-19 pandemic and shortened business hours.

With regard to KFC, profitability at stores located in city centers declined, incurring impact from the customer tendency to remain indoors during the COVID-19 pandemic and the spread of teleworking. The company booked JPY200mn in impairment loss associated with stores and other facilities as extraordinary loss, and net income declined.

System sales

In cumulative Q3 FY03/21, system sales (including franchises) were JPY109.9bn (+12.1% YoY). This growth was driven by existing stores, where average monthly sales were JPY11.3mn, their highest level in the past 24 years.

System sales in Q3 FY03/21 were JPY40.3bn (+9.7% YoY). Finding success with a combination of measures that encourage daily use by eliciting the sense of a bargain and product policies that deliver surprises and enjoyment, existing stores generated sales that were 14.4% higher YoY. Starting in January 2020, the company converted its JPY500 lunch into a standard menu item and began offering various limited-time meal packages, including its boneless chicken packs for JPY1,000 and JPY1,500 and its winter packs. As new limited-time products, the company began selling its truffle-scented creamy rich sandwich, as well as its chicken cream pot pie and red-hot chicken, which are both standard winter items. Apparently, the company's Ii Tokodori Pack (chicken set including crispy fried chicken breast, a biscuit, and French fries) and its half-price ten-piece nuggets set have helped attract younger customers aged 10 through 29, in addition to the family customer base that the company had previously targeted.

System sales in December, the company's busiest month, rose 0.8% YoY. Prioritizing the prevention of COVID-19 infections, the company suspended in-store dining and the opening of outdoor booths. Despite these circumstances, system sales generated over the seven days spanning from December 19–25, 2020 were JPY6.9bn (versus JPY7.1bn from December 20–25, 2019). Contributing to this result was the company's early focus on conducting pre-order sales for Christmas campaign items, which it began accepting on November 4. Nationwide online pre-orders grew substantially, in part because the percentage of customers that purchased items via pre-order rose.

Also contributing to solid system sales in December were the company's active efforts aimed at capturing demand both before and after the Christmas sales period. The COVID-19 pandemic has resulted in an environment within which large numbers of people cannot gather for parties or other events. In response, the company expanded its lineup of meal set and package items targeting parties held by small groups of people such as families and friends. This lineup expansion led to an increase in system sales generated outside of the Christmas sales period.

The company's enhancement of takeout, drive-through, and delivery services in response to a rise in needs related to in-home consumption occurring during the COVID-19 pandemic appears to have contributed to the increase in system sales. In particular, the company has arranged a system for capturing expanding delivery demand, providing delivery services at 341 of its 1,140 stores (as of December 31, 2020; +121 stores compared to March 31, 2020). Currently, the company is providing delivery both through its own service and through delivery agencies, such as Uber Eats. Moving forward, the company plans to continue implementing delivery services within areas where they are projected to generate results. Additionally, the company is strengthening efforts related to contactless services, including store pickup lockers, a system through which delivery service staff and customers can pick up items ordered online without interacting with employees using in-store storage compartments.

The company opened 17 stores (one directly operated and16 franchised stores), bringing the total number of stores to 1,140 at end-Q3 FY03/21. Renovations were carried out at 162 stores consisting of 39 directly operated stores and 123 franchised stores. The company remodeled more stores than in typical years, increasing its investment in forward-leaning remodeling work during a period of strong results.

1H FY03/21 results (out November 11, 2020)

Results summary

- ▷ 1H FY03/21 results: 1H FY03/21 revenues were JPY43.3bn (+13.8% YoY), operating profit was JPY3.4bn (+37.8% YoY), and net income was JPY1.6bn (-15.5% YoY). The restaurant industry faces a challenging operating environment with the consumption tax hike in October 2019 leading to austerity among consumers, as well as the impact of restrictions on events and group dining as a part of efforts to prevent the spread of COVID-19. Amid the rise in at-home dining, the company's forte of takeout and drive-through services drove higher revenues and operating profit. System sales at existing stores were up 17.9% YoY. On the other hand, the COVID-19 outbreak is causing equity-method affiliates (Bamboo [Thailand] Holding Pte. Ltd. and BYO Co., Ltd.) to continue to face a harsh business climate, so the company recorded a JPY556mn loss on investment in equity-method affiliates as non-operating expenses. As a result, net income fell YoY.
- ▷ Revisions to full-year FY03/21 forecast: The company revised FY03/21 forecast upward for revenues of JPY86.5bn (+8.6% YoY; previous forecast was JPY85.0bn) and operating profit of JPY6.0bn (+25.4% YoY; previous forecast was JPY5.0bn). Following strong 1H earnings results, the company expects 2H revenues to exceed year-ago levels on continued promotion of daily patronage through increased messaging with the *Why not make it KFC today?* campaign; developing new products; and strengthening takeout, drive-through, and delivery services. By end-FY03/21, the company expects to have 1,135 stores (net increase of two), including 22 newly opened ones, 197 that are renovated, and 340 that provide delivery services (+120 YoY). In 1H, equity-method affiliates faced tough conditions, including temporary closures and reduced hours of operation due to the COVID-19 outbreak. Operating hours have been gradually returning to normal since lifting of the emergency declaration, but this has not led to a recovery in sales. Recurring profit and net income forecasts remain undetermined as uncertainty over when the COVID-19 pandemic will end makes it difficult to make rational forecasts. The planned dividend for FY03/21 remains unchanged at JPY50 per share, on par with the dividend paid in FY03/20.

