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Yum China Holdings, Inc.
百勝中國控股有限公司

(Incorporated in the State of Delaware of the United States of America)
(Stock Code: 9987)

ANNUAL RESULTS ANNOUNCEMENT
FOR THE YEAR ENDED DECEMBER 31, 2023

Yum China Holdings, Inc. (the “Company” or “Yum China”) (NYSE: YUMC and HKEX: 9987) hereby announces the audited consolidated results of the Company for the year ended December 31, 2023 (the “Reporting Period”), together with the comparative audited figures for the corresponding period in 2022 and 2021, which have been prepared under generally accepted accounting principles in the United States (the “U.S. GAAP”) and reviewed by the audit committee (the “Audit Committee”) of the Board of Directors (the “Board” or “Directors”) of the Company.

By order of the Board
Yum China Holdings, Inc.
Joey WAT
Director and Chief Executive Officer

Hong Kong, February 29, 2024

As of the date of this announcement, the Board comprises Dr. Fred HU as the chairman and an independent director, Ms. Joey WAT as a director, and Mr. Peter A. BASSI, Mr. Edouard ETTEGGUI, Mr. David HOFFMANN, Ms. Ruby LU, Mr. Zili SHAO, Mr. William WANG, Ms. Min (Jenny) ZHANG and Ms. Christina Xiaojing ZHU as independent directors.

Key Financial and Operational Highlights

- **Total system sales** grew 21% excluding F/X. Growth was mainly attributable to 9% net new unit contribution, 7% same-store sales growth and lapping temporary closures from the pandemic in the prior year.
- Store count increased 13%, or 1,697 **net new stores**, exceeding the full-year net new store target. Total stores reached 14,644 in over 2,000 cities.
- **Total revenues** were up 15% to \$10.98 billion, or 21% excluding F/X.
- **Operating profit** grew 76% to \$1.1 billion. Adjusted operating profit grew 77% to \$1.1 billion. **Core operating profit** grew 79%.
- **Restaurant margin** expanded to 16.3%. Excluding items affecting comparability at the restaurant level, restaurant margin expanded 270 basis points.
- **Diluted EPS** increased by 89% to \$1.97. Excluding Special Items as well as unfavorable impacts of \$0.11 from F/X and \$0.04 from the mark-to-market investment in Meituan, the increase was 101%.
- Foreign currency translation unfavorably impacted total revenues by \$589 million, operating profit by \$61 million and diluted EPS by \$0.11.
- **Shareholder returns** through share repurchases and cash dividends increased 25% to \$833 million.
- **Digital sales** exceeded \$9.2 billion, with digital ordering accounted for approximately 89% of total company sales.
- **Total membership** of KFC and Pizza Hut exceeded 470 million, up 14% versus the prior year. Member sales accounted for approximately 65% of KFC and Pizza Hut's system sales in the aggregate.



Independent auditor’s report
to the stockholders of Yum China Holdings, Inc.
(incorporated in Delaware, United States of America)

Opinion

We have audited the consolidated financial statements of Yum China Holdings, Inc. (“Yum China”) and its subsidiaries (“the Company”) set out on pages 7 to 61, which comprise the consolidated balance sheet as at December 31, 2023, the consolidated statement of income, the consolidated statement of comprehensive income, the consolidated statement of equity and the consolidated statement of cash flows for the year then ended and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the consolidated financial statements give a true and fair view of the consolidated financial position of the Company as at December 31, 2023 and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with U.S. generally accepted accounting principles and have been properly prepared in compliance with the disclosure requirements of the Hong Kong Companies Ordinance.

Basis for opinion

We conducted our audit in accordance with Hong Kong Standards on Auditing (“HKSA”) issued by the HKICPA. Our responsibilities under those standards are further described in the *Auditor’s responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Company in accordance with the HKICPA’s *Code of Ethics for Professional Accountants* (“the Code”) and we have fulfilled our other ethical responsibilities in accordance with the Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters (continued)

Assessment of impairment of long-lived assets of restaurants	
<i>Refer to notes 7 and 11 to the consolidated financial statements on pages 29 to 31, pages 33 to 35, and the accounting policies on pages 16 to 17.</i>	
The Key Audit Matter	How the matter was addressed in our audit
<p>Property, plant and equipment, net and operating lease right-of-use assets were US\$2,310 million and US\$2,217 million, respectively, as of December 31, 2023, which included the long-lived assets of the Company's restaurants. For restaurant assets with indicators that the carrying value may not be recoverable, the Company evaluates the recoverability of these assets by comparing the forecasted undiscounted cash flows of the restaurant's operation to the carrying value of such assets. For restaurant assets that are not deemed to be recoverable, the Company writes down the restaurant assets to the estimated fair value. The Company determines the fair value of the restaurant assets based on the higher of the forecasted discounted cash flows of the restaurant's operation and the price market participants would pay to sub-lease the operating lease right-of-use assets and acquire the remaining restaurant assets.</p> <p>We identified the assessment of impairment of long-lived assets of restaurants as a key audit matter. A high degree of auditor judgment was required in assessing the sales growth rates used to estimate the forecasted undiscounted cash flows of the restaurants' operations. In addition, specialized skills and knowledge were needed to assess the Company's market rental assumptions to estimate the fair values of the operating lease right-of-use assets.</p>	<p>The following are the primary procedures we performed to address this key audit matter. We evaluated the design and tested the operating effectiveness of certain internal controls related to the Company's long-lived assets of restaurants impairment assessment process. This included controls related to the determination of the sales growth rates and the market rentals. To evaluate the sales growth rates, we compared the sales growth rates of a sample of restaurants to the historical sales growth rates and the Company's operation plans for the respective restaurants. We performed sensitivity analyses over the sales growth rates for a selection of restaurants to assess their impact on the restaurants' forecasted undiscounted cash flows. We involved valuation professionals with specialized skills and knowledge, who assisted in:</p> <ul style="list-style-type: none"> • Comparing the market rentals of a sample of restaurants to respective market rental ranges that we independently developed using external data; and • Developing independent estimates of the fair values of the operating lease right-of-use assets based on the price that market participants would pay to sub-lease the right-of-use assets for a sample of restaurants and comparing the results of our estimates to the Company's estimates.

Key audit matters (continued)

Evaluation of uncertain tax position	
<i>Refer to note 16 to the consolidated financial statements on pages 42 to 45 and the accounting policies on pages 18 to 19.</i>	
The Key Audit Matter	How the matter was addressed in our audit
<p>The Company recognizes the benefit of positions taken or expected to be taken in tax returns in the financial statements when it is more likely than not (more than a 50% likelihood) that the position would be sustained upon examination by tax authorities. Since 2016, the Company has been under a national audit on transfer pricing by the Chinese State Taxation Administration (“STA”) in China regarding the related party transactions for the period from 2006 to 2015.</p> <p>We identified the evaluation of the Company’s uncertain tax position pertaining to the transfer pricing used in the related party transactions under audit by the STA as a key audit matter. A high degree of auditor judgment and specialized skills and knowledge were required in evaluating the Company’s interpretation of the applicable tax laws and regulations and the estimate of the more likely than not assessment of tax position being sustained under examination by tax authorities.</p>	<p>The following are the primary procedures we performed to address this key audit matter. We evaluated the design and tested the operating effectiveness of the internal control related to the Company’s assessment process pertaining to the transfer pricing audit, including the control related to the interpretation of the applicable tax laws and regulations and the assessment of the uncertain tax position being sustained under examination by tax authorities. Since tax law is complex and often subject to interpretation, we involved tax professionals with specialized skills and knowledge, who assisted in:</p> <ul style="list-style-type: none">• Reading the correspondence received by the Company from the tax authorities in connection with the transfer pricing audit by the STA, as well as responses and information the Company submitted to the tax authorities;• Evaluating the Company’s identification and consideration of information that could significantly affect the recognition and measurement of the uncertain tax position; and• Evaluating the Company’s interpretation of applicable tax laws and regulations, technical analysis and the application of the accounting standards in assessing the recognition and measurement of the potential impact from the uncertain tax position.

Information other than the consolidated financial statements and auditor’s report thereon

The directors are responsible for the other information. The other information comprises all the information included in the annual report, other than the consolidated financial statements and our auditor’s report thereon.

Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

Responsibilities of the directors for the consolidated financial statements

The directors are responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with U.S. generally accepted accounting principles, and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Responsibilities of the directors for the consolidated financial statements (continued)

In preparing the consolidated financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the Company or to cease operations, or have no realistic alternative but to do so.

The directors are assisted by the Audit Committee in discharging their responsibilities for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. This report is made solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with HKSA's will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HKSA's, we exercise professional judgement and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the directors.
- Conclude on the appropriateness of the directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Company to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

Auditor's responsibility for the audit of the consolidated financial statements (continued)

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence and, where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated with the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor's report is Tse, Wong Pui.

KPMG
Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

29 February 2024

Consolidated Statements of Income

Yum China Holdings, Inc.

Years ended December 31, 2023, 2022 and 2021

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

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Revenues			
Company sales	\$ 10,391	\$ 9,110	\$ 8,961
Franchise fees and income	89	81	153
Revenues from transactions with franchisees	372	287	663
Other revenues	126	91	76
Total revenues	<u>10,978</u>	<u>9,569</u>	<u>9,853</u>
Costs and Expenses, Net			
Company restaurants			
Food and paper	3,224	2,836	2,812
Payroll and employee benefits	2,725	2,389	2,258
Occupancy and other operating expenses	2,752	2,604	2,664
Company restaurant expenses	<u>8,701</u>	<u>7,829</u>	<u>7,734</u>
General and administrative expenses	638	594	564
Franchise expenses	36	34	64
Expenses for transactions with franchisees	356	279	649
Other operating costs and expenses	112	78	65
Closures and impairment expenses, net	29	32	34
Other expenses (income), net	—	94	(643)
Total costs and expenses, net	<u>9,872</u>	<u>8,940</u>	<u>8,467</u>
Operating Profit	<u>1,106</u>	<u>629</u>	<u>1,386</u>
Interest income, net	169	84	60
Investment loss	<u>(49)</u>	<u>(26)</u>	<u>(54)</u>
Income Before Income Taxes and Equity in			
Net Earnings (Losses) from Equity Method Investments	1,226	687	1,392
Income tax provision	(329)	(207)	(369)
Equity in net earnings (losses) from equity method investments	<u>4</u>	<u>(2)</u>	<u>—</u>
Net income – including noncontrolling interests	901	478	1,023
Net income – noncontrolling interests	74	36	33
Net Income – Yum China Holdings, Inc.	<u>\$ 827</u>	<u>\$ 442</u>	<u>\$ 990</u>
Weighted-average common shares outstanding (in millions):			
Basic	416	421	422
Diluted	420	425	434
Basic Earnings Per Common Share	<u>\$ 1.99</u>	<u>\$ 1.05</u>	<u>\$ 2.34</u>
Diluted Earnings Per Common Share	<u>\$ 1.97</u>	<u>\$ 1.04</u>	<u>\$ 2.28</u>

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Comprehensive Income

Yum China Holdings, Inc.

Years ended December 31, 2023, 2022 and 2021

(in US\$ millions)

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Net income – including noncontrolling interests	\$ 901	\$ 478	\$ 1,023
Other comprehensive (loss) income, net of tax of nil			
Foreign currency translation adjustments	(146)	(431)	108
Comprehensive income – including noncontrolling interests	755	47	1,131
Comprehensive income (loss) – noncontrolling interests	54	(24)	40
Comprehensive Income – Yum China Holdings, Inc.	<u>\$ 701</u>	<u>\$ 71</u>	<u>\$ 1,091</u>

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

Yum China Holdings, Inc.

Years ended December 31, 2023, 2022 and 2021

(in US\$ millions)

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Cash Flows – Operating Activities			
Net income – including noncontrolling interests	\$ 901	\$ 478	\$ 1,023
Depreciation and amortization	453	602	516
Non-cash operating lease cost	404	435	424
Closures and impairment expenses	29	32	34
Gain from re-measurement of equity interest upon acquisition	—	—	(628)
Investment loss	49	26	53
Equity in net (earnings) losses from equity method investments	(4)	2	—
Equity income from investments in unconsolidated affiliates	—	—	(44)
Distributions of income received from equity method investments	11	7	32
Deferred income taxes	(10)	(20)	160
Share-based compensation expense	64	42	41
Changes in accounts receivable	(6)	(1)	(5)
Changes in inventories	(19)	(19)	(16)
Changes in prepaid expenses, other current assets and value-added tax assets	(35)	207	(72)
Changes in accounts payable and other current liabilities	84	16	118
Changes in income taxes payable	25	25	(26)
Changes in non-current operating lease liabilities	(407)	(396)	(461)
Other, net	(66)	(23)	(18)
Net Cash Provided by Operating Activities	<u>1,473</u>	<u>1,413</u>	<u>1,131</u>
Cash Flows – Investing Activities			
Capital spending	(710)	(679)	(689)
Purchases of short-term investments, long-term bank deposits and notes	(3,517)	(5,189)	(6,139)
Maturities of short-term investments, long-term bank deposits and notes	3,499	5,365	6,383
Acquisition of business, net of cash acquired	—	(23)	(115)
Acquisitions of equity investments	(20)	—	(300)
Other, net	5	4	5
Net Cash Used in Investing Activities	<u>(743)</u>	<u>(522)</u>	<u>(855)</u>
Cash Flows – Financing Activities			
Proceeds from short-term borrowings	264	2	—
Repayment of short-term borrowings	(100)	—	—
Repurchase of shares of common stock	(613)	(466)	(75)
Cash dividends paid on common stock	(216)	(202)	(203)
Dividends paid to noncontrolling interests	(77)	(72)	(57)
Acquisitions of noncontrolling interests	—	(113)	—
Contributions from noncontrolling interests	35	18	37
Payment of acquisition related holdback	(3)	(7)	(8)
Other, net	(6)	(4)	(7)
Net Cash Used in Financing Activities	<u>(716)</u>	<u>(844)</u>	<u>(313)</u>
Effect of Exchange Rates on Cash, Cash Equivalents and Restricted Cash	<u>(16)</u>	<u>(53)</u>	<u>15</u>
Net Decrease in Cash, Cash Equivalents and Restricted Cash	<u>(2)</u>	<u>(6)</u>	<u>(22)</u>
Cash, Cash Equivalents and Restricted Cash – Beginning of Year	<u>1,130</u>	<u>1,136</u>	<u>1,158</u>
Cash, Cash Equivalents and Restricted Cash – End of Year	<u><u>\$ 1,128</u></u>	<u><u>\$ 1,130</u></u>	<u><u>\$ 1,136</u></u>
Supplemental Cash Flow Data			
Cash paid for income tax	324	204	255
Cash paid for interest	3	—	—
Non-cash Investing and Financing Activities			
Capital expenditures included in accounts payable and other current liabilities	226	181	269

See accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

Yum China Holdings, Inc.
December 31, 2023 and 2022
(in US\$ millions)

	<u>2023</u>	<u>2022</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 1,128	\$ 1,130
Short-term investments	1,472	2,022
Accounts receivable, net	68	64
Inventories, net	424	417
Prepaid expenses and other current assets	339	307
Total Current Assets	<u>3,431</u>	<u>3,940</u>
Property, plant and equipment, net	2,310	2,118
Operating lease right-of-use assets	2,217	2,219
Goodwill	1,932	1,988
Intangible assets, net	150	159
Long-term bank deposits and notes	1,265	680
Equity investments	332	361
Deferred income tax assets	129	113
Other assets	265	248
Total Assets	<u><u>12,031</u></u>	<u><u>11,826</u></u>
LIABILITIES, REDEEMABLE NONCONTROLLING INTEREST AND EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	2,164	2,096
Short-term borrowings	168	2
Income taxes payable	90	68
Total Current Liabilities	<u>2,422</u>	<u>2,166</u>
Non-current operating lease liabilities	1,899	1,906
Non-current finance lease liabilities	44	42
Deferred income tax liabilities	390	390
Other liabilities	157	162
Total Liabilities	<u>4,912</u>	<u>4,666</u>
Redeemable Noncontrolling Interest	13	12
Equity		
Common stock, \$0.01 par value; 1,000 million shares authorized; 407 million shares and 419 million shares issued and outstanding at December 31, 2023 and 2022, respectively.	4	4
Additional paid-in capital	4,320	4,390
Retained earnings	2,310	2,191
Accumulated other comprehensive loss	(229)	(103)
Total Yum China Holdings, Inc. Stockholders' Equity	<u>6,405</u>	<u>6,482</u>
Noncontrolling interests	701	666
Total Equity	<u>7,106</u>	<u>7,148</u>
Total Liabilities, Redeemable Noncontrolling Interest and Equity	<u><u>\$ 12,031</u></u>	<u><u>\$ 11,826</u></u>

See accompanying Notes to Consolidated Financial Statements.

Notes to Consolidated Financial Statements

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

Note 1 – Description of Business

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

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

In 1987, KFC was the first major global restaurant brand to enter China. As of December 31, 2023, there were 10,296 KFC stores in China. We maintain a controlling interest of 58%, 70%, 83%, 92% and approximately 60% in the entities that own and operate the KFCs in and around Shanghai, Beijing, Wuxi, Suzhou and Hangzhou, respectively.

The first Pizza Hut in China opened in 1990. As of December 31, 2023, there were 3,312 Pizza Hut restaurants in China.

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

In 2017, the Company acquired a controlling interest in the holding company of DAOJIA.com.cn (“Daojia”), an online food delivery service provider in China. This business was extended to also include a team managing the delivery services for restaurants, including restaurants in our system, with their results reported under our delivery operating segment.

As part of our strategy to drive growth from off-premise occasions, we also developed our own retail brand operations, Shaofaner, which sells packaged foods through online and offline channels. The operating results of Shaofaner are included in our e-commerce business operating segment.

The Company has two reportable segments: KFC and Pizza Hut. Our non-reportable operating segments, including the operations of Lavazza, Huang Ji Huang, Little Sheep and Taco Bell, our delivery operating segment and our e-commerce business, are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in the aggregate. For 2022 and 2021, All Other Segments also included COFFii & JOY and East Dawning. The Company decided to wind down the operations of the East Dawning brand in 2021, and closed all stores by March 2022. In addition, the Company decided to wind down the operations of COFFii & JOY and closed all stores in 2022. Additional details on our segment reporting are included in Note 17.