Q2 FY03/21 results

Q2 FY03/21 revenues were JPY23.5bn (+15.7% YoY), operating profit was JPY2.1bn (+39.1% YoY), and net income was JPY1.5bn (+27.2% YoY). YoY growth accelerated from the previous quarter with Q1 revenues up 11.5% and Q1 operating profit up 35.5%. The average spend per customer increased supported by takeout, likely for at-home family dining. The gross profit margin declined from 44.0% in Q2 FY03/20 to 43.7% while the company managed to keep SG&A expenses at JPY8.2bn (+10.0% YoY). As a result, SG&A expense ratio improved from 36.6% in Q2 FY03/20 to 34.8%. The main factors contributing to the increased SG&A expense are the greater number of directly operated stores where renovations were made (nine stores, an increase of two from seven stores in Q2 FY03/20), higher delivery agent fees due to a larger number of stores introducing delivery, and higher fees associated with a higher proportion of cashless transactions. In Q2, no stores were temporarily closed, but there were stores with shortened opening hours, and utility expenses and rent decreased. The operating profit margin increased from 7.5% in Q2 FY03/20 to 9.0%. In Q2, the company recorded a JPY208mn gain on investment in equity-method affiliates, up from a loss of JPY764mn in Q1.

System sales

In 1H FY03/21, system sales (including franchises) were JPY69.6bn (+13.5% YoY). Existing stores drove results, with average monthly system sales at existing stores of JPY1.1bn, the highest level in the last 24 years. The combination of value measures to promote daily use (in the form of reasonably-priced set menus) and product measures to deliver pleasant surprise and enjoyment was successful. Popular menu items include a JPY500 lunch set that became a regular menu item in January 2020, as well as limited-time offerings such as Founding Anniversary Pack, 30% off Pack, and Dip Barrel (including three types of dipping sauce). Limited-time new products included Kaoru Yuzu Shichimi Chicken and Torori Tsukimi Sandwich. To boost convenience for customers, QR code payment systems were adopted in all stores, further expanding cashless payment options. The company also started incorporating an electronic toll collection (ETC) multipurpose use system for drive-through payments on a trial basis. The combination of such new initiatives to improve convenience appears to have contributed to revenue growth.

Following the lifting of the state of emergency, system sales at existing stores were down 1.0% YoY in June (that system sales at existing stores were up significantly in June FY 03/20, by 24.1% YoY, was also a factor), but have remained strong since the following month, up 27.3% YoY in July (customer count up 13.3% YoY; average spend per customer up 12.3% YoY), up 13.6% YoY in August (customer count up 6.1% YoY; average spend per customer up 7.1% YoY), up 4.8% YoY in September (customer count down 2.2% YoY; average spend per customer up 7.1% YoY), and up 12.2% YoY in October (customer count up 8.1% YoY; average spend per customer up 3.7% YoY). System sales at existing stores have risen for nine consecutive quarters, since Q2 FY03/19. The company opened seven franchised stores in 1H, bringing the total number of stores to 1,134 at end-Q2 FY03/21 (net increase of six stores YoY). Renovations were carried out at 100 stores (+36 stores YoY), consisting of 21 directly operated stores and 79 franchised stores. As of end-September 2020, delivery services were offered at 312 stores (+92 stores versus end-March 2020).

Q2 FY03/21 system sales (including franchises) amounted to JPY37.6bn (+14.1% YoY). Since FY03/19, the company has undertaken the following measures to optimize operations (targeting customer visits on regular days): 1) enhancing drive-through and delivery in areas where there is demand; 2) increasing convenience by promoting use of its app, and expanding online orders and support for cashless payment; and 3) promoting everyday patronage by combining value measures and product measures that deliver pleasant surprise and enjoyment, as well as by making the JPY500 lunch a regular fixture on the menu. Such measures acted as a tailwind and contributed to increased revenue during the COVID-19 outbreak, during which consumer behavior transformed drastically: people refrained from going out, at-home consumption increased, and people were more inclined to save.

Stores in city centers, downtown areas, shopping centers, and tourist spots were temporarily closed in Q1 during the state of emergency, but there were no temporary store closures in Q2. The operation of stores under shortened opening hours continues, and stores that were previously open until 10 p.m. are closing at 9 p.m., and the company will respond to all government policies and requests as a basic principle. However, it appears that demand after 9 p.m. is decreasing due to the proliferation of teleworking and staggered commuting, so the impact on the company's revenue is minor.

There are 430 stores offering drive-through services (38% of total stores), and they have come to be chosen as stores where customers can purchase with confidence. It appears that stores offering drive-through services drove revenue growth in Q2. The number of stores offering delivery services rose to 312 stores as at end-September 2020, up from 220 stores as at end-March 2020. The company is strategically increasing the number of stores offering delivery services as a measure to enhance convenience during the COVID-19 crisis. The company has been actively using delivery agents since its introduction at 22 stores in Greater Tokyo in May 2017, leading to an expansion of the number of stores offering the service. The company states that the positive impact on revenue associated with delivery services varies significantly by store. However, this is a factor pushing up revenue, and the company plans to continue to increase the number of stores supporting delivery, including the use of delivery agents.

Previously approximately 70% of all transactions were takeout purchases, but it appears that this has risen to approximately 80% due to at-home consumption demand. Because the proportion of transactions that were takeout purchase was previously high, the company has already put operational mechanisms in place to support takeout. Demand for takeout increased as a result of the COVID-19 pandemic and the company was able to capture this demand, which contributed to higher revenue.

Q1 FY03/21 results (out August 7, 2020)

Results summary

- ▷ Q1 FY03/21 results: Q1 FY03/21 revenues were JPY19.8bn (+11.5% YoY), operating profit was JPY1.3bn (+35.5% YoY), and net income attributable to owners of the parent was JPY82mn (-88.3% YoY). The restaurant industry faces a challenging operating environment with the consumption tax hike in October 2019 leading to austerity among consumers, followed by the impact of voluntary restraints from going out and restrictions on events as a part of efforts to prevent the spread of the COVID-19 pandemic. In this environment, the company continued promoting daily use, developing new products, and capturing demand for its mainstay takeout, drive-through, and delivery services, resulting in higher revenues and operating profit. System sales at existing stores were up 21.2% YoY. On the other hand, the COVID-19 outbreak led to weak performance at equity-method affiliates (Bamboo [Thailand] Holding Pte. Ltd. and BYO Co., Ltd.), and the company recorded an equity-method investment loss of JPY764mn as non-operating expenses. Of the JPY764mn in losses, JPY627mn was due to the revaluation of fair value for the investee of Bamboo (Thailand) Holding Pte. Ltd. As a result, net income fell substantially YoY. Progress versus full-year FY03/21 forecast (which was announced alongside Q1 results) came to 23.2% for revenues (22.2% in Q1 FY03/20 versus full-year FY03/20 results) and 25.8% for operating profit (19.9%).
- ▷ System sales: In Q1 FY03/21, system sales (including franchises) were JPY32.0bn (+12.8% YoY). The combination of value measures to promote daily use (in the form of reasonably-priced set menus) and product measures to deliver pleasant surprise and enjoyment was successful. New products included chicken menu items such as Garlic Chicken (boneless) and Popcorn Chicken, and the company also enhanced its drink menu such as Lemonade and other drinks. Even during the state of emergency, system sales at existing stores remained strong, up 33.1% YoY in April, up 37.6% YoY in May, and down 1.0% YoY in June. The rise in average spend per customer was driven by an uptick in family purchases in response to voluntary restraints from going out. The company opened three franchised stores, bringing the total number of stores to 1,131 at end-Q1 FY03/21 (net decrease of one store or -0.1% YoY). Renovations were carried out at 58 stores (+16 stores or +38.1% YoY), consisting of 12 directly operated stores and 46 franchised stores. As of end-June 2020, delivery services were offered at 264 stores (+44 stores versus end-March 2020).
- ▷ Full-year FY03/21 forecast: The company's FY03/21 forecast calls for revenues of JPY85.0bn (+6.7% YoY) and operating profit of JPY5.0bn (+4.5% YoY) while forecasts for recurring profit and net income remain undetermined. KFC Japan expects revenues for the mainstay KFC business to continue growing in Q2 onward, driven by strong takeout, drive-through, and delivery demand. On the other hand, equity-method affiliates continue to face tough conditions, including temporary closure of stores and shortening hours of operation due to the COVID-19 outbreak. While the company expects a recovery in revenues through 2H FY03/21, it kept forecasts for recurring profit and net income undetermined as it is currently not able to make reasonable forecast calculations. The company plans to disclose the forecast as soon as it becomes possible to do so. It also intends to pay a dividend of JPY50 per share for FY03/21, which is on par with FY03/20.