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

Note 2 – Summary of Significant Accounting Policies

Our preparation of the accompanying Consolidated Financial Statements in conformity with Generally Accepted Accounting Principles in the United States of America ("GAAP") requires us to make estimates and assumptions that affect reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from these estimates. We have also prepared the Consolidated Financial Statements in accordance with the disclosure requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "Hong Kong Listing Rules") and the disclosure requirements of the Hong Kong Companies Ordinance (Cap.622 of the Laws of Hong Kong).

Basis of Preparation and Principles of Consolidation. Intercompany accounts and transactions have been eliminated in consolidation. We consolidate entities in which we have a controlling financial interest, the usual condition of which is ownership of a majority voting interest. We also consider consolidating an entity in which we have certain interests where the controlling financial interest may be achieved through arrangements that do not involve voting interests. Such an entity, known as a variable interest entity ("VIE"), is required to be consolidated by its primary beneficiary. The primary beneficiary is the entity that possesses the power to direct the activities of the VIE that most significantly impact its economic performance and has the obligation to absorb losses or the right to receive benefits from the VIE that are significant to it.

Our most significant variable interests are in entities that operate restaurants under franchise arrangements. We do not generally have an equity interest in our franchisee businesses. Additionally, we do not typically provide significant financial support such as loans or guarantees to our franchisees. We have variable interests in certain entities that operate restaurants under franchise agreements through real estate and property, plant and equipment ("PP&E") lease arrangements with them to which we are a party. At December 31, 2023, the Company had future lease payments due from franchisees, on a nominal basis, of approximately \$34 million. As our franchise arrangements provide our franchisee entities the power to direct the activities that most significantly impact their economic performance, we do not consider ourselves the primary beneficiary of any such entity that might otherwise be considered a VIE.

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

We consolidate the entities that operate KFCs in and around Shanghai, Beijing, Wuxi, Suzhou and Hangzhou, as well as the Lavazza joint venture where we have controlling interests since the respective acquisition dates (see Note 3 for additional information). We refer to these joint ventures that operate our concepts as former unconsolidated affiliates before the acquisitions. As a result of the acquisitions of all former unconsolidated affiliates by December 2021, the Company consolidated their results since their respective acquisition dates, and therefore we no longer have franchise fees and expenses from and revenues and expenses from transactions with former unconsolidated affiliates for years ended December 31, 2023 and 2022.

Comparative Information. Certain comparative items in the Consolidated Financial Statements have been reclassified to conform to the current year's presentation to facilitate comparison.

Fiscal Calendar. Our fiscal year ends on December 31, with each quarter comprised of three months.

Foreign Currency. Our functional currency for the operating entities in China is the Chinese Renminbi (“RMB”), the currency of the primary economic environment in which they operate. Income and expense accounts for our operations are then translated into U.S. dollars at the average exchange rates prevailing during the period. Assets and liabilities are then translated into U.S. dollars at exchange rates in effect at the balance sheet date. Foreign currency translation adjustments are recorded in the Accumulated other comprehensive income on the Consolidated Balance Sheets. Gains and losses arising from the impact of foreign currency exchange rate fluctuations on transactions in foreign currency, to the extent they arise, are included in Other expenses (income), net in our Consolidated Statements of Income.

Franchise Operations. We execute agreements which set out the terms of our arrangement with franchisees. Our franchise agreements typically require the franchisee to pay an initial, non-refundable fee and continuing fees based upon a percentage of sales. Subject to our approval and their payment of a renewal fee, a franchisee may generally renew the franchise agreement upon its expiration.

The 3% license fees we pay to YUM for the right to sublicense the KFC, Pizza Hut and Taco Bell intellectual property to franchisees and former unconsolidated affiliates that operate our concepts are recorded in Franchise expenses. License fees due to YUM for our Company-owned stores are included in Occupancy and other operating expenses. Total license fees paid to YUM were \$317 million, \$277 million and \$298 million during the years ended December 31, 2023, 2022 and 2021, respectively.

Certain direct costs of our franchise operations are charged to Franchise expenses. These costs include provisions for estimated uncollectible fees, rent or depreciation expense associated with restaurants we sub-lease to franchisees, and certain other direct incremental franchise support costs.

We also have certain transactions with franchisees and former unconsolidated affiliates that operate our concepts, which consist primarily of sales of food and paper products, advertising services, delivery services and other services. Related expenses are included in Expenses for transactions with franchisees.

Revenue Recognition. The Company’s revenues include Company sales, Franchise fees and income, Revenues from transactions with franchisees, and Other revenues.

Company Sales

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

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

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

Franchise Fees and Income

Franchise fees and income primarily include upfront franchise fees, such as initial fees and renewal fees, and continuing fees. We have determined that the services we provide in exchange for upfront franchise fees and continuing fees are highly interrelated with the franchise right. We recognize upfront franchise fees received from a franchisee as revenue over the term of the franchise agreement or the renewal agreement because the franchise rights are accounted for as rights to access our symbolic intellectual property. The franchise agreement term is generally 10 years for KFC and Pizza Hut, generally five years for Little Sheep and three to 10 years for Huang Ji Huang. We recognize continuing fees, which are based upon a percentage of franchisee sales, as those sales occur. During 2021, it also includes franchise fees and income from former unconsolidated affiliates that operate our concepts before acquisition.

Revenues from Transactions with Franchisees

Revenues from transactions with franchisees consist primarily of sales of food and paper products, advertising services, delivery services and other services provided to franchisees. During 2021, it also includes revenues from transactions with former unconsolidated affiliates that operate our concepts before acquisition.

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

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

Other Revenues

Other revenues primarily include i) sales of products to customers through e-commerce channels, sales of Lavazza coffee retail products beyond Lavazza coffee shops, and sales of our seasoning products to distributors, and ii) revenues from logistics and warehousing services provided to third parties through our supply chain network. Our segment disclosures also include revenues relating to delivery services that were provided to our Company-owned restaurants and, therefore, were eliminated for consolidation purposes.

Other revenues are recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products or services.

Loyalty Programs

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

Direct Marketing Costs. We charge direct marketing costs to expense ratably in relation to revenues over the year in which incurred and, in the case of advertising production costs, in the year the advertisement is first shown. Deferred direct marketing costs, which are classified as prepaid expenses, consist of media and related advertising production costs which will generally be used for the first time in the next fiscal year and have historically not been significant. Our direct marketing expenses incurred for Company-owned restaurants were \$374 million, \$343 million and \$368 million in 2023, 2022 and 2021, respectively, and were included in Occupancy and other operating expenses. In addition, the direct marketing costs incurred for franchisees and former unconsolidated affiliates were \$25 million, \$23 million and \$55 million in 2023, 2022 and 2021, respectively, and were recorded in Expenses for transactions with franchisees.

Research and Development Expenses. Research and development expenses associated with our food innovation activities, which are expensed as incurred, are reported in general and administrative ("G&A") expenses. Research and development expenses were \$6 million in each of 2023, 2022 and 2021.

Share-Based Compensation. We recognize all share-based payments to employees and directors, including grants of stock options, restricted stock units ("RSUs"), stock appreciation rights ("SARs") and performance share units ("PSUs"), in the Consolidated Financial Statements as compensation cost over the service period based on their fair value on the date of grant. This compensation cost is recognized over the service period on a straight-line basis, net of an assumed forfeiture rate, for awards that actually vest and when performance conditions are probable of being achieved, if applicable. Forfeiture rates are estimated at grant date based on historical experience and compensation cost is adjusted in subsequent periods for differences in actual forfeitures from the previous estimates. We present this compensation cost consistent with the other compensation costs for the employee recipient in either payroll and employee benefits or G&A expenses.

Impairment or Disposal of Long-Lived Assets. Long-lived assets, primarily PP&E and operating lease right-of-use ("ROU") assets are tested for impairment whenever events or changes in circumstances indicate that the carrying value of the assets may not be recoverable. The assets are not recoverable if their carrying value is higher than the undiscounted cash flows we expect to generate from such assets. If the assets are not deemed to be recoverable, impairment is measured based on the excess of their carrying value over their fair value.

For purposes of impairment testing for our restaurants, we have concluded that an individual restaurant is the lowest level of independent cash flows unless our intent is to rebrand restaurants as a group. We review our long-lived assets of such individual restaurants (primarily operating lease ROU assets and PP&E) semi-annually for impairment, or whenever events or changes in circumstances indicate that the carrying amount of a restaurant may not be recoverable. Our primary indicators of potential impairment for our semi-annual impairment testing of these restaurant assets include two consecutive years of operating losses after a restaurant has been open for three years. We evaluate the recoverability of these restaurant assets by comparing the forecasted undiscounted cash flows of the restaurant's operation, which are based on our entity-specific assumptions, to the carrying value of such assets. The forecasted undiscounted cash flows incorporate our best estimate of sales growth based upon our operation plans for the unit and actual results at comparable restaurants. For restaurant assets that are not deemed to be recoverable, we write down an impaired restaurant to its estimated fair value, which becomes its new cost basis. Fair value is an estimate of the price market participants would pay for the restaurant and its related assets. In determining the fair value of restaurant-level assets, we considered the highest and best use of the assets from market participants' perspective, which is represented by the higher of the forecasted discounted cash flows from operating restaurants and the price market participants would pay to sub-lease the operating lease ROU assets and acquire remaining restaurant assets, even if that use differs from the current use by the Company. The after-tax cash flows incorporate reasonable assumptions we believe a franchisee would make such as sales growth and include a deduction for royalties we would receive under a franchise agreement with terms substantially at market. The discount rate used in the fair value calculation is our estimate of the required rate-of-return that a franchisee would expect to receive when purchasing a similar restaurant and the related long-lived assets. The discount rate incorporates rates of returns for historical rebranding market transactions and is commensurate with the risks and uncertainty inherent in the forecasted cash flows. Estimates of the price market participants would pay to sub-lease the operating lease ROU assets are based on comparable market rental information that could be reasonably obtained for the property. In situations where the highest and best use of the restaurant-level assets from market participants' perspective is represented by sub-leasing the operating lease ROU assets and acquiring remaining restaurant assets, the Company continues to use these assets in operating its restaurant business, which is consistent with its long-term strategy of growing revenue through operating restaurant concepts.

When we believe it is more likely than not a restaurant or groups of restaurants will be rebranded for a price less than their carrying value, but do not believe the restaurant(s) have met the criteria to be classified as held for sale, we review the restaurants for impairment. We evaluate the recoverability of these restaurant assets by comparing estimated sales proceeds plus holding period cash flows, if any, to the carrying value of the restaurant or group of restaurants. For restaurant assets that are not deemed to be recoverable, we recognize impairment for any excess of carrying value over the fair value of the restaurants, which is based on the expected net sales proceeds. To the extent ongoing agreements to be entered into with the franchisee simultaneous with the rebranding are expected to contain terms, such as royalty rates, not at prevailing market rates, we consider the off-market terms in our impairment evaluation. We recognize any such impairment charges in Rebranding gain. Rebranding gain includes the gains or losses from the sales of our restaurants to new and existing franchisees, including any impairment charges discussed above. We recognize gains on restaurant rebranding when the sale transaction closes, the franchisee has a minimum amount of the purchase price in at-risk equity and we are satisfied that the franchisee can meet its financial obligations.

When we decide to close a restaurant, it is reviewed for impairment, and depreciable lives are adjusted based on the expected disposal date. Other costs incurred when closing a restaurant such as costs of disposing of the assets as well as other facility-related expenses are generally expensed as incurred. Additionally, at the time we decide to close a restaurant, we reassess whether it is reasonably certain that we will exercise the termination option, and remeasure lease liability to reflect changes in lease term and remaining lease payments based on the planned exit date, if applicable. The amount of the re-measurement of the lease liability is recorded as an adjustment to the operating lease ROU asset first, with any remaining amount recorded in Closures and impairment expenses if the carrying amount of the operating lease ROU asset is reduced to zero. Any costs recorded upon store closure as well as any subsequent adjustments to remaining operating lease ROU assets and lease liabilities as a result of lease termination are recorded in Closures and impairment expenses. In the event we are forced to close a store and receive compensation for such closure, that compensation is recorded in Closures and impairment expenses. To the extent we sell assets associated with a closed store, any gain or loss upon that sale is also recorded in Closures and impairment expenses.

Considerable management judgment is necessary to estimate future cash flows, including cash flows from continuing use, terminal value, lease term and rebranding proceeds. Accordingly, actual results could vary significantly from our estimates.

Government Subsidies. Government subsidies generally consist of financial subsidies received from provincial and local governments for operating a business in their jurisdictions and compliance with specific policies promoted by the local governments. The eligibility to receive such benefits and amount of financial subsidy to be granted are determined at the discretion of the relevant government authorities. Government subsidies are recognized when it is probable that the Company will comply with the conditions attached to them, and the subsidies are received. If the subsidy is related to an expense item, it is recognized as a reduction to the related expense to match the subsidy to the costs that it is intended to compensate. If the subsidy is related to an asset, it is deferred and recorded in Other liabilities and then recognized ratably over the expected useful life of the related asset in the Consolidated Statements of Income. The balances of deferred government subsidies included in Other liabilities were immaterial as of both December 31, 2023 and 2022. There were no significant commitment or contingencies for the government subsidies received for the years ended December 31, 2023, 2022 and 2021.

Government subsidies in the form of cash were recognized as reduction in following expense line items in our Consolidated Statements of Income as follows:

Costs and Expenses, Net	<u>2023</u>	<u>2022</u>	<u>2021</u>
Company restaurant			
Payroll and employee benefits ^(a)	\$ 7	\$ 15	\$ 14
Occupancy and other operating expenses	<u>1</u>	<u>3</u>	<u>3</u>
Company restaurant expenses	8	18	17
General and administrative expenses	<u>22</u>	<u>26</u>	<u>28</u>
Total	<u>\$ 30</u>	<u>\$ 44</u>	<u>\$ 45</u>

- (a) This primarily represents government subsidies for employee benefits and providing training to employees, with higher amounts received during 2022 and 2021, the years impacted by the COVID-19 pandemic.

Based on the policy related to COVID-19 issued in 2020 on reducing enterprise social security contribution, the Company also recorded one-time relief of \$33 million during 2022, which were recognized as a reduction to the Company restaurant expenses and G&A expenses.

Income Taxes. We record deferred tax assets and liabilities for the future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases as well as operating loss, capital loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those differences or carryforwards are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Additionally, in determining the need for recording a valuation allowance against the carrying amount of deferred tax assets, we consider the amount of taxable income and periods over which it must be earned, actual levels of past taxable income and known trends and events or transactions that are expected to affect future levels of taxable income. Where we determine that it is more likely than not that all or a portion of an asset will not be realized, we record a valuation allowance.

We are subject to reviews, examinations and audits by Chinese tax authorities, the IRS and other taxing authorities with respect to income and non-income based taxes. We recognize the benefit of positions taken or expected to be taken in our tax returns when it is more likely than not that the position would be sustained upon examination by these tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. We evaluate unrecognized tax benefits, including interest thereon, on a quarterly basis to ensure that they have been appropriately adjusted for events, including change or developments with respect to tax audits, audit settlements and expiration of the statute of limitation, which may impact our ultimate payment for such exposures.

We have investments in our foreign subsidiaries where the carrying values for financial reporting exceed the tax basis. Except for the planned but yet to be distributed earnings, we have not provided deferred tax on the portion of the excess that we believe is indefinitely reinvested, as we have the ability and intent to indefinitely postpone the basis differences from reversing with a tax consequence. The Company's separation from YUM was intended to qualify as a tax-free reorganization for U.S. income tax purposes resulting in the excess of financial reporting basis over tax basis in our investment in the China business continuing to be indefinitely reinvested. The excess of financial reporting basis over tax basis as of December 31, 2017 was subject to the one-time transition tax under the Tax Cuts and Jobs Act ("Tax Act") as a deemed repatriation of accumulated undistributed earnings from the foreign subsidiaries. However, we continue to believe that the portion of the excess of financial reporting basis over tax basis (including earnings and profits subject to the one-time transition tax) is indefinitely reinvested in our foreign subsidiaries for foreign withholding tax purposes.

Pursuant to the China Enterprise Income Tax Law (“EIT Law”), a 10% PRC withholding tax is generally levied on dividends declared by companies in China to their non-resident enterprise investors unless otherwise reduced according to treaties or arrangements between the Chinese central government and the governments of other countries or regions where the non-China resident enterprises are incorporated. Hong Kong has a tax arrangement with mainland China that provides for a 5% withholding tax on dividends distributed to a Hong Kong resident enterprise, upon meeting certain conditions and requirements, including, among others, that the Hong Kong resident enterprise own at least 25% equity interest of the Chinese enterprise and is a “beneficial owner” of the dividends. We believe that our principal Hong Kong subsidiary, which is the equity holder of our Chinese subsidiaries operating substantially all of our KFC and Pizza Hut restaurants, met the relevant requirements pursuant to the tax arrangement between mainland China and Hong Kong in 2018 and is expected to meet the requirements in the subsequent years; thus, it is more likely than not that our dividends or earnings expected to be repatriated to our principal Hong Kong subsidiary since 2018 are subject to the reduced withholding tax of 5%.

See Note 16 for a further discussion of our income taxes.

Fair Value Measurements. Fair value is the price we would receive to sell an asset or pay to transfer a liability (exit price) in an orderly transaction between market participants. For those assets and liabilities we record or disclose at fair value, we determine fair value based upon the quoted market price, if available. If a quoted market price is not available for identical assets, we determine fair value based upon the quoted market price of similar assets or the present value of expected future cash flows considering the risks involved, including counterparty performance risk if appropriate, and using discount rates appropriate for the duration. The fair values are assigned a level within the fair value hierarchy, depending on the source of the inputs into the calculation.

Level 1 Inputs based upon quoted prices in active markets for identical assets.

Level 2 Inputs other than quoted prices included within Level 1 that are observable for the asset, either directly or indirectly.

Level 3 Inputs that are unobservable for the asset.

In addition, when we acquire additional equity interest in the unconsolidated affiliates to obtain control, it may result in gain or loss from re-measurement of our previously held equity interest at fair value using a discounted cash flow valuation approach and incorporating assumptions and estimates that are Level 3 inputs. Key assumptions used in estimating future cash flows included projected revenue growth and costs and expenses, which were based on internal projections, store expansion plans, historical performance of stores and the business environment, as well as the selection of an appropriate discount rate based on the weighted-average cost of capital which includes company-specific risk premium.

Cash and Cash Equivalents. Cash equivalents represent highly liquid investments with original maturities not exceeding three months and are primarily comprised of time deposits, fixed income debt securities and money market funds. Cash and overdraft balances that meet the criteria for right to offset are presented net on our Consolidated Balance Sheets. See Note 12 for detail discussion on our Cash equivalents.