Q1 FY03/21 results

In Q1 FY03/21, revenues were JPY19.8bn (+11.5% YoY), operating profit was JPY1.3bn (+35.5% YoY), and net income was JPY82mn (-88.3% YoY). Over FY03/21, KFC Japan is continuing to promote everyday patronage through value measures and develop new products that deliver pleasant surprise and enjoyment. Customer purchasing methods underwent a major shift amid the COVID-19 pandemic. In Q1, system sales at existing stores were up 21.2% YoY, driven by higher average spending per customer (customer numbers up 1.4% YoY, average spending per customer up 19.5% YoY). Excluding store closures, system sales at existing stores rose 33.1% YoY in April (customer numbers up 7.3% YoY, average spending per customer up 24.0% YoY) and 37.6% YoY in May (customer numbers up 6.5% YoY, average spending per customer up 29.2% YoY). Contributing to the sharp increase in average spending per customer over April to May was an increase in customers purchasing large volume packs to take home and eat with their families amid greater at-home consumption demand. In June, system sales at existing stores fell 1.0% YoY (customer numbers down 7.3% YoY, average spending per customer down 6.8% YoY). In June 2019, anniversary menus commemorating KFC Japan's foundation day of July 4 sold well, with the promotion period lasting 23 days from June 12. However, system sales were lower YoY in June 2020 because the same promotion was limited to seven days from July 1 due to the COVID-19 pandemic (system sales at existing stores were up 27.3% YoY in July 2020). During the state of emergency when many food and beverage establishments had to close, KFC Japan was able to capture demand for deliveries and drive-through as part of its measures in response to the pandemic, on top of demand for takeout, which was already high. As at end-June 2020, the number of stores offering delivery services stood at 264, and those with drive-through services stood at approximately 400.

In Q1 FY03/21, gross profit was up 10.5% YoY to JPY8.6bn, and GPM was 43.5% (43.9% in Q1 FY03/20). The high GPM was linked to the ongoing reduction of losses from food disposal through efforts to refine sales forecasting. SG&A expenses rose 7.0% YoY to JPY7.3bn, and the SG&A expense ratio was 37.0% (38.5% in Q1 FY03/20). Higher sales variable expenses, delivery agent expenses, and renovation expenses were the main factors in SG&A expenses rising. Over the period, the company renovated 12 directly operated stores (+50% YoY) and 46 franchised stores (+35% YoY).

At equity-method affiliates (Bamboo [Thailand] Holding Pte. Ltd. and BYO Co., Ltd.), earnings deteriorated due to the impact from the spread of COVID-19, and the company recorded an equity-method investment loss of JPY764mn as a non-operating expense. JPY627mn of this was due to a reduction in the assessed fair value of Bamboo (Thailand) Holding Pte. Ltd. during a reassessment. As a result, net income decreased sharply. At BYO Co., Ltd., performance remains severe because business hours have been shortened to try and stem the spread of COVID-19.

System sales

In Q1 FY03/21, system sales (including franchises) were JPY32.0bn (+12.8% YoY), the highest level in Q1 for 28 years. This was owing to the success of the combination of value set menus to promote daily patronage and product initiatives to deliver pleasant surprise and enjoyment. Average monthly system sales per store at existing stores were up 21.1% YoY to JPY10.3mn, the highest level in 19 years.

Full-year FY03/20 results (out May 13, 2020)

Results summary

- FY03/20 results: FY03/20 revenues were JPY79.6bn (+7.1% YoY), operating profit was JPY4.8bn (2.2x the FY03/19 figure), and net income attributable to owners of the parent was JPY1.5bn (-25.4% YoY). In the mainstay KFC business, system sales at existing stores were up 10.1% YoY and strong throughout the year as the company stepped up measures to promote daily use. While revenues grew, the cost of revenues ratio improved due to a reduction in losses from food disposal and other factors. OPM was 6.0%, up from 3.0% in FY03/19. SG&A expenses rose only 1.1% YoY as a result of cost optimization efforts. On the other hand, the spread of COVID-19 led to a decline in business results of equity-method affiliates, and the company recorded an equity-method investment loss of JPY1.9bn as a non-operating expense, resulting in lower net income. The company will pay an annual dividend of JPY50 per share (dividend payout ratio of 72.9%) for FY03/20.
- System sales: In FY03/20, system sales (including franchises) were JPY128.8bn (+9.0% YoY). The combination of value measures to promote daily use (in the form of reasonably-priced set menus) and product measures to deliver pleasant surprise and enjoyment was successful. System sales were strong throughout the year, reaching the highest level in the last 27 years. System sales at existing stores were up 10.1% YoY. Although average spend per customer was flat YoY, a 10.1% increase in the total number of customers drove sales growth. The company opened seven directly operated stores and 12 franchised stores, bringing the total number of stores to 1,133 at end-FY03/20 (net increase of one store /+0.1% YoY). Renovations were carried out at 212 stores (+112 stores / 2.1x the FY03/19 figure), consisting of 46 directly operating stores and 166 franchised stores.

- ▷ In the second year of the medium-term management plan (FY03/19–FY03/21), the company took on activities to sustainably enhance brand value based on the three basic themes of 1) getting back to the roots of the business, 2) customer orientation (focus on frontline operations), and 3) the cultivation of human resources. In order to promote daily use, the company made efforts to concurrently appeal through value promotions (value packs) and new menu items, improved ease of purchase through online ordering and cashless payment support, and strengthened its delivery service. The company enhanced delivery services (including delivery agents), increasing the number of stores offering delivery to 220 as of end-March. As well as targeting customers who are unable to visit a store, the company worked to improve customer comfort when eating in-store through initiatives such as making all seats non-smoking (completed by the end of the previous year). Additionally, to enhance the value of the experience, the company implemented QSC (Quality, Service, Cleanliness) x H (Hospitality) and promoted the use of the official KFC app to foster customer loyalty through its reward program and coupons. App downloads have crossed the 1.5mn mark as of end-March 2020.
- ▷ Improved profitability: FY03/20 gross profit was JPY35.0bn (+9.1% YoY). GPM improved to 43.9% from 43.1% in FY03/19 on rising customer counts and sales, which made it possible to reduce losses from food disposal and increase store-level productivity. Although SG&A expenses increased by 1.1% YoY to JPY30.2bn, the SG&A expense ratio improved to 37.9% from 40.1% in FY03/19. Cost optimization efforts have taken effect.
- ▷ Full-year FY03/21 forecast: The company’s FY03/21 forecast is undetermined. This is due to the spread of COVID-19 making it difficult to perform reasonable forecast calculations. Following the government’s declaration of a state of emergency on April 7, 2020, the company temporarily closed some stores, shortened hours of operation, and suspended dine-in services in its mainstay KFC business. The company plans to disclose the forecast as soon as it can make reasonable calculations. In April 2020, total system sales were up 20.6% YoY (system sales at existing stores, excluding closed stores, were up 33.1% YoY).

FY03/20 results

In FY03/20, revenues were JPY79.6bn (+7.1% YoY), operating profit was JPY4.8bn (2.2x the FY03/19 figure), and net income attributable to owners of the parent was JPY1.5bn (-25.4% YoY). Revenues increased on the back of a promotional campaign calendar featuring a two-layer structure that interlocks product campaigns with value promotions throughout the year, and gross profit grew 9.1% YoY to JPY35.0bn, with the GPM improving to 43.9% from 43.1% in FY03/19. As a result of higher revenues and initiatives to ensure greater precision in sales forecast, losses from disposal of food decreased and the cost of revenues ratio improved. SG&A expenses increased 1.1% YoY to JPY30.2bn, mainly because of store refurbishments. In FY03/20 the company renovated 212 stores. This was 112 more than the 100 stores renovated in FY03/19, but whereas most of the prior-year refurbishments were major (including making all seats non-smoking), the majority of FY03/20 refurbishments were small in scale, including facelifts for aging stores and the replacement of fixtures. The SG&A expense ratio improved to 37.9% from 40.1% in FY03/19, and operating profit increased, thanks also to cost optimization efforts.

On the other hand, the spread of COVID-19 led to changes in consumers’ spending habits and store closures from April, as a result of which equity-method affiliates saw sales decrease and margins narrow. This led to the company recording a loss on equity-method investments of JPY1.9bn, with expansion in equity-method losses resulting in lower net income.

In Q4 FY03/20, revenues were JPY18.7bn (+6.4% YoY), operating profit was JPY530mn (9.6x the Q4 FY03/19 figure), and the company booked a net loss attributable to owners of the parent of JPY1.5bn (versus a JPY585mn profit in Q4 FY03/19). In Q4, too, the company captured different types of demand with the two-layer promotional campaigns and also with a two-layer approach consisting of group menus and individual meal menus. In terms of new offerings, the company launched Black Hot Chicken in January and the Quattro Cheese Sandwich in March. It also appealed to people holding gatherings with the JPY1,500 Share Box launched in March, where customers can choose two box types from an array of four. The company previously had rolled out a JPY500 lunch as a limited-time offer, and this was made a regular fixture on the menu from January. Thanks to the above initiatives, the company is progressively transforming its image from a brand strongly associated with special occasions such as Christmas to one also used on regular days, leading to increased customer traffic. In Q4, the GPM improved slightly to 44.1% from 44.0% in

Q4 FY03/19. SG&A expenses were up 0.7% YoY to JPY7.7bn, mostly because the company undertook renovations at 98 stores (including franchises), up from 36 in Q4 FY03/19. COVID-19 apparently had a minimal impact in Q4 FY03/20.