Short-term Investments. Short-term investments purchased primarily represent i) time deposits, fixed income debt securities with original maturities of over three months but less than one year when purchased; ii) time deposits with original maturities over one year but are expected to be realized in cash during the next 12 months; iii) variable return investments offered by financial institutions measured at fair value; and iv) certain structured deposits that are principal-protected and provide returns in the form of both fixed and variable interests with original maturities of less than one year. Such variable interest rates indexed to gold prices or foreign exchange rates are considered embedded derivatives and bifurcated from host contracts, and measured at fair value on a recurring basis. The fair value change of the embedded derivatives is recorded in Investment gain or loss in the Consolidated Statements of Income. The remaining host contracts to receive guaranteed principal and fixed interest are measured at amortized cost, with accretion of interest recorded in Interest income, net in the Consolidated Statements of Income. As of December 31, 2023 and 2022, the fair value of embedded derivatives included in Short-term investments was immaterial. See Note 12 for detail discussion on our Short-term investments.

Long-term Bank Deposits and Notes. Long-term bank deposits and notes represent time deposits and bank notes bearing fixed interest rate with remaining maturities exceeding one year for which the Company has the positive intent to hold for more than one year. See Note 12 for detail discussion on our Long-term bank deposits and notes.

Accounts Receivable. Accounts receivable primarily consist of trade receivables and royalties from franchisees, and are generally due within 30 days of the period in which the corresponding sales occur. Our provision of credit losses for accounts receivable is based upon the current expected credit losses ("CECL") model. The CECL model requires an estimate of the credit losses expected over the life of accounts receivable since initial recognition, and accounts receivable with similar risk characteristics are grouped together when estimating CECL. In assessing the CECL, the Company considers both quantitative and qualitative information that is reasonable and supportable, including historical credit loss experience, adjusted for relevant factors impacting collectability and forward-looking information indicative of external market conditions. While we use the best information available in making our determination, the ultimate recovery of recorded receivables is also dependent upon future economic events and other conditions that may be beyond our control. Accounts receivable that are ultimately deemed to be uncollectible, and for which collection efforts have been exhausted, are written off against the allowance for doubtful accounts. As of December 31, 2023 and 2022, the ending balances of provision for accounts receivable were \$1 million and \$2 million, respectively, and amounts of accounts receivable past due were immaterial.

Receivables from Payment Processors or Aggregators. Receivables from payment processors such as WeChat and Alipay or aggregators including delivery aggregators and third-party e-commerce platforms are cash due from them for clearing transactions and are included in Prepaid expenses and other current assets. The cash was paid by customers through these payment processors or aggregators for food provided or coupons sold by the Company. The Company considers and monitors the credit worthiness of the third-party payment processors and aggregators used. We adopted the same methodology of estimating expected credit losses based upon the CECL model as described above. Receivable balances are written off after all collection efforts have been exhausted. As of December 31, 2023 and 2022, no allowance for doubtful accounts was provided for such receivables.

Inventories. We value our inventories at the lower of cost (computed on the first-in, first-out method) or net realizable value.

Property, Plant and Equipment. We state PP&E at cost less accumulated depreciation and amortization. We calculate depreciation and amortization on a straight-line basis over the estimated useful lives of the assets as follows: generally 20 to 50 years for buildings, the lesser of estimated useful lives (generally 5 to 12 years) and remaining lease term for leasehold improvements, 3 to 10 years for restaurant machinery and equipment and 3 to 5 years for capitalized software costs. We suspend depreciation and amortization on assets related to restaurants that are held for sale. The useful life of PP&E is periodically reviewed.

We capitalize direct costs associated with the site acquisition and construction of a Company unit on that site, including direct internal payroll and payroll-related costs. Only those site-specific costs incurred subsequent to the time that the site acquisition is considered probable are capitalized. If we subsequently make a determination that it is probable a site for which internal development costs have been capitalized will not be acquired or developed, any previously capitalized internal development costs are expensed and included in G&A expenses.

We capitalize software costs incurred in connection with developing or obtaining computer software for internal use. We capitalize payroll and payroll-related costs for employees that are directly attributable to the development of our internal-use software. Internal costs incurred in the software application development stage are capitalized and amortized over the estimated useful lives of software. Costs associated with planning and post-implementation operation and software maintenance costs are expensed and included in G&A expenses.

Leases. ROU assets and lease liabilities are recognized upon lease commencement for operating leases based on the present value of lease payments over the lease term. As the rate implicit in the lease cannot be readily determined, we use our incremental borrowing rate at the lease commencement date in determining the imputed interest and present value of lease payments. The incremental borrowing rate was determined using a portfolio approach based on the rate of interest that we would have to borrow an amount equal to the lease payments on a collateralized basis over a similar term. The incremental borrowing rate is primarily influenced by the risk-free interest rate of China, the Company's credit rating and lease term, and is updated on a quarterly basis for measurement of new lease liabilities.

For operating leases, the Company recognizes a single lease cost on a straight-line basis over the remaining lease term. For finance leases, the Company recognizes straight-line amortization of the ROU asset and interest on the lease liability. For rental payments either based on a percentage of the restaurant's sales in excess of a fixed base amount or solely based on a percentage of the restaurant's sales, they are recognized as variable lease expenses as incurred.

The Company has elected not to recognize ROU assets or lease liabilities for leases with an initial term of 12 months or less; we recognize lease expense for these leases on a straight-line basis over the lease term. In addition, the Company has elected not to separate non-lease components (e.g., common area maintenance fees) from the lease components.

From time to time, we purchase the rights to use government-owned land and the building occupying the land for a fixed period of time. Prior to the adoption of Accounting Standards Update No. 2016-02, *Leases (Topic 842)* (“ASC 842”), these land use rights and related buildings were recorded in Other Assets and Property, Plant and Equipment in our Consolidated Balance Sheets, and are amortized on a straight-line basis over the term of the land use rights. Upon the adoption of ASC 842 on January 1, 2019, land use rights acquired are assessed in accordance with ASC 842 and recognized in ROU assets if they meet the definition of lease.

See Note 11 for further discussions on our leases.

Goodwill and Intangible Assets. From time to time, the Company acquires restaurants from our existing franchisees or acquires another business, including restaurants business of unconsolidated affiliates that operate our concepts. Goodwill from these acquisitions represents the excess of the cost of a business acquired over the net of the amounts assigned to assets acquired, including identifiable intangible assets and liabilities assumed. Goodwill is not amortized and has been assigned to reporting units for purposes of impairment testing. Our reporting units are our individual operating segments.

We evaluate goodwill for impairment on an annual basis or more often if an event occurs or circumstances change that indicate impairment might exist. We have selected the beginning of our fourth quarter as the date on which to perform our ongoing annual impairment test for goodwill. We may elect to perform a qualitative assessment for our reporting units to determine whether it is more likely than not that the fair value of the reporting unit is greater than its carrying value. If a qualitative assessment is not performed, or if as a result of a qualitative assessment it is not more likely than not that the fair value of a reporting unit exceeds its carrying value, then the reporting unit’s fair value is compared to its carrying value. Fair value is the price a willing buyer would pay for a reporting unit, and is generally estimated using discounted expected future after-tax cash flows from the business operation of the reporting unit. The discount rate is our estimate of the required rate-of-return that a third-party buyer would expect to receive when purchasing a business from us that constitutes a reporting unit. We believe the discount rate is commensurate with the risks and uncertainty inherent in the forecasted cash flows. If the carrying value of a reporting unit exceeds its fair value, we will record an impairment charge based on that difference. The impairment charge will be limited to the amount of goodwill allocated to that reporting unit.

If we record goodwill upon acquisition of a restaurant(s) from a franchisee and such restaurant(s) is then sold within two years of acquisition, the goodwill associated with the acquired restaurant(s) is written off in its entirety. If the restaurant is franchised two years or more subsequent to its acquisition, we include goodwill in the carrying amount of the restaurants disposed of based on the relative fair values of the portion of the reporting unit disposed of in the franchising and the portion of the reporting unit that will be retained.

We determine the useful life of intangible assets with consideration of factors including the expected use of the asset, the expected useful life of another asset or a group of assets to which the useful life of the intangible asset may relate, any legal, regulatory or contractual provisions that may limit the useful life, our historical experience in renewing or extending similar arrangements, the effects of obsolescence, demand, competition and other economic factors, and the level of maintenance expenditures required to obtain the expected future cash flows from the assets. We evaluate the remaining useful life of an intangible asset that is not being amortized each reporting period to determine whether events and circumstances continue to support an indefinite useful life. If an intangible asset that is not being amortized is subsequently determined to have a finite useful life, we amortize the intangible asset prospectively over its estimated remaining useful life. The Company’s indefinite-lived intangible asset represents Little Sheep and Huang Ji Huang trademarks as we consider their useful life to be indefinite since we intend to use Little Sheep and Huang Ji Huang trademarks indefinitely and there are no legal, regulatory or contractual provisions that may limit the useful life of the trademarks. Intangible assets that are deemed to have a finite life are generally amortized over their estimated useful lives on a straight-line basis to their residual value as follows:

Reacquired franchise rights	1 to 10 years
Huang Ji Huang franchise related assets	19 years
Daojia platform	8 years
Customer-related assets	2 to 15 years
Others	up to 20 years

The useful life of reacquired franchise rights was determined based on the contractual term whereas both the contractual term and historical pattern of renewing franchise agreements were considered in assessing the useful life of Huang Ji Huang franchise related assets. Customer-related assets primarily represent the customer relationship and user base acquired and the estimate of the useful life was based on the historical pattern of extending similar arrangements and attrition rate of users. Others primarily represent Little Sheep's secret recipe. The useful life of the Daojia platform and Little Sheep's secret recipe was assessed based on our estimate of periods generating cash flows from utilizing such assets.

We evaluate our indefinite-lived intangible assets for impairment on an annual basis or more often if an event occurs or circumstances change that indicate impairments might exist. We perform our annual test for impairment of our indefinite-lived intangible assets at the beginning of our fourth quarter. We may elect to perform a qualitative assessment to determine whether it is more likely than not that the fair value of an indefinite-lived intangible asset is greater than its carrying value. If a qualitative assessment is not performed, or if as a result of a qualitative assessment it is not more likely than not that the fair value of an indefinite-lived intangible asset exceeds its carrying value, then the asset's fair value is compared to its carrying value. Fair value is an estimate of the price a willing buyer would pay for the intangible asset and is generally estimated by discounting the expected future after-tax cash flows associated with the intangible asset.

Our finite-lived intangible assets that are not allocated to an individual restaurant are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable. An intangible asset that is deemed not recoverable based on forecasted undiscounted future cash flow is written down to its estimated fair value, which is our estimate of the price a willing buyer would pay for the intangible asset based on discounted expected future after-tax cash flows. For purposes of our impairment analysis, we update the cash flows that were initially used to value the finite-lived intangible asset to reflect our current estimates and assumptions over the asset's future remaining life.

Equity Investments. The Company's equity investments include investments in equity method investees and investments in equity securities with readily determinable fair value.

The Company applies the equity method to account for the investments in equity method investees over which it has significant influence but does not control. Our share of earnings or losses and share of changes in other comprehensive income or losses of equity method investees is included in net income and other comprehensive income or losses, respectively. We record impairment charges related to an investment in equity method investees whenever events or circumstances indicate that a decrease in the fair value of an investment has occurred which is other than temporary. Management's assessment as to the nature of a decline in fair value is based on, among other things, the length of time and the extent to which the market value has been less than our cost basis; the financial condition and near-term prospects of the equity method investees; and our intent and ability to retain the investment for a period of time sufficient to allow for any anticipated recovery in market value.

For our investments in equity securities with readily determinable fair value, over which the Company has neither significant influence nor control, they are measured at fair value with subsequent changes recognized in net income.

See Note 3 and Note 7 for further discussions on our equity investments.

Short-term Borrowings. Borrowings are recognized initially at fair value, net of debt discounts or premiums and debt issuance costs, if applicable. Debt discounts or premiums and debt issuance costs are recorded as an adjustment to the principal amount and the related accretion is amortized into interest expense in the Consolidated Statements of Income over the term of the borrowings using the effective interest method. Borrowings are subsequently measured at amortized cost. Interest expense is recognized over the term of the borrowing and recorded in the Consolidated Statements of Income. See Note 9 for additional information.

Financial Instruments. We account for derivative instruments as either assets or liabilities in the Consolidated Balance Sheets. The financial instruments are recorded at their respective fair value as determined on the day of issuance and subsequently adjusted to the fair value at each reporting date. Changes in the fair value of financial instruments are recognized periodically in the Consolidated Statements of Income. The estimated fair values of derivative instruments are determined at discrete points in time using standard valuation techniques.

Noncontrolling Interests. We report Net income attributable to noncontrolling interests separately on the face of our Consolidated Statements of Income. The portion of equity attributable to noncontrolling interests is reported within equity, separately from the Company's stockholders' equity on the Consolidated Balance Sheets.

When the noncontrolling interest is redeemable at the option of the noncontrolling shareholder, or contingently redeemable upon the occurrence of a conditional event that is not solely within the control of the Company, the noncontrolling interest is separately classified as mezzanine equity. In connection with the acquisition of Huang Ji Huang and Daojia, redeemable noncontrolling interests were initially recognized at fair value and classified outside of permanent equity on our Consolidated Balance Sheets due to redemption rights being held by noncontrolling shareholders. Subsequent changes in the redemption value of redeemable noncontrolling interests are immediately recognized as they occur and adjusted to the carrying amount of redeemable noncontrolling interests.

Guarantees. We account for guarantees in accordance with ASC Topic 460 (“ASC 460”), *Guarantees*. Accordingly, the Company evaluates its guarantees to determine whether (a) the guarantee is specifically excluded from the scope of ASC 460, (b) the guarantee is subject to ASC 460 disclosure requirements only, but not subject to the initial recognition and measurement provisions, or (c) the guarantee is required to be recorded in the financial statements at fair value. The Company provides: (i) indemnifications to certain investors and other parties for certain losses suffered or incurred by the indemnified party in connection with third-party claims; and (ii) indemnifications of officers and directors against third-party claims arising from the services they provide to the Company. To date, the Company has not incurred costs as a result of these obligations and does not expect to incur material costs in the future. Accordingly, the Company has not accrued any liabilities on the Consolidated Balance Sheets related to these indemnifications.

Asset Retirement Obligations. We recognize an asset and a liability for the fair value of a required asset retirement obligation (“ARO”) when such an obligation is incurred. The Company’s AROs are primarily associated with leasehold improvements which, at the end of the lease, the Company is contractually obligated to remove in order to comply with the lease agreement. As such, we amortize the asset on a straight-line basis over the lease term and accrete the liability to its nominal value using the effective interest method over the lease term.

Contingencies. The Company records accruals for certain of its outstanding legal proceedings or claims when it is probable that a liability will be incurred and the amount of loss can be reasonably estimated. The Company evaluates, on a quarterly basis, developments in legal proceedings or claims that could affect the amount of any accrual, as well as any developments that would make a loss contingency both probable and reasonably estimable. The Company discloses the amount of the accrual if it is material.

Retirement Plans. Certain of the Company’s employees participate in noncontributory defined benefit plans and post-retirement medical plans sponsored by YUM prior to October 31, 2016. Subsequent to the separation, employees participating in YUM’s plans were enrolled in the Yum China Holdings, Inc. Leadership Retirement Plan (“YCHLRP”), an unfunded, unsecured account-based retirement plan which allocates a percentage of pay to an account payable to the executive following the executive’s separation of employment from the Company or attainment of age 55.

The Company also offers other defined contribution plans to employees. The total contribution for such employee benefits was expensed as incurred. The Company has no additional legal obligation or liabilities for the benefits beyond the paid and accrued amounts. See Note 13 for additional information.

PRC Value-Added Tax (“VAT”). The Company has been subject to VAT within the normal course of its restaurant business nationwide since May 1, 2016.

Entities that are VAT general taxpayers are permitted to offset qualified input VAT paid to suppliers against their output VAT upon receipt of appropriate supplier VAT invoices on an entity-by-entity basis. When the output VAT exceeds the input VAT, the difference is remitted to tax authorities, usually on a monthly basis; whereas when the input VAT exceeds the output VAT, the difference is treated as a VAT asset which can be carried forward indefinitely to offset future net VAT payables. VAT related to purchases and sales which have not been settled at the balance sheet date is disclosed separately as an asset and liability, respectively, on the Consolidated Balance Sheets. VAT assets are classified as Prepaid expenses and other current assets if they are expected to be used within one year. At each balance sheet date, the Company reviews the outstanding balance of VAT assets for recoverability assessment.

Pursuant to the tax policy issued by relevant government authorities, general VAT taxpayers in certain industries that meet certain criteria are allowed to claim an additional 10% or 15% input VAT, which will be used to offset their VAT payables. This VAT policy was further extended to December 31, 2023 but the additional deduction was reduced to 5% or 10% respectively. Accordingly, the Company recognized such VAT deductions of \$44 million and \$16 million in 2023 and 2022, respectively. The VAT deductions were recorded as a reduction to the related expense item, primarily in Company restaurant expenses included in the Consolidated Statements of Income.

Earnings Per Share. Basic earnings per share represent net earnings to common stockholders divided by the weighted-average number of common shares outstanding for the period. Diluted earnings per share reflect the potential dilution that could occur if securities or other contracts to issue common shares were exercised or converted into common shares. See Note 5 for further information.

Common Stock Repurchases. We may repurchase shares of Yum China common stock under a program authorized by our Board of Directors from time to time in open market or, subject to applicable regulatory requirements, through privately negotiated transactions, block trades, accelerated share repurchase transactions and the use of Rule 10b5-1 trading plans. Shares repurchased are included in treasury stock in the financial statements until they are retired. When repurchased shares are retired, the Company's accounting policy is to allocate the excess of the repurchase price over the par value of shares acquired between Additional paid-in capital and Retained earnings. The amount allocated to Additional paid-in capital is based on the value of Additional paid-in capital per share outstanding at the time of retirement and the number of shares to be retired. Any remaining amount is allocated to Retained earnings. In connection with the Primary Conversion, all shares repurchased and included in the treasury stock were immediately retired. See Note 15 for further information.

Recently Adopted Accounting Pronouncements

In October 2021, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2021-08 *Business Combinations (Topic 805) — Accounting for Contract Assets and Contract Liabilities from Contracts with Customers* (“ASU 2021-08”). It requires issuers to apply ASC 606 *Revenue from Contracts with Customers* to recognize and measure contract assets and contract liabilities from contracts with customers acquired in a business combination. We adopted this standard on January 1, 2023, and such adoption did not have a material impact on our financial statements.