System sales

In FY03/20, system sales (including franchises) were JPY128.8bn (+9.0% YoY), reaching the highest level in the last 27 years. Q3 system sales were JPY36.7bn (+7.2% YoY) and system sales were upbeat in Q4 also, rising 8.6% YoY to JPY30.8bn. Clearly, the combination of value measures to promote daily use (in the form of reasonably-priced set menus) and product measures to deliver pleasant surprise and enjoyment was successful. Average monthly system sales at existing stores were up 10.1% YoY at JPY9.7mn, the highest level in the past 20 years.

News and topics

Other information

History

Date	Event
Mar 1970	KFC International opens test restaurant at Japan Expo, with daily sales of up to JPY2.8mn
Jul 1970	KFC Japan established in Shibuya, Tokyo with equal investments from Kentucky Fried Chicken Corporation and Mitsubishi Corporation and capital of JPY72mn
Nov 1970	First KFC restaurant in Japan opens in Nishi, Nagoya
Sep 1971	First KFC franchise opens in Enoshima
Jul 1972	Heublein Inc. buys Kentucky Fried Chicken Corporation
Oct 1982	R.J. Reynolds Industries Inc. buys Heublein Inc.
Oct 1986	PepsiCo Inc. buys Kentucky Fried Chicken Corporation from RJR Nabisco Inc.
Aug 1990	Lists on Tokyo Stock Exchange Second Section and increases capital to JPY7.3bn
Mar 1991	Establishes consolidated subsidiary K Ad
May 1991	Launches Pizza Hut business
Oct 1997	Food services business spun out from PepsiCo to establish Tricon Global Restaurants Inc. (currently Yum! Brands, Inc.)
Dec 2007	Mitsubishi Corporation becomes parent company after Yum! Brands, Inc. sells shares indirectly held in KFC Japan to Mitsubishi via public tender offer
Sep 2008	Consolidated subsidiary K Foods established
Apr 2013	Consolidated subsidiary Phoenix Foods established
May 2013	Consolidated subsidiaries K Dining Ltd. (new company name: Kentucky Fried Chicken Japan, Ltd.), Phoenix Ltd., and Natural Dining Ltd. established
Apr 2014	Name changed to KFC Holdings Japan Ltd. Restaurant operating company spun off and takes over 100% subsidiaries Kentucky Fried Chicken Japan, Ltd., Phoenix Ltd., and Natural Dining Ltd.
Nov 2015	Mitsubishi Corporation sells ordinary shares in the company and changes from parent company to other affiliated company
Aug 2016	Establishes investment holding company Fast Restaurant International Pte. Ltd. (FRI) as a consolidated subsidiary in Singapore. Invests in Bamboo (Thailand) Holding Pte. Ltd., which operates KFC restaurants in Thailand, through FRI.
June 2017	Sells and transfers all share of consolidated subsidiaries, Pizza Hut Japan Ltd. and Phoenix Foods Inc., to Endeavor United Partners Six, Co., Ltd.
Feb 2018	Entered capital and business alliance with BYO Co., Ltd.

Source: Shared Research based on company data

Relationship with Mitsubishi Corporation

In the 1960s, a manager in Mitsubishi Corporation's food business noticed that Kentucky Fried Chicken Corporation had a successful franchise business in the US and visited Colonel Harland Sanders on multiple occasions. Following four years of negotiations, he won the approval of Colonel Sanders in 1969 and a test restaurant was opened at the Osaka Expo in March 1970.

Following the success at the Osaka Expo, in July 1970 KFC Japan was established with equal investments from Mitsubishi and Kentucky Fried Chicken. Mitsubishi built a value chain from chicken feed through animal breeding and restaurant operations. Upstream is Mitsubishi's US subsidiary Agrex, Inc., a wholesaler of grains used in chicken feed, and on the downstream end is KFC Japan, which is responsible for restaurant operations.

In November 2015, Mitsubishi sold 627,000 of KFC Japan's ordinary shares. The aim was to improve the company's corporate value as increased liquidity of the shares led to an expanded investor base. Mitsubishi held a 65.86% stake of KFC Holdings Japan before the sale, and changed from being the parent company to a major shareholder (stake: 35.12% as of March 31, 2020).

However, Mitsubishi said it would continue to use its network of grain, chicken feed, and made-in-Japan chicken raised at designated KFC-accredited farms to support KFC Japan.