In March 2022, the FASB issued ASU 2022-01 *Fair Value Hedging—Portfolio Layer Method* (“ASU 2022-01”), which allows entities to expand their use of the portfolio layer method for fair value hedges of interest rate risk. Under the guidance, entities can hedge all financial assets under the portfolio layer method and designate multiple hedged layers within a single closed portfolio. The guidance also clarifies the accounting for fair value hedge basis adjustments in portfolio layer hedges and how these adjustments should be disclosed. We adopted this standard on January 1, 2023, and such adoption did not have a material impact on our financial statements.

In March 2022, the FASB issued ASU 2022-02 *Financial Instrument—Credit Losses* (“ASU 2022-02”), amending ASC 310 to eliminate the recognition and measurement guidance for a troubled debt restructuring for creditors that have adopted ASC 326 and requiring them to make enhanced disclosures about loan modifications for borrowers experiencing financial difficulty. The guidance also requires entities to present gross write-offs by year of origination in their vintage disclosures. We adopted this standard on January 1, 2023, and such adoption did not have a material impact on our financial statements.

In June 2022, the FASB issued ASU 2022-03 *Fair Value Measurement—Fair Value Measurement of Equity Securities Subject to Contractual Sale Restriction* (“ASU 2022-03”), clarifying that a contractual restriction on sales of an equity security is not considered part of the unit of account of the equity security, and therefore, is not considered when measuring fair value. The guidance also clarifies that a contractual sales restriction should not be recognized as a separate unit of account. We adopted this standard on January 1, 2023, and such adoption did not have a material impact on our financial statements.

In September 2022, the FASB issued ASU 2022-04 *Liabilities—Disclosure of Supplier Finance Program Obligations* (“ASU 2022-04”), requiring entities that use supplier finance programs in connection with the purchase of goods and services to disclose the key terms of the programs and information about their obligations outstanding at the end of the reporting period. We adopted this standard on January 1, 2023, and such adoption did not have a material impact on our financial statements.

Note 3 – Business Acquisitions and Equity Investments

Consolidation of Hangzhou KFC and Equity Investment in Hangzhou Catering

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

As a result of the consolidation of the Hangzhou KFC, the Company also recognized a gain of \$618 million in the fourth quarter of 2021 from the re-measurement of our previously held equity interest at fair value. The gain was recorded in Other income, net and not allocated to any segment for performance reporting purposes. Additionally, \$66 million of the purchase price was allocated to the reacquired franchise right, which is amortized over the remaining franchise contract period of 1 year.

In addition to its equity interest in Hangzhou KFC, Hangzhou Catering operates approximately 70 Chinese dining restaurants under four time-honored brands and a food processing business. The Company applies the equity method of accounting to the 28% equity interest in Hangzhou Catering excluding the Hangzhou KFC business and recorded this investment in Equity investment based on its then fair value. The Company elected to report its share of Hangzhou Catering's financial results with a one-quarter lag because its results are not available in time for the Company to record them in the concurrent period. The Company's equity income (losses) from Hangzhou Catering, net of taxes, were immaterial for the years ended December 31, 2023 and 2022, and included in Equity in net earnings (losses) from equity method investments in our Consolidated Statement of Income. As of December 31, 2023 and 2022, the carrying amount of the Company's equity method investment in Hangzhou Catering was \$41 million and \$37 million, respectively, exceeding the Company's interest in Hangzhou Catering's underlying net assets by \$24 million and \$26 million, respectively. Substantially all of this difference was attributable to its self-owned properties and impact of related deferred tax liabilities determined upon acquisition, which is being depreciated over a weighted-average remaining useful life of 20 years.

The Company purchased inventories of \$6 million from Hangzhou Catering for the year ended December 31, 2023, and the purchase amount was immaterial for the years ended December 31, 2022 and 2021, respectively. The Company's accounts payable and other current liabilities due to Hangzhou Catering were immaterial at both December 31, 2023 and 2022.

Consolidation of Suzhou KFC

In the third quarter of 2020, the Company completed the acquisition of an additional 25% equity interest in Suzhou KFC for cash consideration of \$149 million, increasing its equity interest to 72%, and thus the Company obtained control over Suzhou KFC and started to consolidate its results from the acquisition date.

As a result of the consolidation of Suzhou KFC, \$61 million of the purchase price was allocated to the reacquired franchise right in 2020, which is amortized over the remaining franchise contract period of 2.4 years.

In December 2022, the Company acquired an additional 20% equity interest in Suzhou KFC for cash consideration of \$115 million, bringing its total ownership to 92%. As the Company has previously obtained control of Suzhou KFC, this transaction was accounted for as an equity transaction. Upon completion of the transaction, the excess of purchase consideration over the carrying amount of the non-controlling interests was \$15 million, which was recorded in Additional paid-in capital.

Consolidation of Lavazza Joint Venture

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

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

Fujian Sunner Development Co., Ltd. (“Sunner”) Investment

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

The Company accounted for the equity securities at fair value based on their closing market price on each measurement date, with subsequent fair value changes recorded in our Consolidated Statements of Income. The unrealized loss of \$22 million were included in Investment gain or loss in our Consolidated Statements of Income for the year ended December 31, 2021, representing changes in fair value before the equity method of accounting was applied.

In May 2021, a senior executive of the Company was nominated and appointed to Sunner’s board of directors upon Sunner’s shareholder approval. Through this representation, the Company participates in Sunner’s policy making process. The representation on the board, along with the Company being one of Sunner’s significant shareholders, provides the Company with the ability to exercise significant influence over the operating and financial policies of Sunner. As a result, the Company started to apply the equity method of accounting to the investment in May 2021 based on its then fair value. The Company elected to report its share of Sunner’s financial results with a one-quarter lag because Sunner’s results are not available in time for the Company to record them in the concurrent period. The Company’s equity income from Sunner, net of taxes, was \$6 million for the year ended December 31, 2023 and immaterial for both the years ended December 31, 2022 and 2021, and included in Equity in net earnings (losses) from equity method investments in our Consolidated Statement of Income.

Since Sunner became the Company’s equity method investees in May 2021, the Company purchased inventories of \$318 million from Sunner for the year ended December 31, 2021. The Company purchased inventories of \$507 million and \$433 million for years ended December 31, 2023 and 2022, respectively. The Company’s accounts payable and other current liabilities due to Sunner were \$51 million and \$53 million as of December 31, 2023 and 2022, respectively.

As of December 31, 2023 and 2022, the Company’s investment in Sunner was stated at the carrying amount of \$225 million and \$227 million, respectively, which was \$152 million and \$157 million higher than the Company’s interest in Sunner’s underlying net assets, respectively. Of this basis difference, \$16 million and \$18 million was related to finite-lived intangible assets which are being amortized over estimated useful life of 20 years, respectively. The remaining differences were related to goodwill and indefinite-lived intangible assets, which are not subject to amortization, as well as deferred tax liabilities impact. As of December 31, 2023 and 2022, the market value of the Company’s investment in Sunner was \$151 million and \$214 million based on its quoted closing price, respectively.

Meituan Dianping (“Meituan”) Investment

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

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

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

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Unrealized losses recorded on equity securities still held as of the end of the year	<u>\$ (50)</u>	<u>\$ (27)</u>	<u>\$ (38)</u>

Note 4 – Revenue

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

Revenues	2023						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 8,116	\$ 2,214	\$ 61	\$ —	\$ 10,391	\$ —	\$ 10,391
Franchise fees and income	62	7	20	—	89	—	89
Revenues from transactions with franchisees	45	4	74	249	372	—	372
Other revenues	17	21	624	44	706	(580)	126
Total revenues	<u>\$ 8,240</u>	<u>\$ 2,246</u>	<u>\$ 779</u>	<u>\$ 293</u>	<u>\$ 11,558</u>	<u>\$ (580)</u>	<u>\$ 10,978</u>

Revenues	2022						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 7,120	\$ 1,939	\$ 51	\$ —	\$ 9,110	\$ —	\$ 9,110
Franchise fees and income	56	7	18	—	81	—	81
Revenues from transactions with franchisees	33	4	39	211	287	—	287
Other revenues	10	10	563	42	625	(534)	91
Total revenues	<u>\$ 7,219</u>	<u>\$ 1,960</u>	<u>\$ 671</u>	<u>\$ 253</u>	<u>\$ 10,103</u>	<u>\$ (534)</u>	<u>\$ 9,569</u>

Revenues	2021						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated	Combined	Elimination	Consolidated
Company sales	\$ 6,816	\$ 2,092	\$ 53	\$ —	\$ 8,961	\$ —	\$ 8,961
Franchise fees and income	120	8	25	—	153	—	153
Revenues from transactions with franchisees	59	6	98	500	663	—	663
Other revenues	8	3	297	20	328	(252)	76
Total revenues	<u>\$ 7,003</u>	<u>\$ 2,109</u>	<u>\$ 473</u>	<u>\$ 520</u>	<u>\$ 10,105</u>	<u>\$ (252)</u>	<u>\$ 9,853</u>

Franchise Fees and Income

	2023	2022	2021
Initial fees, including renewal fees	\$ 6	\$ 6	\$ 8
Continuing fees and rental income	83	75	145
Franchise fees and income	<u>\$ 89</u>	<u>\$ 81</u>	<u>\$ 153</u>

Costs to Obtain Contracts

Costs to obtain contracts consist of upfront franchise fees that we paid to YUM prior to the separation in relation to initial fees or renewal fees we received from franchisees, as well as license fees that are payable to YUM in relation to our deferred revenue of prepaid stored-value products, privilege membership programs and customer loyalty programs. They meet the requirements to be capitalized as they are incremental costs of obtaining contracts with customers and the Company expects to generate future economic benefits from such costs incurred. Such costs to obtain contracts are included in Other assets in the Consolidated Balance Sheets and are amortized on a systematic basis that is consistent with the transfer to the customer of the goods or services to which the assets relate. Subsequent to the separation, we are no longer required to pay YUM initial or renewal fees that we receive from franchisees. The Company did not incur any impairment losses related to costs to obtain contracts during any of the periods presented. Costs to obtain contracts were \$6 million at both December 31, 2023 and 2022.

Contract Liabilities

Contract liabilities at December 31, 2023 and 2022 were as follows:

	<u>2023</u>	<u>2022</u>
Contract liabilities		
- Deferred revenue related to prepaid stored-value products	\$ 142	\$ 139
- Deferred revenue related to upfront franchise fees	37	32
- Deferred revenue related to customer loyalty programs	24	23
- Deferred revenue related to privilege membership programs	24	16
- Others	1	—
Total	<u>\$ 228</u>	<u>\$ 210</u>

Contract liabilities primarily consist of deferred revenue related to prepaid stored-value products, privilege membership programs, customer loyalty programs and upfront franchise fees. Deferred revenue related to prepaid stored-value products, privilege membership programs, and customer loyalty programs is included in Accounts payable and other current liabilities in the Consolidated Balance Sheets. Deferred revenue related to upfront franchise fees that we expect to recognize as revenue in the next 12 months is included in Accounts payable and other current liabilities, and the remaining balance is included in Other liabilities in the Consolidated Balance Sheets. Revenue recognized that was included in the contract liability balance at the beginning of the year amounted to \$106 million and \$110 million in 2023 and 2022, respectively. Changes in contract liability balances were not materially impacted by business acquisition, change in estimate of transaction price or any other factors during any of the years presented.

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

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

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

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Net Income – Yum China Holdings, Inc.	\$ 827	\$ 442	\$ 990
Weighted-average common shares outstanding (for basic calculation) ^(a)	416	421	422
Effect of dilutive share-based awards ^(a)	4	4	6
Effect of dilutive warrants ^(b)	—	—	6
Weighted-average common and dilutive potential common shares outstanding (for diluted calculation)	420	425	434
Basic Earnings Per Common Share	<u>\$ 1.99</u>	<u>\$ 1.05</u>	<u>\$ 2.34</u>
Diluted Earnings Per Common Share	<u>\$ 1.97</u>	<u>\$ 1.04</u>	<u>\$ 2.28</u>
Share-based awards excluded from the diluted EPS computation ^(c)	<u>3</u>	<u>4</u>	<u>2</u>

- (a) As a result of the separation, shares of Yum China common stock were distributed to YUM’s shareholders of record as of October 19, 2016 and were included in the calculated weighted-average common shares outstanding. Holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety. Any subsequent exercise of these awards, whether held by the Company’s employees or YUM’s employees, would increase the number of common shares outstanding. The incremental shares arising from outstanding equity awards are included in the computation of diluted EPS, if there is dilutive effect. See Note 14 for a further discussion of share-based compensation.

- (b) Pursuant to the investment agreements dated September 1, 2016 (Note 10), Yum China issued to strategic investors two tranches of warrants on January 9, 2017, with each tranche initially providing the right to purchase 8,200,405 shares of Yum China common stock, at an initial exercise price of \$31.40 and \$39.25 per share, respectively, subject to customary anti-dilution adjustments. The warrants were exercisable at any time through October 31, 2021. The incremental shares arising from outstanding warrants were included in the computation of diluted EPS, if there is dilutive effect when the average market price of Yum China common stock for the year exceeds the applicable exercise price of the warrants. During 2021, an aggregate of 7,534,316 common shares were issued as a result of the cashless exercise of all warrants outstanding, which upon exercise were excluded from the calculation of dilutive warrants and included in the weighted-average common shares outstanding.
- (c) These outstanding SARs, RSUs and PSUs were excluded from the computation of diluted EPS because to do so would have been antidilutive for the years presented, or because certain PSUs are contingently issuable based on the achievement of performance and market conditions, which have not been met as of December 31, 2023, 2022 and 2021.

Note 6 – Other Expenses (Income), net

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Amortization of reacquired franchise rights ^(a)	\$ 2	\$ 97	\$ 43
Gain from re-measurement of equity interest upon acquisition ^(b)	—	—	(628)
Equity income from investments in unconsolidated affiliates ^(c)	—	—	(43)
Foreign exchanges and other	(2)	(3)	(15)
Other expenses (income), net	<u>\$ —</u>	<u>\$ 94</u>	<u>\$ (643)</u>

- (a) As a result of the acquisition of Hangzhou KFC, Suzhou KFC and Wuxi KFC, \$66 million, \$61 million and \$61 million of the purchase price were allocated to intangible assets related to reacquired franchise rights, respectively, which are being amortized over the remaining franchise contract period of 1 year, 2.4 years and 5 years. (See Note 3 for additional information). The above reacquired franchise rights were substantially amortized as of December 31, 2022 and resulted in the decrease of amortization expenses in 2023.
- (b) In the fourth and third quarters of 2021, as a result of the consolidation of Hangzhou KFC and the Lavazza joint venture, the Company recognized a gain of \$618 million and \$10 million, respectively, from the re-measurement of our previously held equity interest at fair value. (See Note 3 for additional information).
- (c) Includes equity income from our investments in Hangzhou KFC and the Lavazza joint venture before we consolidated the results of these entities upon completion of acquisitions. (See Note 3 for additional information).

Note 7 – Supplemental Balance Sheet Information

	<u>2023</u>	<u>2022</u>
Accounts Receivable, net		
Accounts receivable, gross	\$ 69	\$ 66
Allowance for doubtful accounts	(1)	(2)
Accounts receivable, net	<u>\$ 68</u>	<u>\$ 64</u>

The Company generally allows a credit period within 30 days of the period in which the corresponding sales occur to its customers. An aging analysis of accounts receivable as of December 31, 2023 and 2022, based on the date of delivering goods and services, is as follows:

	<u>2023</u>	<u>2022</u>
Within 30 days	\$ 56	\$ 56
31-90 days	11	7
Over 91 days	2	3
Total	<u>\$ 69</u>	<u>\$ 66</u>

Prepaid Expenses and Other Current Assets

	<u>2023</u>	<u>2022</u>
VAT assets	\$ 91	\$ 88
Receivables from payment processors and aggregators	78	53
Interest receivables	46	31
Deposits, primarily lease deposits	25	24
Other prepaid expenses and current assets	99	111
Prepaid expenses and other current assets	<u>\$ 339</u>	<u>\$ 307</u>

PP&E

	<u>2023</u>	<u>2022</u>
Buildings and improvements, and construction in progress	\$ 3,073	\$ 2,912
Finance leases, primarily buildings	68	62
Machinery and equipment	1,742	1,612
PP&E, gross	4,883	4,586
Accumulated depreciation	(2,573)	(2,468)
PP&E, net	<u>\$ 2,310</u>	<u>\$ 2,118</u>

Depreciation and amortization expense related to property, plant and equipment was \$442 million, \$497 million and \$465 million in 2023, 2022 and 2021, respectively.

Equity Investments

	<u>2023</u>	<u>2022</u>
Investment in equity method investees	\$ 287	\$ 266
Investment in equity securities	45	95
Equity investments	<u>\$ 332</u>	<u>\$ 361</u>

Other Assets

	<u>2023</u>	<u>2022</u>
Land use right ^(a)	\$ 115	\$ 123
Long-term deposits, primarily lease deposits	94	90
Prepayment for acquisition of PP&E ^(b)	28	6
Costs to obtain contracts	6	6
VAT assets	6	5
Others	16	18
Other assets	<u>\$ 265</u>	<u>\$ 248</u>

(a) Amortization expense related to land use right was \$4 million, \$5 million and \$5 million in 2023, 2022 and 2021, respectively.

(b) The increase was primarily due to a prepayment made in relation to the acquisition of a building located in Shanghai to house the Company's headquarters and flagship stores, which is currently expected to be delivered to the Company around 2026.

Accounts Payable and Other Current Liabilities

	<u>2023</u>	<u>2022</u>
Accounts payable	\$ 786	\$ 727
Operating lease liabilities	426	448
Accrued compensation and benefits	299	285
Accrued capital expenditures	226	181
Contract liabilities	196	182
Accrued marketing expenses	51	72
Dividends payable	40	51
Other current liabilities	140	150
Accounts payable and other current liabilities	<u>\$ 2,164</u>	<u>\$ 2,096</u>

Other Liabilities

	<u>2023</u>	<u>2022</u>
Accrued income tax payable	\$ 39	\$ 52
Contract liabilities	32	28
Other non-current liabilities	86	82
Other liabilities	<u>\$ 157</u>	<u>\$ 162</u>

An aging analysis of the accounts payable as of December 31, 2023 and 2022 is as follows:

	<u>2023</u>	<u>2022</u>
Within 60 days	\$ 783	\$ 722
Over 60 days	3	5
Total	<u>\$ 786</u>	<u>\$ 727</u>

The accounts payable consist of invoiced and certain accrued balances, and are generally repaid within one to two months depending on payment term and the invoice date. Accrued accounts payable reflect payable of goods and services that have not yet been invoiced to the Company, and will be reclassified to invoiced accounts payable when invoices are received. Aging analysis of invoiced accounts payable has been presented based on invoice date and the amounts of accrued accounts payable were categorized as within 60 days.

Accounts payable and Other current liabilities also include remuneration payable to auditors. Total auditors' remuneration was \$3 million in each of 2023, 2022 and 2021.

Note 8 – Goodwill and Intangible Assets

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

	<u>Total Company</u>	<u>KFC</u>	<u>Pizza Hut</u>	<u>All Other Segments</u>
Balance as of December 31, 2021				
Goodwill, gross	\$ 2,533	\$ 2,040	\$ 20	\$ 473
Accumulated impairment losses ^(a)	(391)	—	—	(391)
Goodwill, net	\$ 2,142	\$ 2,040	\$ 20	\$ 82
Goodwill acquired ^(b)	16	15	1	—
Effect of currency translation adjustments	(170)	(162)	(2)	(6)
Balance as of December 31, 2022				
Goodwill, gross	2,379	1,893	19	467
Accumulated impairment losses ^(a)	(391)	—	—	(391)
Goodwill, net	\$ 1,988	\$ 1,893	\$ 19	\$ 76
Goodwill acquired ^(b)	1	1	—	—
Effect of currency translation adjustments	(57)	(54)	(1)	(2)
Balance as of December 31, 2023				
Goodwill, gross	2,323	1,840	18	465
Accumulated impairment losses ^(a)	(391)	—	—	(391)
Goodwill, net	<u>\$ 1,932</u>	<u>\$ 1,840</u>	<u>\$ 18</u>	<u>\$ 74</u>

(a) Accumulated impairment losses represent goodwill impairment attributable to the reporting units of Little Sheep and Daojia.

(b) Goodwill acquired resulted from the acquisition of restaurants from our existing franchisees during 2022 and 2023, which was immaterial.

Intangible assets, net as of December 31, 2023 and 2022 are as follows:

	2023				2022			
	Gross Carrying Amount ^(a)	Accumulated Amortization ^(a)	Accumulated Impairment Losses ^(b)	Net Carrying Amount	Gross Carrying Amount	Accumulated Amortization	Accumulated Impairment Losses ^(b)	Net Carrying Amount
Finite-lived intangible assets								
Reacquired franchise rights	\$ 268	\$ (265)	\$ —	\$ 3	\$ 276	\$ (271)	\$ —	\$ 5
Huang Ji Huang franchise related assets	21	(4)	—	17	22	(3)	—	19
Daojia platform	16	(4)	(12)	—	16	(4)	(12)	—
Customer-related assets	12	(10)	(2)	—	12	(9)	(2)	1
Other	9	(6)	—	3	9	(5)	—	4
	<u>\$ 326</u>	<u>\$ (289)</u>	<u>\$ (14)</u>	<u>\$ 23</u>	<u>\$ 335</u>	<u>\$ (292)</u>	<u>\$ (14)</u>	<u>\$ 29</u>
Indefinite-lived intangible assets								
Little Sheep trademark	\$ 51	\$ —	\$ —	\$ 51	\$ 52	\$ —	\$ —	\$ 52
Huang Ji Huang trademark	76	—	—	76	78	—	—	78
	<u>\$ 127</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 127</u>	<u>\$ 130</u>	<u>\$ —</u>	<u>\$ —</u>	<u>\$ 130</u>
Total intangible assets	<u>\$ 453</u>	<u>\$ (289)</u>	<u>\$ (14)</u>	<u>\$ 150</u>	<u>\$ 465</u>	<u>\$ (292)</u>	<u>\$ (14)</u>	<u>\$ 159</u>

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

Amortization expense for finite-lived intangible assets was \$4 million in 2023, \$99 million in 2022 and \$45 million in 2021. The decrease in amortized expense for finite-lived intangible assets in 2023 was primarily due to certain reacquired franchise rights being substantially amortized as of December 31, 2022 (See Note 6 for details). Amortization expense for finite-lived intangible assets is expected to approximate \$2 million in each of 2024, 2025, 2026, 2027 and 2028.

Note 9 – Credit Facilities and Short-term Borrowings

As of December 31, 2023, the Company had credit facilities of RMB7,112 million (approximately \$1,002 million), comprised of onshore credit facilities in the aggregate amount of RMB5,550 million (approximately \$782 million) and offshore credit facilities in the aggregate amount of \$220 million.

The credit facilities had remaining terms ranging from less than one year to three years as of December 31, 2023. Our credit facilities mainly include term loans, overdrafts, letters of credit, banker's acceptance notes and bank guarantees. The credit facilities in general bear interest based on the Loan Prime Rate (“LPR”) published by the National Interbank Funding Centre of the PRC, or Secured Overnight Financing Rate (“SOFR”) published by the Federal Reserve Bank of New York. Each credit facility contains a cross-default provision whereby our failure to make any payment on a principal amount from any credit facility will constitute a default on other credit facilities. Some of the credit facilities contain covenants limiting, among other things, certain additional indebtedness and liens, and certain other transactions specified in the respective agreements. As of December 31, 2023 and 2022, we had outstanding short-term bank borrowings of \$168 million and \$2 million, respectively, mainly to manage working capital at our operating subsidiaries, which were secured by short-term investments of \$79 million and \$1 million, respectively. The RMB denominated bank borrowings bear a weighted-average interest rate of 1.7%, and are due within one year from their issuance dates. As of December 31, 2023, we also had outstanding bank guarantees of RMB222 million (approximately \$31 million) mainly to secure our lease payments to landlords for certain Company-owned restaurants. Our credit facilities were therefore reduced by outstanding short-term bank borrowings, adjusted for unamortized interest and collateral, and outstanding guarantees. As of December 31, 2023, the Company had unused credit facilities of approximately \$881 million.

Note 10 – Investment Agreements with Strategic Investors

On September 1, 2016, YUM and the Company entered into investment agreements (the “Investment Agreements”) with each of Pollos Investment L.P., an affiliate of Primavera Capital Group (“Primavera”), and API (Hong Kong) Investment Limited, an affiliate of Ant Group Co., Ltd (previously known as Zhejiang Ant Small and Micro Financial Services Group Co., Ltd., “Ant Financial”). Pursuant to the Investment Agreements, on November 1, 2016 (“Closing Date”), Primavera and Ant Financial invested \$410 million and \$50 million, respectively, for a collective \$460 million investment (the “Investment”) in the Company in exchange for: (i) over 18 million shares of Yum China common stock and (ii) two tranches of warrants (the “Warrants”). Upon exercise, the first tranche of Warrants initially provided Primavera and Ant Financial with the right to purchase 7,309,057 and 891,348 shares of Yum China common stock, respectively, at an initial exercise price of \$31.40 per share. The second tranche of Warrants initially provided Primavera and Ant Financial with the right to purchase the same number of shares of Yum China common stock under the first tranche of Warrants, at an initial exercise price of \$39.25 per share. The Warrants were exercisable at any time through October 31, 2021 and contain customary anti-dilution protections, which were equity-classified and recorded in Additional paid in capital in the Consolidated balance sheet presented since December 2016, when the number of Warrants to be issued became fixed.

As of December 31, 2020, Primavera and Ant Financial had separately entered into pre-paid forward sale transactions with respect to all of their Warrants with several financial institutions, pursuant to which Primavera and Ant Financial would deliver their respective Warrants on the applicable settlement date.

In 2021, 7,534,316 shares of Yum China common stock were issued as a result of the cashless exercise of all Warrants, representing approximately 1.8% of Yum China common stock issued and outstanding as of December 31, 2021.

Note 11 – Leases

As of December 31, 2023, we leased over 12,500 properties in China for our Company-owned restaurants. We generally enter into lease agreements for our restaurants with initial terms of 10 to 20 years. Most of our lease agreements contain termination options that permit us to terminate the lease agreement early if the restaurant profit is negative for a specified period of time. We generally do not have renewal options for our leases. Such options are accounted for only when it is reasonably certain that we will exercise the options. The rent under the majority of our current restaurant lease agreements is generally payable in one of three ways: (i) fixed rent; (ii) the higher of a fixed base rent or a percentage of the restaurant’s sales; or (iii) a percentage of the restaurant’s sales. Most leases require us to pay common area maintenance fees for the leased property. In addition to restaurants leases, we also lease office spaces, logistics centers and equipment. Our lease agreements do not contain any material residual value guarantees or material restrictive covenants.

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

Supplemental Balance Sheet

	<u>2023/12/31</u>	<u>2022/12/31</u>	Account Classification
Assets			
Operating lease right-of-use assets	\$ 2,217	\$ 2,219	Operating lease right-of-use assets
Finance lease right-of-use assets	41	38	PP&E
Total leased assets	<u>\$ 2,258</u>	<u>\$ 2,257</u>	
Liabilities			
Current			
Operating lease liabilities	\$ 426	\$ 448	Accounts payable and other current liabilities
Finance lease liabilities	5	5	Accounts payable and other current liabilities
Non-current			
Operating lease liabilities	1,899	1,906	Non-current operating lease liabilities
Finance lease liabilities	44	42	Non-current finance lease liabilities
Total lease liabilities	<u>\$ 2,374</u>	<u>\$ 2,401</u>	

Summary of Lease Cost	Account Classification			
	2023	2022	2021	
Operating lease cost	\$ 517	\$ 564	\$ 564	Occupancy and other operating expenses, G&A or Franchise expenses
Finance lease cost				
Amortization of leased assets	5	4	3	Occupancy and other operating expenses
Interest on lease liabilities	2	2	2	Interest expense, net
Variable lease cost ^(a)	402	303	346	Occupancy and other operating expenses or Franchise expenses
Short-term lease cost	15	12	9	Occupancy and other operating expenses or G&A
Sub-lease income	(21)	(23)	(26)	Franchise fees and income or Other revenues
Total lease cost	<u>\$ 920</u>	<u>\$ 862</u>	<u>\$ 898</u>	

- (a) The Company was granted \$11 million, \$39 million and \$12 million in lease concessions from landlords related to the effects of the COVID-19 pandemic for the years ended December 31, 2023, 2022 and 2021, respectively. The lease concessions were primarily in the form of rent reduction over the period of time when the Company's restaurant business was adversely impacted. The Company applied the interpretive guidance in a FASB staff question-and-answer document issued in April 2020 and elected: (1) not to evaluate whether a concession received in response to the COVID-19 pandemic is a lease modification and (2) to assume such concession was contemplated as part of the existing lease contract with no contract modification. Such concession was recognized as negative variable lease cost in the period the concession was granted.

Supplemental Cash Flow Information

	2023	2022	2021
Cash paid for amounts included in the measurement of lease liabilities:			
Operating cash flows from operating leases	\$ 531	\$ 549	\$ 573
Operating cash flows from finance leases	2	2	2
Financing cash flows from finance leases	5	4	2
Right-of-use assets obtained in exchange for lease liabilities ^(b) :			
Operating leases	\$ 456	\$ 191	\$ 541
Finance leases	7	10	11

- (b) This supplemental non-cash disclosure for ROU assets obtained in exchange for lease liabilities includes an increase in lease liabilities associated with obtaining new ROU assets of \$451 million, \$344 million and \$557 million for the years ended December 31, 2023, 2022 and 2021, respectively, as well as adjustments to lease liabilities or ROU assets due to modification or other reassessment events, which resulted in an increase of \$12 million, a decrease of \$143 million and \$5 million in lease liabilities for the years ended December 31, 2023, 2022 and 2021, respectively.

Lease Term and Discount Rate

	2023	2022
Weighted-average remaining lease term (years)		
Operating leases	7.1	7.1
Finance leases	10.9	11.2
Weighted-average discount rate		
Operating leases	4.9%	5.1%
Finance leases	5.0%	5.1%

Summary of Future Lease Payments and Lease Liabilities

Maturities of lease liabilities as of December 31, 2023 were as follows:

	Amount of Operating Leases	Amount of Finance Leases	Total
2024	\$ 525	\$ 7	\$ 532
2025	445	6	451
2026	399	6	405
2027	345	6	351
2028	280	6	286
Thereafter	763	32	795
Total undiscounted lease payment	<u>2,757</u>	<u>63</u>	<u>2,820</u>
Less: imputed interest ^(c)	432	14	446
Present value of lease liabilities	<u>\$ 2,325</u>	<u>\$ 49</u>	<u>\$ 2,374</u>

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

As of December 31, 2023, we have additional lease agreements that have been signed but not yet commenced, with total undiscounted minimum lease payments of \$110 million. These leases will commence between 2024 and 2026 with lease terms of 1 year to 20 years.

Note 12 – Fair Value Measurements and Disclosures

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

The Company's financial assets also include its investment in the equity securities of Meituan, which is measured at fair value based on the closing market price for the shares at the end of each reporting period, with subsequent fair value changes recorded in our Consolidated Statements of Income.

The following table is a summary of our financial assets measured on a recurring basis or disclosed at fair value and the level within the fair value hierarchy in which the measurement falls. The Company classifies its cash equivalents, short-term investments, long-term bank deposits and notes, and investment in equity securities within Level 1 or Level 2 in the fair value hierarchy because it uses quoted market prices or alternative pricing sources and models utilizing market observable inputs to determine their fair value, respectively. No transfers among the levels within the fair value hierarchy occurred in 2023 and 2022.

	Balance at December 31, 2023	Fair Value Measurement or Disclosure at December 31, 2023		
		Level 1	Level 2	Level 3
Cash equivalents:				
Time deposits	\$ 293		\$ 293	
Fixed income debt securities ^(a)	14	14		
Money market funds	11	11		
Total cash equivalents	318	25	293	—
Short-term investments:				
Time deposits	1,113		1,113	
Fixed income debt securities ^(a)	200		200	
Structured deposits	138		138	
Variable return investments	21	21		
Total short-term investments	1,472	21	1,451	—
Long-term bank deposits and notes				
Time deposits	903		903	
Fixed income bank notes	362		362	
Total long-term bank deposits and notes	1,265		1,265	
Equity investments:				
Investment in equity securities	45	45		
Total	\$ 3,100	\$ 91	\$ 3,009	\$ —

	Balance at December 31, 2022	Fair Value Measurement or Disclosure at December 31, 2022		
		Level 1	Level 2	Level 3
Cash equivalents:				
Time deposits	\$ 355		\$ 355	
Fixed income debt securities ^(a)	129	29	100	
Money market funds	59	59		
Total cash equivalents	543	88	455	—
Short-term investments:				
Time deposits	1,434		1,434	
Fixed income debt securities ^(a)	500		500	
Structured deposits	88		88	
Total short-term investments	2,022	—	2,022	—
Long-term bank deposits and notes				
Time deposits	680		680	
Equity investments:				
Investment in equity securities	95	95		
Total	\$ 3,340	\$ 183	\$ 3,157	\$ —

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

The Company is required to place bank deposits or purchase insurance to secure the balance of prepaid stored-value cards issued by the Company pursuant to regulatory requirements. \$21 million of time deposits in Short-term investments and \$28 million of time deposits in Long-term bank deposits and notes were restricted for use as of December 31, 2023, and \$81 million of time deposits in Long-term bank deposits and notes was restricted for use as of December 31, 2022. The decrease was primarily due to insurance purchased by the Company to secure a portion of prepaid stored-value cards.

Non-recurring fair value measurements

In addition, certain of the Company's restaurant-level assets (including operating lease ROU assets, PP&E), goodwill and intangible assets, are measured at fair value based on unobservable inputs (Level 3) on a non-recurring basis, if determined to be impaired. As of each relevant measurement date, the fair value of restaurant-level assets, if determined to be impaired, are primarily represented by the price market participant would pay to sub-lease the operating lease ROU assets and acquire the remaining restaurants assets, which reflects the highest and best use of the assets. Significant unobservable inputs used in the fair value measurement include market rental prices, which were determined with the assistance of an independent valuation specialist. The direct comparison approach is used as the valuation technique by assuming a sub-lease of each of the properties in its existing state with vacant possession. By making reference to lease transactions as available in the relevant market, comparable properties in close proximity have been selected and adjustments have been made to account for any difference in factors such as location and property size.

The following table presents amounts recognized from all non-recurring fair value measurements based on unobservable inputs (Level 3) during the years ended December 31, 2023, 2022 and 2021. These amounts exclude fair value measurements made for restaurants that were subsequently closed or refranchised prior to those respective year-end dates.

	<u>2023</u>	<u>2022</u>	<u>2021</u>	Account Classification
Restaurant-level impairment ^(a)	<u>20</u>	<u>24</u>	<u>32</u>	Closures and impairment expenses, net

- (a) Restaurant-level impairment charges are recorded in Closures and impairment expenses, net and resulted mainly from our semi-annual impairment evaluation of long-lived assets of individual restaurants that were being operated at the time of impairment and had not been offered for refranchising. After considering the impairment charges recorded during the corresponding years, the fair value of such assets as of the relevant measurement date was \$68 million, \$97 million and \$112 million during the years ended December 31, 2023, 2022 and 2021, respectively.

Note 13 – Retirement Plans

For executives who were hired or re-hired after September 30, 2001, YUM has implemented the YUM LRP. This is an unfunded, unsecured account-based retirement plan which allocates a percentage of pay to an account payable to the executive following the executive's separation of employment from YUM or attainment of age 55. The Company adopted the YCHLRP upon separation while the assets and liabilities associated with these employees under YUM LRP were transferred to YCHLRP. YCHLRP will continue to be in effect until terminated by the Company's Board of Directors. The terms of the YCHLRP are substantially similar to the terms of the YUM LRP. Under the YCHLRP, certain executives who are at least age 21, who are classified as salary level 12, who are not eligible to participate in a tax-qualified defined benefit plan, and who satisfy certain additional requirements as to work location and assignment, are eligible to participate in the YCHLRP if selected for participation by the Company. The YCHLRP is an unfunded, unsecured account-based retirement plan that allocates a percentage of pay to an account payable to an executive following the later to occur of the executive's separation of employment from the Company or attainment of age 55. Under the YCHLRP, participants aged 55 or older are entitled to a lump sum distribution of their account balance on the last day of the calendar quarter that occurs on or follows their separation of employment. The liabilities attributable to our employees under the YCHLRP were insignificant as of December 31, 2023 and 2022.