Corporate governance and top management

Corporate governance system (as of June 2021)

Capital structure	
Controlling shareholders	None
Foreign investor shareholding	Less than 10%
Organization and directors	
Organizational type	Company with audit and supervisory committee
Number of directors under Articles of Association	Upper limit on number of directors not specified
Number of directors	8
Directors' terms under Articles of Association	1 year
Chair of the Board of Directors	President
Number of external directors	4
Number of external directors designated as independent directors	3
Voluntary committee equivalent to Nomination Committee or Compensation Committee	In place
Number of members on Audit Committee	3
Number of external members on Audit Committee	3
Number of external Audit Committee members designated as independent Audit Committee members	3
Other	
Measures to provide incentives to directors	Performance linked compensation system in place
Stock-option grantees	None
Disclosure of directors' compensation	No individual compensation disclosure
Policy on determining amount of compensation and calculation methodology	In place
Corporate takeover defenses	None

Source: Shared Research based on company data

CEO Takayuki Hanji (born December 24, 1965)

Takayuki Hanji joined Mitsubishi Corporation in April 1988. He was assigned to MC Meats Holdings Pty. Ltd. in Australia in May 1996 and to the Feed, Meat & Livestock Dept. of Mitsubishi Corporation in February 1999. In April 2007, he became executive officer and general manager of the Corporate Planning Office and Products Unit at Kentucky Fried Chicken Japan, Ltd. In April 2016, he became manager of the Corporate Communications Dept. at Mitsubishi Corporation. He became director and managing executive officer of KFC Holdings Japan, Ltd. and Kentucky Fried Chicken Japan, Ltd. in June 2020. In June 2021, he was appointed to his current position of representative director and president of KFC Holdings and Kentucky Fried Chicken Japan.

Major shareholders (as of end-March 2021)

Top shareholders	Shares held ('000)	Shareholding ratio
Mitsubishi Corporation	7,875	35.12%
Custody Bank of Japan, Ltd. (Trust account)	350	1.56%
THE BANK OF NEW YORK MELLON 140044 (Standing proxy: Mizuho Bank, Ltd.)	194	0.86%
JP MORGAN CHASE BANK 385781 (Standing proxy: Mizuho Bank, Ltd.)	190	0.85%
STATE STREET BANK AND TRUST COMPANY 505103 (Standing proxy: Mizuho Bank, Ltd.)	189	0.84%
Japan KFC Holdings Franchise Owners Stockholding Association	173	0.77%
STATE STREET BANK WEST CLIENT – TREATY 505234 (Standing proxy: Mizuho Bank, Ltd.)	144	0.64%
MSCO CUSTOMER SECURITIES (Standing proxy: Morgan Stanley MUFG Securities Co., Ltd.)	123	0.55%
Meiji Yasuda Life Insurance Company (Standing proxy: Custody Bank of Japan, Ltd.)	110	0.49%
Custody Bank of Japan, Ltd. (Securities investment trust account)	99	0.44%

Source: Shared Research based on company data

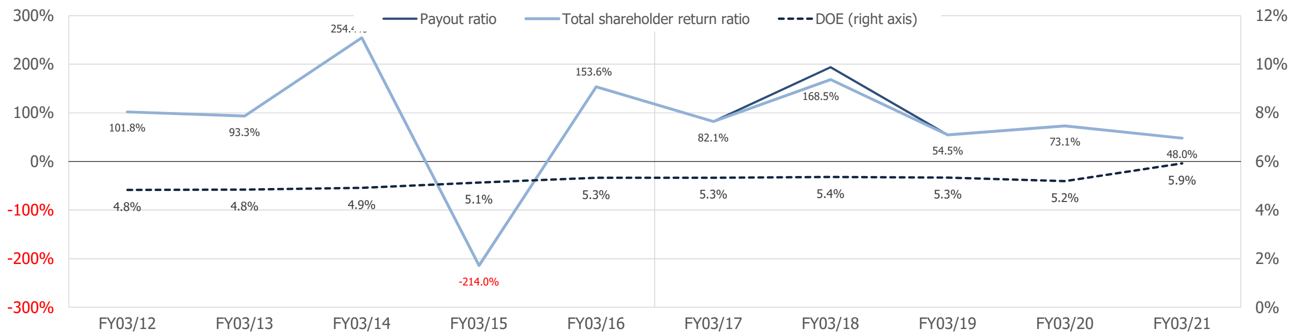
Principal group companies (as of March 2021)

Company	Location	Stake	Business description
Kentucky Fried Chicken Japan, Ltd.	Yokohama, Kanagawa Prefecture	100%	Operation of KFC restaurants
K Ad, Ltd.	Yokohama, Kanagawa Prefecture	100%	Advertising of KFC
K Foods, Ltd.	Osaka, Osaka Prefecture	100%	Operation of KFC restaurants
Fast Restaurant International Pte. Ltd.	Republic of Singapore	100%	Investment holding company

Source: Shared Research based on company data

Dividend policy

The company has a policy of paying out surplus funds as dividends twice a year, as interim and year-end dividends. Since FY03/12, it has maintained a stable annual dividend of JPY50 per share. The annual dividend was JPY60 per share in FY03/21 (JPY50 per share in ordinary dividend plus JPY10 per share in dividend to commemorate 50th anniversary; its initial dividend forecast was JPY50 per share). The company also presented shareholder benefits to mark its 50th anniversary.



Source: Shared Research based on company data

Employees

No. of employees (consolidated)	FY03/13	FY03/14	FY03/15	FY03/16	FY03/17	FY03/18	FY03/19	FY03/20	FY03/21
KFC	661	633	674	666	708	723	813	790	796
Pizza Hut	268	247	266	248	244	-	-	-	-
Other	17	17	14	134	111	104	-	-	-
Company-wide (common)	137	148	117	-	-	-	70	66	66
Total	1,083	1,045	1,071	1,048	1,063	827	883	856	862
No. of temporary workers (consolidated)	**FY03/13**	**FY03/14**	**FY03/15**	**FY03/16**	**FY03/17**	**FY03/18**	**FY03/19**	**FY03/20**	**FY03/21**
KFC	2,325	2,394	2,371	2,349	2,435	2,369	2,234	2,373	2,510
Pizza Hut	1,228	1,218	1,325	1,071	922	-	-	-	-
Other	57	59	97	24	16	12	-	-	-
Company-wide (common)	5	6	8	-	-	-	12	15	-
Total	3,615	3,677	3,801	3,444	3,373	2,381	2,246	2,388	2,510

Source: Shared Research based on company data

By the way

The story of Colonel Sanders

In 1930, Harland Sanders (Sanders was commissioned with the honorary title of Kentucky Colonel in 1935 by the state governor, and was henceforth known as Colonel Harland Sanders) opened a gas station in Corbin, Kentucky. At one side of the station, he started a restaurant with one table and six chairs. In 1939 Sanders perfected his “original-recipe chicken” recipe using 11 secret herbs and spices for fried chicken cooked with pure vegetable oil in a pressure cooker.

In 1952, he launched the franchise system that became the basis for the current KFC chain. He granted permission to use the Kentucky Fried Chicken brand to restaurant owners and in return received five cents in royalty for every chicken sold.

In 1964, he sold the franchise rights, which were bringing in USD300,000 annually, to future governor of Kentucky John Y. Brown, Jr. and Jack C. Massey. In his subsequent worldwide travels, he visited Japan three times and apparently confided to Roy Weston, then the chairman of KFC Japan that “Japanese fried chicken is my favorite.”

Profile

Company	**Head office**
KFC Holdings Japan, Ltd.	Yokohama i-MARK PLACE, 4-4-5 Minatomirai, Nishi-ku, Yokohama, Kanagawa
Phone	**Listed on**
+81-45-307-0700	Tokyo Stock Exchange 2nd section
Established	**Exchange listing**
July 4, 1970	August 21, 1990
Website	**Fiscal year-end**
-	March

About Shared Research Inc.

We offer corporate clients comprehensive report coverage, a service that allows them to better inform investors and other stakeholders by presenting a continuously updated third-party view of business fundamentals, independent of investment biases. Shared Research can be found on the web at https://sharedresearch.jp.

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Demae-Can CO., LTD
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Digital Garage Inc.
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en Japan Inc.
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Hope, Inc.
HOUSEDO Co., Ltd.
H2O Retailing Corporation
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IGNIS LTD.
i-mobile Co.,Ltd.
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Infocom Corporation
Infomart Corporation
Intelligent Wave, Inc.
ipet Holdings CO., Ltd.
Itochu Enex Co., Ltd.
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JMDC Inc.
JSB Co., Ltd.
JTEC Corporation
J Trust Co., Ltd
Japan Best Rescue System Co., Ltd.
JINS HOLDINGS Inc.
JP-HOLDINGS, INC.
KAMEDA SEIKA CO., LTD.
Kanamic Network Co.,LTD
KANEMATSU CORPORATION
kaonavi, inc.
KFC Holdings Japan, Ltd.
KI-Star Real Estate Co., Ltd.
KLab Inc.
Kondotec Inc.
Kumiai Chemical Industry Co., Ltd.
Lasertec Corporation
Locondo, Inc.
LUCKLAND CO., LTD.
Marumae Co., Ltd.
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MEDINET Co., Ltd.
MedPeer,Inc.
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Metaps Inc.
Micronics Japan Co., Ltd.
MIRAIT Holdings Corporation
Monex Goup Inc.
MORINAGA MILK INDUSTRY CO., LTD.
Mortgage Service Japan Limited.
MRT Inc.
NAGASE & CO., LTD
NAIGAI TRANS LINE LTD.
NanoCarrier Co., Ltd.
NEC Networks & System Integration Corporation
Net Marketing Co., Ltd.
Net One Systems Co.,Ltd.
Nichi-Iko Pharmaceutical Co., Ltd.
NIHON CHOUZAI Co.,Ltd.
Nihon Denkei Co., Ltd.
Nippon Commercial Development Co., Ltd.
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NIPPON PARKING DEVELOPMENT Co., Ltd.
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Nisso Corporation
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