YUM offers certain of the Company's executives working in China retirement benefits under the Bai Sheng Restaurants China Holdings Limited Retirement Scheme (previously known as the Bai Sheng Restaurants (Hong Kong) Ltd. Retirement Scheme). Under this defined contribution plan, YUM provides a Company-funded contribution ranging from 5% to 10% of an executive's base salary. Upon termination, participants will receive a lump sum equal to a percentage of the Company's contributions inclusive of investment return. This percentage is based on a vesting schedule that provides participants with a vested 30% interest upon completion of a minimum of 3 years of service, and an additional 10% vested interest for each additional completed year, up to a maximum of 100%. The Company adopted the same plan after the separation and the contribution amount to the plan for the years ended December 31, 2023, 2022 and 2021 was immaterial. Forfeited contribution utilized under the plan to reduce the existing level of contribution during the years of 2023, 2022 and 2021 was immaterial. Unutilized forfeited contribution as of December 31, 2023 was immaterial as well.

As stipulated by Chinese state regulations, the Company participates in a government-sponsored defined contribution retirement plan. Substantially all employees are entitled to an annual pension equal to a fixed proportion of the average basic salary amount of the geographical area of their last employment at their retirement date. We are required to make contributions to the local social security bureau between 13% and 20% of the previous year's average basic salary amount of the geographical area where the employees are under our employment. Contributions are recorded in the Consolidated Statements of Income as they become payable. We have no obligation for the payment of pension benefits beyond the annual contributions as set out above. In 2022, in relation to effect of the COVID-19 pandemic, the Company also recorded one-time relief of enterprise social security contributions as a reduction to related expense (See Note 2 government subsidies for additional information). The Company contributed \$230 million, \$183 million and \$183 million to the government-sponsored plan for the year ended December 31, 2023, 2022 and 2021, respectively.

Note 14 – Share-Based Compensation

Overview

Upon the separation, holders of outstanding YUM equity awards generally received both adjusted YUM awards and Yum China awards, or adjusted awards of either YUM or Yum China in their entirety, to maintain the pre-separation intrinsic value of the awards. Depending on the tax laws of the country of employment, awards were modified using either the shareholder method or the employer method. Share issuances for Yum China awards held by YUM's employees will be satisfied by Yum China. Share issuances for YUM awards held by the Company's employees will be satisfied by YUM. The shareholder method was based on the premise that employees holding YUM awards prior to the separation should receive an equal number of awards of both YUM and Yum China. Under the employer method, employees holding YUM awards prior to the separation had their awards converted into awards of the Company that they worked for subsequent to the separation. As a result, Yum China may issue shares of common stock to YUM's employees upon exercise or vesting of various types of awards, including stock options, SARs, RSUs, and awards from the executive income deferral plan.

The modified equity awards have the same terms and conditions as the awards held immediately before the separation, except that the number of shares and the price were adjusted. Share-based compensation for the Company's employees is based on both YUM awards and Yum China awards held by those employees.

Effective October 31, 2016, the Company adopted the Yum China Holdings, Inc. Long Term Incentive Plan (the "2016 Plan"). The Company has reserved for issuance under the 2016 Plan of 45,000,000 shares of our common stock. Under this plan, the exercise price of stock options and SARs granted must be equal to or greater than the fair market value of the Company's stock on the date of grant.

In connection with the Primary Conversion, the Company's stockholders approved the Yum China Holdings, Inc. 2022 Long Term Incentive Plan (the "2022 Plan"), with 31,000,000 shares of Company common stock authorized for grants. The 2022 Plan replaced the 2016 Plan and became effective on October 24, 2022. The 2016 Plan continued to govern awards granted prior to the effectiveness of the 2022 Plan. Under the 2022 Plan, the exercise price of stock options and SARs granted must be the higher of 1) the fair market value of the Company's stock on the date of grant and (ii) the average fair market value for the five trading days immediately preceding the date of grant. The 2022 Plan is largely based on the 2016 Plan, but with updates to conform to the requirements of the HKEX, to delete provisions relating to our spin-off that are no longer applicable and to make certain other administrative changes.

Similar to the 2016 Plan, potential awards to employees and non-employee directors under the 2022 Plan include stock options, incentive options, SARs, restricted stock, stock units, RSUs, performance shares, performance units, and cash incentive awards. While awards under the 2016 and 2022 Plan can have varying vesting provisions and exercise periods, outstanding awards vest in periods ranging from three to five years. Stock options and SARs expire 10 years after grant.

The Company recognizes all share-based payments to employees and non-employee directors in the Consolidated Financial Statements as compensation cost on a straight-line basis over the service period based on their fair value on the date of grant, for awards that actually vest and when performance conditions are probable of being achieved, if applicable. If no substantive service condition exists, the grant-date fair value is fully recognized as expense upon grant.

Award Valuation

Stock Options and SARs

The Company estimated the fair value of each stock option and SAR award granted to the Company's employees as of the date of grant, using the BS model with the following assumptions:

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Risk-free interest rate	3.9%	1.6%	0.4%
Expected term (years)	6.50	6.25	6.25
Expected volatility	36.3%	32.4%	33.9%
Expected dividend yield	0.8%	1.0%	0.8%

Share option and SAR awards granted to employees typically have a graded vesting schedule of 25% per year over four years and expire 10 years after grant. The Company uses a single weighted-average term for awards that have a graded vesting schedule and determined average terms of exercise based on analysis of the historical exercise and post-vesting termination behavior. Forfeitures were estimated based on historical experience. Historical data used to estimate the expected term and forfeiture rate include data associated with the Company's employees who were granted share-based awards by YUM prior to the separation.

For those awards granted by the Company after the separation, the Company considered the volatility of common shares of comparable companies in the same business as the Company, as well as the historical volatility of the Company stock. The dividend yield was estimated based on the Company's dividend policy at the time of the grant.

RSUs

RSU awards generally vest over three to four years, with either cliff vesting at 100% on the third grant anniversary or graded vesting on anniversary dates. The fair values of RSU awards are based on the closing price of the Company's stock on the date of grant.

PSUs

In February 2020, the Company's Board of Directors approved new grants of a special award of PSUs ("Partner PSU Awards") to select employees who were deemed critical to the Company's execution of its strategic operating plan under the 2016 Plan. These Partner PSU Awards are subject to market and performance conditions, and will cliff vest only if threshold performance goals are achieved over a four-year performance period, with the payout ranging from 0% to 200% of the target number of shares.

In addition, the Company also granted annual PSU awards since 2020. These annual PSU awards are based on the Company's achievement of one or more performance goals, including relative total shareholder return against selected indices or the constituents of the indices, and will cliff vest only if threshold performance goals are achieved over a three-year performance period.

The fair value of PSU awards was determined based on the closing price of the Company's stock on the date of the grant and the outcome of the MCS model with the following assumptions:

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Risk-free interest rate	4.2%	1.8%	0.2%
Expected volatility	39.3%	30.8%	35.7%

Compensation costs associated with annual and Partner PSU Awards are recognized on a straight-line basis over the performance period when performance conditions are probable of being achieved, adjusted for estimated forfeiture rate.

Others

Commencing from November 11, 2016, Yum China also granted annual awards of common stock to non-employee directors for their service on Yum China's Board of Directors. The fair value of these awards is based on the closing price of the Company's common stock on the date of grant. The shares were issued outright to the directors on the date of grant, with no conditions attached. Therefore, the fair value of the awards was fully recognized as expenses upon grant. For the years ended December 31, 2023, 2022 and 2021, a total of 45,843, 47,820 and 31,182 shares of Yum China common stock, respectively, were granted to non-employee directors and the grant-date fair value of \$2.7 million, \$2.1 million and \$2.1 million, respectively, was immediately recognized in full in the Consolidated Statements of Income.

Award Activity

Stock Options and SARs

	Shares (in thousands)	Weighted-average Exercise Price	Weighted-average Remaining Contractual Term (years)	Aggregate Intrinsic Value (in millions)
Outstanding at the beginning of 2023	9,605	34.71		
Granted	345	62.14		
Exercised	(1,367)	24.98		
Forfeited or expired	(112)	52.81		
Outstanding at the end of 2023	<u>8,471^(a)</u>	37.16	4.52	73
Exercisable at the end of 2023	<u>6,766</u>	33.09	3.71	73

- (a) Outstanding awards include 87,077 stock options and 8,384,079 SARs with weighted-average exercise prices of \$21.66 and \$37.32, respectively. Outstanding awards represent Yum China awards held by employees of both the Company and YUM.

The weighted-average grant-date fair value of SARs granted in 2023, 2022 and 2021 was \$24.67, \$15.55 and \$17.44, respectively. The total intrinsic value of stock options and SARs exercised by the Company's employees during the years ended December 31, 2023, 2022 and 2021 was \$25 million, \$22 million and \$22 million, respectively.

As of December 31, 2023, \$18 million of unrecognized compensation cost related to unvested SARs, which will be reduced by any forfeitures that occur, is expected to be recognized over a remaining weighted-average vesting period of approximately 1.53 years. The total fair value at grant date of awards held by the Company's employees that vested during 2023, 2022 and 2021 was \$15 million, \$16 million and \$15 million, respectively.

RSUs

	Shares (in thousands)	Weighted- Average Grant Date Fair Value
Unvested at the beginning of 2023	875	54.13
Granted	503	61.17
Vested	(154)	51.31
Forfeited or expired	(57)	56.06
Unvested at the end of 2023	<u>1,167</u>	<u>57.44</u>

The weighted-average grant-date fair value of RSUs granted in 2023, 2022 and 2021 was \$61.17, \$50.11 and \$58.77, respectively. As of December 31, 2023, \$34 million of unrecognized compensation cost related to 1,166,863 unvested RSUs, which will be reduced by any forfeiture that occurs, is expected to be recognized over a remaining weighted-average vesting period of approximately 1.65 years. The total fair value at grant date of awards that vested during 2023, 2022 and 2021 was \$8 million, \$7 million and \$11 million, respectively.

PSUs

	Shares (in thousands)	Weighted- Average Grant Date Fair Value
Unvested at the beginning of 2023	1,076	44.04
Granted	189	71.01
Vested	(963)	42.23
Forfeited or expired	(34)	47.91
Unvested at the end of 2023	<u>268</u>	<u>69.05</u>

The weighted-average grant-date fair value of PSUs granted in 2023, 2022 and 2021 was \$71.01, \$61.33 and \$68.04, respectively. As of December 31, 2023, \$13 million of unrecognized compensation cost related to 268,435 unvested PSUs, which will be reduced by any forfeiture that occurs and adjusted based on the Company's achievement of performance goals, is expected to be recognized over a remaining weighted-average vesting period of approximately 1.88 years. The total fair value at grant date of awards that vested during 2023, 2022 and 2021 was \$41 million, \$5 million and \$3 million, respectively.

On December 30, 2022, in recognition of the extended impact of the COVID-19 pandemic and the Company's performance over the three-year performance period of the 2020 annual PSU awards, the Compensation Committee of the Board of Directors determined to adjust the weighting of the performance goals applicable to the 2020 annual PSU awards. This modification pertained to all recipients of this award, and resulted in incremental compensation expense of \$6 million recognized during the year ended December 31, 2022.

Impact on Net Income

Share-based compensation expense was \$64 million, \$42 million and \$41 million for 2023, 2022 and 2021, respectively. Deferred tax benefits and tax benefits realized on our tax returns from tax deductions associated with share-based compensation were immaterial in each of 2023, 2022 and 2021.

Note 15 – Equity

Immediately after the separation on October 31, 2016, Yum China authorized capital stock consisted of 1,000 million shares of common stock, par value \$0.01 per share, and 364 million shares of Yum China common stock were issued and outstanding. As of December 31, 2023, 407 million shares of Yum China common stock were issued and outstanding.

Share Repurchase and Retirement

The Company repurchased 12.4 million shares of common stock for \$617 million, 10.5 million shares of common stock for \$466 million and 1.3 million shares of common stock for \$75 million for the years ended December 31, 2023, 2022 and 2021, respectively. The total repurchase cost of 2023 included \$4 million settled subsequent to December 31, 2023 for shares repurchased with trade dates on and prior to December 31, 2023. On November 2, 2023, our Board of Directors increased the share repurchase authorization by \$1 billion to an aggregate of \$3.4 billion, of which \$1.5 billion remained available as of December 31, 2023.

As both of December 31, 2023 and 2022, all shares repurchased were retired and resumed the status of authorized and unissued shares of common stock.

The Inflation Reduction Act of 2022 ("IRA"), which is discussed further in Note 16, imposes an excise tax of 1% on net share repurchases that occur after December 31, 2022. Estimated excise tax on net share repurchases, which was recognized as part of the cost of the shares repurchased, amounted to \$6 million for the year ended December 31, 2023.

Cash Dividend

On October 4, 2017, the Board of Directors approved a regular quarterly cash dividend program, and we have paid a quarterly cash dividend on Yum China's common stock since the fourth quarter of 2017, except for the second and third quarters of 2020 due to the unprecedented effects of the COVID-19 pandemic. Cash dividends totaling \$216 million, \$202 million and \$203 million were paid to stockholders in 2023, 2022 and 2021, respectively.

Accumulated Other Comprehensive Income (Loss) (“AOCI”)

The Company’s Other comprehensive income (loss) for the years ended December 31, 2023, 2022 and 2021 and AOCI balances as of December 31, 2023 and 2022 were comprised solely of foreign currency translation adjustments. Other comprehensive loss was \$146 million and \$431 million for the year ended December 31, 2023 and 2022, respectively, and other comprehensive income was \$108 million for the years ended December 31, 2021. The accumulated balances reported in AOCI in the Consolidated Balance Sheets for currency translation adjustments were a net loss of \$229 million and \$103 million as of December 31, 2023 and 2022, respectively. There was no tax effect related to the components of Other comprehensive income (loss) for all years presented.

Restricted net assets

The Company’s ability to pay dividends is primarily dependent on the Company receiving distributions of funds from its subsidiaries. Relevant PRC statutory laws and regulations permit payments of dividends by the Company’s PRC subsidiaries only out of their retained earnings, if any, as determined in accordance with PRC accounting standards and regulations. The results of operations reflected in the Consolidated Financial Statements prepared in accordance with U.S. GAAP differ from those reflected in the statutory financial statements of the Company’s subsidiaries.

In accordance with the PRC Regulations on Enterprises with Foreign Investment and the articles of association of the Company’s PRC subsidiaries, a foreign-invested enterprise established in the PRC is required to provide certain statutory reserves, namely general reserve fund, the enterprise expansion fund and staff welfare and bonus fund which are appropriated from net profit as reported in the enterprise’s PRC statutory accounts. A foreign-invested enterprise is required to allocate at least 10% of its annual after-tax profit to the general reserve until such reserve has reached 50% of its respective registered capital based on the enterprise’s PRC statutory accounts. Appropriations to the enterprise expansion fund and staff welfare and bonus fund are at the discretion of the board of directors for all foreign-invested enterprises. The aforementioned reserves can only be used for specific purposes and are not distributable as cash dividends.

As a result of these Chinese laws and regulations subject to the limit discussed above that require annual appropriations of 10% of after-tax income to be set aside, prior to payment of dividends as general reserve fund, the Company’s PRC subsidiaries are restricted in their ability to transfer a portion of their net assets to the Company in the form of dividend payments, loans or advances. The restricted net assets of the PRC subsidiaries were approximately \$1 billion as of December 31, 2023.

Furthermore, cash transfers from the Company’s PRC subsidiaries to its subsidiaries outside of China are subject to PRC government control of currency conversion. Shortages in the availability of foreign currency may restrict the ability of the PRC subsidiaries to remit sufficient foreign currency to pay dividends or other payments to the Company, or otherwise satisfy their foreign currency-denominated obligations.

Note 16 – Income Taxes

In December 2017, the U.S. enacted the Tax Act, which included a broad range of tax reforms. The Tax Act requires a U.S. shareholder to be subject to tax on Global Intangible Low Taxed Income (“GILTI”) earned by certain foreign subsidiaries. We have elected the option to account for current year GILTI tax as a period cost as incurred.

In August 2022, the IRA was signed into law in the U.S., which contains certain tax measures, including a Corporate Alternative Minimum Tax (“CAMT”) of 15% on certain large corporations. On December 27, 2022, the U.S. Treasury Department and the Internal Revenue Services (the “IRS”) released Notice 2023-7, announcing their intention to issue proposed regulations addressing the application of the new CAMT. In 2023, additional notices were released to continue to provide interim guidance regarding certain CAMT issues before proposed regulations are published. The Company will monitor the regulatory developments and continue to evaluate the impact on our financial statements, if any.

In December 2022, a refined Foreign Sourced Income Exemption (“FSIE”) regime was published in Hong Kong and took effect from January 1, 2023. Under the new FSIE regime, certain foreign sourced income would be deemed as being sourced from Hong Kong and chargeable to Hong Kong Profits Tax, if the recipient entity fails to meet the prescribed exception requirements. Certain dividends, interests and disposal gains, if any, received by us and our Hong Kong subsidiaries may be subject to the new tax regime. Based on our preliminary analysis, this legislation did not have a material impact on our financial statements. The Company will monitor the developments and continue to evaluate the impact, if any.

The Organization for Economic Cooperation and Development (the "OECD"), the European Union and other jurisdictions (including jurisdictions in which we have operations or presence) have committed to enacting substantial changes to numerous long-standing tax principles impacting how large multinational enterprises are taxed. In particular, the OECD's Pillar Two initiative introduces a 15% global minimum tax applied on a country-by-country basis and for which many jurisdictions have now committed to an effective enactment date starting January 1, 2024. The Company will monitor the regulatory developments and continue to evaluate the impact, if any.

U.S. and foreign income (loss) before taxes are set forth below:

	<u>2023</u>	<u>2022</u>	<u>2021</u>
U.S.	\$ 42	\$ 7	\$ (1)
Mainland China	1,165	686	1,424
Other Foreign	19	(6)	(31)
	<u>\$ 1,226</u>	<u>\$ 687</u>	<u>\$ 1,392</u>

The details of our income tax provision are set forth below:

	<u>2023</u>	<u>2022</u>	<u>2021</u>
Current: Federal	\$ 14	\$ 5	\$ —
Foreign	325	222	209
	<u>\$ 339</u>	<u>\$ 227</u>	<u>\$ 209</u>
Deferred: Federal	\$ (11)	\$ (6)	\$ (8)
Foreign	1	(14)	168
	<u>\$ (10)</u>	<u>\$ (20)</u>	<u>\$ 160</u>
	<u>\$ 329</u>	<u>\$ 207</u>	<u>\$ 369</u>

The reconciliation of income taxes calculated at the U.S. federal statutory rate to our effective tax rate is set forth below:

	<u>2023</u>		<u>2022</u>		<u>2021</u>	
U.S. federal statutory rate	\$ 257	21.0%	\$ 144	21.0%	\$ 292	21.0%
Statutory rate differential attributable to foreign operations	49	4.0	31	4.5	50	3.6
Withholding tax on distributable earnings	36	2.9	28	4.1	25	1.8
Effect of preferential tax benefit	(15)	(1.2)	(5)	(0.7)	(2)	(0.2)
Adjustments to reserves and prior years	(3)	(0.3)	(3)	(0.6)	(4)	(0.3)
Change in valuation allowances	4	0.3	9	1.3	9	0.7
Other, net	1	0.2	3	0.5	(1)	(0.1)
Effective income tax rate	<u>\$ 329</u>	<u>26.9%</u>	<u>\$ 207</u>	<u>30.1%</u>	<u>\$ 369</u>	<u>26.5%</u>

Statutory rate differential attributable to foreign operations. This item includes local taxes and shareholder-level taxes, net of foreign tax credits. A majority of our income is earned in China, which is generally subject to a 25% tax rate. The negative impact in 2023, 2022 and 2021 is primarily due to the U.S. federal statutory rate of 21%, which is lower than China’s statutory income tax rate.

Withholding tax on distributable earnings. This item represents withholding tax impact on planned or actual repatriation of earnings outside of China, at the withholding tax rate of 5% or 10% depending on the manner of repatriation and the applicable tax treaties or tax arrangements.

Effect of preferential tax benefit. This item represents the benefits from preferential tax rates applied at certain qualified Chinese subsidiaries.

Adjustments to reserves and prior years. This item includes: (1) changes in tax reserves, including interest thereon, established for potential exposure we may incur if a taxing authority takes a position on a matter contrary to our position; and (2) the effects of reconciling income tax amounts recorded in our Consolidated Statements of Income to amounts reflected on our tax returns, including any adjustments to the Consolidated Balance Sheets. The impact of certain effects or changes may affect items reflected in ‘Statutory rate differential attributable to foreign operations’.

Change in valuation allowances. This item relates to changes for deferred tax assets generated or utilized during the current year and changes in our judgment regarding the likelihood of using deferred tax assets that existed at the beginning of the year. The impact of certain changes may affect items reflected in ‘Statutory rate differential attributable to foreign operations’.

Others. This item primarily includes the impact of permanent differences related to current year earnings, gain or loss on investment in equity securities, as well as U.S. tax credits and deductions.

The details of 2023 and 2022 deferred tax assets (liabilities) are set forth below:

	2023			2022		
	Assets	Liabilities	Total	Assets	Liabilities	Total
Operating losses and tax credit carryforwards	\$ 42	\$ —	\$ 42	\$ 47	\$ —	\$ 47
Tax benefit from Little Sheep restructuring	14	—	14	15	—	15
Employee compensation and benefits	12	—	12	12	—	12
Deferred income and other	112	—	112	94	—	94
Lease	600	(556)	44	605	(556)	49
Property, plant and equipment	—	(144)	(144)	—	(136)	(136)
Intangible assets	—	(38)	(38)	—	(40)	(40)
Gain from re-measurement of equity interest upon acquisition	—	(219)	(219)	—	(226)	(226)
Withholding tax on distributable earnings	—	(33)	(33)	—	(34)	(34)
Unrealized gains from equity securities	—	(1)	(1)	—	(12)	(12)
Others	8	—	8	11	—	11
Valuation Allowance	(58)	—	(58)	(57)	—	(57)
Net deferred tax assets (liabilities)	<u>\$ 730</u>	<u>(991)</u>	<u>\$ (261)</u>	<u>\$ 727</u>	<u>(1,004)</u>	<u>\$ (277)</u>

We have investments in our foreign subsidiaries where the carrying values for financial reporting exceed the tax basis. Except for the planned but yet to be distributed earnings, we have not provided deferred tax on the portion of the excess that we believe is indefinitely reinvested, as we have the ability and intent to indefinitely postpone the basis differences from reversing with a tax consequence. The Company’s separation from YUM was intended to qualify as a tax-free reorganization for U.S. income tax purposes resulting in the excess of financial reporting basis over tax basis in our investment in the China business continuing to be indefinitely reinvested. The excess of financial reporting basis over tax basis as of December 31, 2017 was subject to the one-time transition tax under the Tax Act as a deemed repatriation of accumulated undistributed earnings from the foreign subsidiaries. However, we continue to believe that the portion of the excess of financial reporting basis over tax basis (including earnings and profits subject to the one-time transition tax) is indefinitely reinvested in our foreign subsidiaries for foreign withholding tax purposes. We estimate that our total temporary difference for which we have not provided foreign withholding taxes is approximately \$3 billion at December 31, 2023. The foreign withholding tax rate on this amount is 5% or 10% depending on the manner of repatriation and the applicable tax treaties or tax arrangements.

At December 31, 2023, the Company had operating loss carryforwards of \$177 million, primarily related to certain underperforming entities, most of which will expire by 2028. These losses are being carried forward in jurisdictions where we are permitted to use tax losses from prior periods to reduce future taxable income.

Cash payments for tax liabilities on income tax returns filed were \$324 million, \$204 million and \$255 million in 2023, 2022 and 2021, respectively.

We recognize the benefit of positions taken or expected to be taken in tax returns in the financial statements when it is more likely than not that the position would be sustained upon examination by tax authorities. A recognized tax position is measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

	<u>2023</u>	<u>2022</u>
Beginning of Year	\$ 21	\$ 20
Additions on tax positions	5	6
Reductions due to statute expiration	(6)	(5)
End of Year	<u>\$ 20</u>	<u>\$ 21</u>

In 2023 and 2022, our unrecognized tax benefits were increased by \$5 million and \$6 million, respectively. The unrecognized tax benefits balance of \$20 million as of December 31, 2023 related to the uncertainty with regard to the deductibility of certain business expenses incurred, all of which, if recognized upon audit settlement or statute expiration, would affect the effective tax rate. The Company believes it is reasonably possible its unrecognized tax benefits of \$20 million as of December 31, 2023, which is included in Other liabilities on the Consolidated Balance Sheet, may decrease by approximately \$5 million in the next 12 months, which if recognized, would affect the 2024 effective tax rate. The accrued interest and penalties related to income taxes at December 31, 2023 and 2022 are set forth below:

	<u>2023</u>	<u>2022</u>
Accrued interest and penalties	\$ 4	\$ 4

During 2023, 2022 and 2021, a net benefit of nil, \$1 million and nil for interest and penalties was recognized in our Consolidated Statements of Income as components of our income tax provision, respectively.

The Company's results are subject to examination in the U.S. federal jurisdiction as well as various U.S. state jurisdictions as part of YUM's and our own income tax filings, and separately in foreign jurisdictions. Any liability arising from these examinations related to periods prior to the separation is expected to be settled among the Company, YCCL and YUM in accordance with the tax matters agreement we entered into in connection with the separation.

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

Note 17 – Segment Reporting

The Company has two reportable segments: KFC and Pizza Hut. Our non-reportable operating segments, including the operations of Lavazza, Huang Ji Huang, Little Sheep and Taco Bell, our delivery operating segment and our e-commerce business, are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in the aggregate. For 2022 and 2021, All Other Segments also included COFFii & JOY and East Dawning.

	<u>2023</u>						
	<u>KFC</u>	<u>Pizza Hut</u>	<u>All Other Segments</u>	<u>Corporate and Unallocated^(a)</u>	<u>Combined</u>	<u>Elimination</u>	<u>Consolidated</u>
Revenues							
Revenue from external customers	\$ 8,240	\$ 2,246	\$ 199	\$ 293	\$ 10,978	\$ —	\$ 10,978
Inter-segment revenue	—	—	580	—	580	(580)	—
Total	<u>\$ 8,240</u>	<u>\$ 2,246</u>	<u>\$ 779</u>	<u>\$ 293</u>	<u>\$ 11,558</u>	<u>\$ (580)</u>	<u>\$ 10,978</u>

	2022						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenues							
Revenue from external customers	\$ 7,219	\$ 1,960	\$ 155	\$ 235	\$ 9,569	\$ —	\$ 9,569
Inter-segment revenue	—	—	516	18	534	(534)	—
Total	<u>\$ 7,219</u>	<u>\$ 1,960</u>	<u>\$ 671</u>	<u>\$ 253</u>	<u>\$ 10,103</u>	<u>\$ (534)</u>	<u>\$ 9,569</u>

	2021						
	KFC	Pizza Hut	All Other Segments	Corporate and Unallocated ^(a)	Combined	Elimination	Consolidated
Revenues							
Revenue from external customers	\$ 7,003	\$ 2,109	\$ 227	\$ 514	\$ 9,853	\$ —	\$ 9,853
Inter-segment revenue	—	—	246	6	252	(252)	—
Total	<u>\$ 7,003</u>	<u>\$ 2,109</u>	<u>\$ 473</u>	<u>\$ 520</u>	<u>\$ 10,105</u>	<u>\$ (252)</u>	<u>\$ 9,853</u>

Operating Profit (Loss)

	2023	2022	2021
KFC ^(b)	\$ 1,202	\$ 787	\$ 827
Pizza Hut	142	70	111
All Other Segments	(31)	(50)	(29)
Unallocated revenues from transactions with franchisees ^(c)	249	211	500
Unallocated Other revenues	44	42	20
Unallocated expenses for transactions with franchisees ^(c)	(246)	(211)	(497)
Unallocated Other operating costs and expenses	(42)	(39)	(17)
Unallocated and corporate G&A expenses	(214)	(184)	(171)
Unallocated Other income ^(d)	2	3	642
Operating Profit	\$ 1,106	\$ 629	\$ 1,386
Interest income, net ^(a)	169	84	60
Investment loss ^(a)	(49)	(26)	(54)
Income Before Income Taxes and Equity in			
Net Earnings (Losses) from Equity Method Investments	<u>\$ 1,226</u>	<u>\$ 687</u>	<u>\$ 1,392</u>

Depreciation and Amortization

	2023	2022	2021
KFC	\$ 319	\$ 460	\$ 378
Pizza Hut	93	108	111
All Other Segments	9	10	9
Corporate and Unallocated	32	24	18
	<u>\$ 453</u>	<u>\$ 602</u>	<u>\$ 516</u>

Impairment Charges

	2023	2022	2021
KFC ^(e)	\$ 18	\$ 31	\$ 30
Pizza Hut ^(e)	10	9	13
All Other Segments ^(e)	9	11	5
	<u>\$ 37</u>	<u>\$ 51</u>	<u>\$ 48</u>

Capital Spending

	2023	2022	2021
KFC	\$ 358	\$ 327	\$ 398
Pizza Hut	113	116	98
All Other Segments	18	16	16
Corporate and Unallocated	221	220	177
	<u>\$ 710</u>	<u>\$ 679</u>	<u>\$ 689</u>

	Total Assets	
	2023	2022
KFC	\$ 5,371	\$ 5,296
Pizza Hut	904	880
All Other Segments	347	381
Corporate and Unallocated ^(f)	5,409	5,269
	<u>\$ 12,031</u>	<u>\$ 11,826</u>

- (a) Amounts have not been allocated to any segment for performance reporting purposes.
- (b) Includes equity income of \$50 million from our investment in Hangzhou KFC in the year ended 2021 before we consolidated its results upon completion of the acquisition. See Note 3 for details.
- (c) Primarily includes revenues and associated expenses of transactions with franchisees derived from the Company's central procurement model whereby the Company centrally purchases substantially all food and paper products from suppliers then sells and delivers to KFC and Pizza Hut restaurants, including franchisees and former unconsolidated affiliates. Amounts have not been allocated to any segment for purposes of making operating decisions or assessing financial performance as the transactions are deemed corporate revenues and expenses in nature.
- (d) In 2021, unallocated other income primarily includes gain from re-measurement of previously held equity interest in connection with the acquisition of Hangzhou KFC and the Lavazza joint venture. See Note 3 for more information.
- (e) Primarily includes store closure impairment charges and restaurant-level impairment charges resulting from our semi-annual impairment evaluation. See Note 12 for more information.
- (f) Primarily includes cash and cash equivalents, short-term investments, long-term bank deposits and notes, equity investments, and inventories that are centrally managed and PP&E that are not specifically identifiable within each segment.

As substantially all of the Company's revenue is derived from the PRC and substantially all of the Company's long-lived assets are located in the PRC, no geographical information is presented. In addition, revenue derived from and long-lived assets located in the U.S., the Company's country of domicile, are immaterial.

Note 18 – Contingencies

Indemnification of China Tax on Indirect Transfers of Assets

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

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

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

Indemnification of Officers and Directors

The Company's amended and restated certificate of incorporation and amended and restated bylaws include provisions that require the Company to indemnify directors or officers for monetary damages for actions taken as a director or officer of the Company or while serving at the Company's request as a director or officer or another position at another corporation or enterprise, as the case may be. The Company purchases standard directors and officers insurance to cover claims or a portion of the claims made against its directors and officers. Since a maximum obligation is not explicitly stated in the Company's bylaws or in the indemnification agreements and will depend on the facts and circumstances that arise out of any future claims, the overall maximum amount of the obligations cannot be reasonably estimated. The Company has not been required to make payments related to these obligations, and the fair value for these obligations is zero as of December 31, 2023.

Legal Proceedings

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

Note 19 – Subsequent Events

Cash Dividend

On February 6, 2024, the Company announced that the Board of Directors declared a cash dividend of \$0.16 per share on Yum China's common stock, payable on March 26, 2024, to stockholders of record as of the close of business on March 5, 2024. Total estimated cash dividend payable is approximately \$64 million.

Note 20 – Particulars of Principal Subsidiaries of the Company

The following list contains the particulars of subsidiaries which principally affected the results, assets or liabilities of the Company.

Name of Major Subsidiaries	Place of Incorporation and Operation	Issued and Fully Paid Share Capital	Equity Interest Held	Principal Activities
<i>Major subsidiaries engaging in investment holding and/or the operation of our restaurants</i>				
Bai Sheng Restaurants China Holdings Limited	Hong Kong	HKD 993,255,340	100.0%	Investment holding and operating a Little Sheep restaurant in Hong Kong
Yum! Restaurants (China) Investment Company Limited	PRC	USD 128,127,095	100.0%	Investment holding
Yum! Restaurants (Shenyang) Co., Ltd.		USD 12,200,000	100.0%	Operating our KFC, Pizza Hut and Taco Bell restaurants in respective areas
Yum! Restaurants (Guangdong) Co., Ltd.		USD 45,406,000	100.0%	
Yum! Restaurants (Chengdu) Co., Ltd.		USD 4,200,000	100.0%	
Yum! Restaurants (Wuhan) Co., Ltd.		USD 10,100,000	100.0%	
Yum! Restaurants (Shenzhen) Co. Ltd.		USD 5,100,000	100.0%	
Beijing KFC Co., Ltd.		RMB 58,675,169	70.0%	
Shanghai KFC Co., Ltd.		USD 27,010,000	58.0%	
Wuxi KFC Co. Ltd.		USD 6,200,000	83.0%	
Hangzhou KFC Co., Ltd.		USD 21,500,000	59.6%	
Suzhou KFC Co., Ltd.		USD 10,000,000	92.0%	
Nanjing KFC Co., Ltd.		USD 19,060,000	100.0%	
Qingdao KFC Co., Ltd.		USD 8,600,000	100.0%	
Tianjin KFC Co., Ltd.		USD 7,100,000	100.0%	
Changsha KFC Co., Ltd.		USD 2,100,000	100.0%	
Nanning KFC Co., Ltd.	USD 2,700,000	100.0%		
Shanghai Pizza Hut Co., Ltd.	USD 13,173,000	100.0%		
Beijing Pizza Hut Co., Ltd.	RMB 23,508,800	100.0%		
Inner Mongolia Little Sheep Catering Chain Co., Ltd.		USD 76,180,000	100.0%	Operating our Little Sheep business
Beijing Huang Ji Huang Catering Management Co., Ltd.		RMB 1,000,000	93.3%	Operating our Huang Ji Huang business
Yi Bai Coffee (Shanghai) Co., Ltd.		USD 214,500,000	65.0%	Operating Lavazza business in China
<i>Major subsidiaries engaging in the provision of support and services to other entities in our system</i>				
Yum! Restaurants Consulting (Shanghai) Company Limited	PRC	USD 5,000,000	100.0%	Sub-licensing the brands licensed from YUM; performing headquarters functions and providing support and services to other entities in our system
HuanSheng Advertising (Shanghai) Company Limited		RMB 500,000	100.0%	Marketing and advertising services to other entities in our system
Huansheng E-Commerce (Shanghai) Co., Ltd.		RMB 5,000,200	100.0%	Operating our e-commerce business
Yum! (Shanghai) Food Co., Ltd.		USD 17,000,000	100.0%	Purchase of food, paper products and equipment for other entities in our system
Shanghai You Song Jia Information and Technology Co., Ltd.		RMB 500,000	100.0%	Managing delivery services for our restaurants

All our subsidiaries established in the PRC are limited liability companies.

Note 21 – Statement of Financial Position of the Company (Parent Company Only)

	<u>2023</u>	<u>2022</u>
ASSETS		
Current Assets		
Cash and cash equivalents	\$ 57	\$ 178
Short-term investments	321	790
Prepaid expenses and other current assets	<u>13</u>	<u>14</u>
Total Current Assets	391	982
Loan due from subsidiaries	41	505
Long-term bank deposits and notes	262	—
Long term investment in subsidiaries	<u>5,755</u>	<u>5,046</u>
Total Assets	<u><u>6,449</u></u>	<u><u>6,533</u></u>
LIABILITIES AND EQUITY		
Current Liabilities		
Accounts payable and other current liabilities	<u>28</u>	<u>13</u>
Total Current Liabilities	28	13
Deferred income tax liabilities	1	11
Other liabilities	<u>15</u>	<u>27</u>
Total Liabilities	<u>44</u>	<u>51</u>
Equity		
Common stock, \$0.01 par value; 1,000 million shares authorized; 407 million shares and 419 million shares issued and outstanding at December 31, 2023 and 2022, respectively.	4	4
Additional paid-in capital	4,320	4,390
Retained earnings	2,310	2,191
Accumulated other comprehensive loss	<u>(229)</u>	<u>(103)</u>
Total Yum China Holdings, Inc. Stockholders' Equity	6,405	6,482
Total Liabilities and Equity	<u><u>\$ 6,449</u></u>	<u><u>\$ 6,533</u></u>

A summary of the Company's statement of changes in equity is as follows:

	Common Stock		Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)		Treasury Stock		Total Equity
	Shares	Amount			Shares	Amount			
Balance at December 31, 2020	440	\$ 4	\$ 4,658	\$ 2,105	\$ 167	(20)	\$ (728)	\$ 6,206	
Net Income				990	101			990	
Foreign currency translation adjustments								101	
Comprehensive income								1,091	
Cash dividends declared (\$0.48 per common share)				(203)				(203)	
Repurchase of shares of common stock	2	—	(3)				(75)	(75)	
Exercise and vesting of share-based awards	8	—	41			(1)		(3)	
Share-based compensation			(1)					41	
Revaluation of redeemable noncontrolling interest								(1)	
Balance at December 31, 2021	449	\$ 4	\$ 4,695	\$ 2,892	\$ 268	(21)	\$ (803)	\$ 7,056	
Net Income				442	(371)			442	
Foreign currency translation adjustments								(371)	
Comprehensive income								71	
Cash dividends declared								(202)	
Repurchase and retirement of shares (\$0.48 per common share)	(31)	—	(328)	(202)		21	803	(466)	
Exercise and vesting of share-based awards	1	—	(3)	(941)				(3)	
Acquisition of noncontrolling interests			(15)					(15)	
Share-based compensation			41					41	
Balance at December 31, 2022	419	\$ 4	\$ 4,390	\$ 2,191	\$ (103)	—	\$ —	\$ 6,482	
Net Income				827	(126)			827	
Foreign currency translation adjustments								(126)	
Comprehensive income								701	
Cash dividends declared								(216)	
Repurchase and retirement of shares (\$0.52 per common share)	(12)	—	(131)	(216)				(623)	
Exercise and vesting of share-based awards	1	—	(2)	(492)				(2)	
Share-based compensation			63					63	
Balance at December 31, 2023	407	\$ 4	\$ 4,320	\$ 2,310	\$ (229)	—	\$ —	\$ 6,405	

The above statement of financial position of the Company has been prepared in accordance with U.S. GAAP, and in conformity with the disclosure requirements of the Hong Kong Listing Rules and the Hong Kong Companies Ordinance. The Company's accounting policies are the same as set out in the consolidated financial statement and the equity method of accounting has been adopted for investment in subsidiaries based on ASC 323, Investments – Equity Method and Joint Ventures. The above financial information of the Company should be read in conjunction with the Company's consolidated financial statement.

Note 22 – Directors’ Remuneration

Our non-employee directors were each compensated with an annual retainer, payable in Company common stock or, if requested by a director, up to one-half in cash. In addition to the annual retainer paid to all non-employee directors, the Chairman of the Board, committee chairs and committee members received additional stock retainers.

Total remuneration to Joey Wat, chief executive and employee director, includes base salary, annual performance-based cash bonus, share-based awards, benefits, tax reimbursements, and pension scheme contributions.

The remuneration of each director including the chief executive is set out below:

Name	2023							
	Fees earned or paid in cash	Salaries	Performance related bonuses	Share-based awards ^(a)	Pension scheme contributions ^(b)	Allowances and benefits ^(c)	Others	Total remuneration*
(in US\$ thousands)								
Employee director and chief executive								
Joey Wat	—	1,425	4,916	10,000	143	3,852	—	20,336
Independent non-executive directors								
Peter A. Bassi ^(d)	158	—	—	203	—	—	50	410
Edouard Ettedgui	158	—	—	190	—	—	—	348
Fred Hu	—	—	—	560	—	—	—	560
Ruby Lu	—	—	—	350	—	—	—	350
Zili Shao	158	—	—	195	—	—	—	353
William Wang	—	—	—	328	—	—	—	328
Min (Jenny) Zhang	158	—	—	198	—	—	—	355
Christina Xiaojing Zhu	—	—	—	315	—	—	—	315
David Hoffmann ^(e)	—	—	—	305	—	—	—	305
	630	—	—	2,642	—	—	50	3,322
	630	1,425	4,916	12,642	143	3,852	50	23,658
2022								
Name	Fees earned or paid in cash	Salaries	Performance related bonuses	Share-based awards ^(a)	Pension scheme contributions ^(b)	Allowances and benefits ^(c)	Others	Total remuneration*
(in US\$ thousands)								
Employee director and chief executive								
Joey Wat	—	1,419	4,788	9,285	142	259	—	15,893
Independent non-executive directors								
Peter A. Bassi	138	—	—	168	—	—	—	305
Edouard Ettedgui	—	—	—	275	—	—	—	275
Cyril Han ^(f)	—	—	—	275	—	—	—	275
Louis T. Hsieh ^(f)	138	—	—	138	—	—	—	275
Fred Hu	225	—	—	290	—	—	—	515
Ruby Lu	—	—	—	295	—	—	—	295
Zili Shao	—	—	—	290	—	—	—	290
William Wang	—	—	—	275	—	—	—	275
Min (Jenny) Zhang	138	—	—	138	—	—	—	275
	638	—	—	2,143	—	—	—	2,780
	638	1,419	4,788	11,428	142	259	—	18,673

Name	2021							Total remuneration*
	Fees earned or paid in cash	Salaries	Performance related bonuses	Share-based awards ^(a)	Pension scheme contributions ^(b)	Allowances and benefits ^(c)	Others	
(in US\$ thousands)								
Employee director and chief executive								
Joey Wat	—	1,342	3,607	8,704	134	2,769	—	16,556
Independent non-executive directors								
Peter A. Bassi	138			168				305
Edouard Ettedgui	—			275				275
Cyril Han	—			275				275
Louis T. Hsieh	138			138				275
Fred Hu	225			290				515
Ruby Lu	—			295				295
Zili Shao	—			290				290
William Wang	—			275				275
Min (Jenny) Zhang	138			138				275
Christian L. Campbell ^(e)	—			—			128	128
	638	—	—	2,143	—	—	128	2,908
	638	1,342	3,607	10,846	134	2,769	128	19,463

*: Total remuneration may not add due to rounding.

- (a) The amounts reported in this column represent the grant date fair value of the share-based awards, including SARs, RSUs, and PSUs, granted to chief executive and employee director in the applicable year and for 2022, the amounts also included the incremental fair value of the 2020 annual PSUs due to the modifications approved by the Compensation Committee of the board of directors, and not the expense recognized during the applicable reporting year. The Company recognizes compensation expense on a straight-line basis over the vesting period based on their grant date fair value and, if applicable, estimated payout when performance conditions are probable of being achieved. The amounts expensed as share-based compensation are impacted by the estimated payout, which may change in accordance with the estimated and actual achievement of the underlying performance goals during the service period. Together with share-based awards granted in prior years, total share-based compensation expenses recognized were \$15 million, \$8 million and \$8 million for the years ended December 31, 2023, 2022 and 2021, respectively. During the year ended December 31, 2023, the amount recognized as share-based compensation expense included an increase recognized in relation to Partner PSU awards granted in 2020 and annual PSU awards granted in 2021 to the chief executive and employee director. Such PSU awards vested as of December 31, 2023, with the actual payout higher than the past estimates used to determine the expense during the service period. Comparative tabular amounts presented have been reclassified to conform to the current year's presentation to facilitate comparison. See Note 2 and Note 14 for additional information.
- (b) The pension scheme contribution received by the employee director represents retirement benefits under Bai Sheng Restaurants China Holdings Limited Retirement Scheme, with further details set out in Note 13.
- (c) Allowances and benefits primarily represent legacy tax reimbursement arrangements entered into with the Company's former parent, which provide for the reimbursement of taxes incurred with respect to the gains realized upon exercise of share-based awards granted before 2018. These legacy tax reimbursement arrangements do not represent any new benefits but rather the settlement of existing contractual agreements that the Company is required to satisfy.
- (d) Mr. Bassi received an additional award in the amount of \$50,000 for his contribution to a project in 2022 at the request of the Board, of which 50% was paid in cash and 50% was paid in stock in June 2023.
- (e) Mr. Hoffmann was appointed as a director by the Board in July 2023 and received a prorated director annual retainer for 2023.
- (f) Messrs. Han and Hsieh did not stand for re-election at the Annual Meeting of Stockholders in May 2022. While Messrs. Han and Hsieh served as directors before May during 2022, they did not receive any compensation in 2022, as their 2021 annual retainer, which was fully recognized in 2021 upon grant, represented compensation for their services until May 2022.

- (g) Mr. Campbell did not stand for re-election at the Annual Meeting of Stockholders in May 2021. While Mr. Campbell served as a director before May during 2021, he did not receive any compensation in 2021, as his 2020 equity grant, which was fully recognized in 2020 upon grant, represented compensation for his service until May 2021. On July 15, 2021, Mr. Campbell entered into a senior advisor service contract with the Company, pursuant to which Mr. Campbell provided governance and other advisory services to the Board of Directors from July 1, 2021, with a monthly retainer of \$21,000. Pursuant to the senior advisor service contract, hours in excess of 42 hours per quarter were paid at \$1,500 per hour.

Except as mentioned above, there was no other remuneration payable to directors during the years ended December 31, 2023, 2022 and 2021.

Note 23 – Five Highest Paid Individuals

The five individuals whose emoluments are the highest in the Company included one chief executive whose emoluments are reflected in the analysis shown in Note 22.

Details of the total remuneration for the remaining four highest paid employees, who are not directors of the Company, are as follows for the years ended December 31, 2023, 2022 and 2021:

	2023	2022	2021
Salaries, allowances and benefits in kind	\$ 3	\$ 4	\$ 4
Performance related bonuses	4	4	3
Share-based awards ^(a)	6	7	8
Pension scheme contributions	—	—	—
Total remuneration*	<u>\$ 14</u>	<u>\$ 14</u>	<u>\$ 15</u>

*Total remuneration may not add due to rounding.

- (a) The amounts represent the grant date fair value of the share-based awards, including SARs, RSUs, and PSUs, granted to executives and employees in the applicable year and for 2022, the amounts also included the incremental fair value of the 2020 annual PSUs due to the modifications approved by the Compensation Committee of the board of directors, and not the expense recognized during the applicable reporting year. The Company recognizes share-based awards to employees as compensation expense on a straight-line basis over the service period based on their fair value on the date of grant and, if applicable, estimated payout based on the probability of the performance conditions being achieved. The amounts expensed as share-based compensation are impacted by the estimated payout, which may change in accordance with the estimated and actual achievement of the underlying performance goals during the service period. Together with share-based awards granted in prior years, total share-based compensation expenses recognized for remaining four highest paid employees were \$11 million, \$6 million and \$6 million for the year ended December 31, 2023, 2022 and 2021, respectively. During the year ended December 31, 2023, the amount recognized as share-based compensation expense included an increase recognized in relation to Partner PSU awards granted in 2020 and annual PSU awards granted in 2021. Such PSU awards vested as of December 31, 2023 with higher actual results as compared to the past estimates used to determine the expense during the service period. Comparative tabular amounts presented have been reclassified to conform to the current year's presentation to facilitate comparison. See Note 2 and Note 14 for additional information.

The number of highest paid non-director employees whose total remuneration fell within the following bands, is as follows:

	2023	2022	2021
HK 19,000,001 to HK 19,500,000	—	—	1
HK 20,500,001 to HK 21,000,000	—	1	—
HK 21,000,001 to HK 21,500,000	1	—	—
HK 22,500,001 to HK 23,000,000	—	1	—
HK 23,500,001 to HK 24,000,000	2	—	—
HK 24,500,001 to HK 25,000,000	—	—	1
HK 31,500,001 to HK 32,000,000	—	1	1
HK 36,500,001 to HK 37,000,000	—	1	—
HK 37,500,001 to HK 38,000,000	1	—	—
HK 39,500,001 to HK 40,000,000	—	—	1
	<u>4</u>	<u>4</u>	<u>4</u>

Note 24 – Reconciliation between U.S. GAAP and International Financial Reporting Standards

The Company's consolidated financial statements are prepared in accordance with U.S. GAAP, which differ in certain respects from International Financial Reporting Standards ("IFRS"). The effects of material differences between U.S. GAAP and IFRS are as follows:

(i) Reconciliation of consolidated statements of income:

	For the year ended December 31, 2023					
	Amounts as reported under U.S. GAAP	Lease ^(a)	Share-based compensation ^(b)	Deferred taxes on share-based compensation ^(c)	Long-lived assets impairment ^(d)	Amounts under IFRS
Revenues						
Franchise fees and income	\$ 89	(4)				\$ 85
Other revenues	126	(1)				125
Total revenues	10,978	(5)				10,973
Costs and Expenses, Net						
Company restaurants						
Payroll and employee benefits	2,725					2,725
Occupancy and other operating expenses	2,752	(75)			(6)	2,671
Company restaurant expenses	8,701	(75)			(6)	8,620
General and administrative expenses	638	(3)	3			638
Franchise expenses	36	(4)				32
Other operating costs and expenses	112	(1)				111
Closures and impairment expenses, net	29	1			4	34
Total costs and expenses, net	9,872	(82)	3		(2)	9,791
Operating Profit	1,106	77	(3)		2	1,182
Interest income (expense), net	169	(112)				57
Income Before Income Taxes and Equity in Net Earnings (Losses) from Equity Method Investments	1,226	(35)	(3)		2	1,190
Income tax provision	(329)	8			(6)	(327)
Net income – including noncontrolling interests	901	(27)	(3)		(6)	867
Net income – noncontrolling interests	74	(4)				70
Net Income – Yum China Holdings, Inc.	\$ 827	\$(23)	\$(3)	\$(6)	2	\$ 797

For the year ended December 31, 2022
IFRS adjustments

	Amounts as reported under U.S. GAAP	Lease ^(a)	Share-based compensation ^(b)	Deferred taxes on share-based compensation ^(c)	Long-lived assets impairment ^(d)	Amounts under IFRS
Revenues						
Franchise fees and income	\$ 81	(5)				\$ 76
Other revenues	91	(1)				90
Total revenues	9,569	(6)				9,563
Costs and Expenses, Net						
Company restaurants						
Payroll and employee benefits	2,389					2,389
Occupancy and other operating expenses	2,604	(74)			(5)	2,525
Company restaurant expenses	7,829	(74)			(5)	7,750
General and administrative expenses	594	(4)	2			592
Franchise expenses	34	(5)				29
Closures and impairment expenses, net	32	2			(1)	33
Total costs and expenses, net	8,940	(81)	2		(6)	8,855
Operating Profit	629	75	(2)		6	708
Interest income (expense), net	84	(130)				(46)
Income Before Income Taxes and Equity in Net Earnings (Losses) from Equity Method Investments	687	(55)	(2)		6	636
Income tax provision	(207)	13		(2)	(2)	(198)
Net income – including noncontrolling interests	478	(42)	(2)	(2)	4	436
Net income – noncontrolling interests	36	(5)				31
Net Income – Yum China Holdings, Inc.	\$ 442	\$(37)	\$(2)	\$(2)	\$ 4	\$ 405

For the year ended December 31, 2021
IFRS adjustments

	Amounts as reported under U.S. GAAP	Lease^(a)	Share-based compensation^(b)	Deferred taxes on share-based compensation^(c)	Long-lived assets impairment^(d)	Amounts under IFRS
Revenues						
Franchise fees and income	\$ 153	(5)				\$ 148
Other revenues	76	(1)				75
Total revenues	9,853	(6)				9,847
Costs and Expenses, Net						
Company restaurants						
Payroll and employee benefits	2,258					2,258
Occupancy and other operating expenses	2,664	(62)			(9)	2,593
Company restaurant expenses	7,734	(62)			(9)	7,663
General and administrative expenses	564	(3)	1			562
Franchise expenses	64	(5)				59
Closures and impairment expenses, net	34	7			(5)	36
Other expenses (income), net	(643)	(3)				(646)
Total costs and expenses, net	8,467	(66)	1		(14)	8,388
Operating Profit	1,386	60	(1)		14	1,459
Interest income (expense), net	60	(137)				(77)
Income Before Income Taxes and Equity in Net Earnings (Losses) from Equity Method Investments	1,392	(77)	(1)		14	1,328
Income tax provision	(369)	18		(5)	(3)	(359)
Net income – including noncontrolling interests	1,023	(59)	(1)	(5)	11	969
Net income – noncontrolling interests	33	(4)			1	30
Net Income – Yum China Holdings, Inc.	\$ 990	\$(55)	\$(1)	\$(5)	\$ 10	\$ 939

(ii) Reconciliation of consolidated balance sheets

As of December 31, 2023
IFRS adjustments

	Amounts as reported under U.S. GAAP	Lease ^(a) compensation ^(b)	Share-based compensation ^(b)	Deferred taxes on share-based compensation ^(c)	Long-lived assets impairment ^(d)	Redeemable noncontrolling interest ^(e)	Amounts under IFRS
Current Assets							
Accounts receivable, net	\$ 68	\$ 5					\$ 73
Total Current Assets	3,431	5					3,436
Property, plant and equipment, net	2,310	(10)			(9)		2,291
Operating lease right-of-use assets	2,217	(85)					2,132
Deferred income taxes	129			1	2		132
Other assets	265	10					275
Total Assets	12,031	(80)		1	(7)		11,945
Current Liabilities							
Accounts payable and other current liabilities	2,164	1					2,165
Total Current Liabilities	2,422	1					2,423
Non-current operating and finance lease liabilities	1,943	2					1,945
Deferred income tax liabilities	390	(19)					371
Other liabilities	157					13	170
Total Liabilities	4,912	(16)				13	4,909
Redeemable Noncontrolling Interest	13					(13)	—
Equity							
Additional paid-in capital	4,320		6	12			4,338
Retained earnings	2,310	(50)	(6)	(11)	(7)		2,236
Accumulated other comprehensive loss	(229)	—					(229)
Total Yum China Holdings, Inc. Stockholders' Equity	6,405	(50)	—	1	(7)	—	6,349
Noncontrolling interests	701	(14)					687
Total Equity	7,106	(64)	—	1	(7)	—	7,036
Total Liabilities, Redeemable Noncontrolling Interest and Equity	\$ 12,031	\$ (80)	\$ —	\$ 1	\$ (7)	\$ —	\$ 11,945

As of December 31, 2022
IFRS adjustments

Amounts as reported under U.S. GAAP	Lease ^(a)	Share-based compensation ^(b)	Deferred taxes on share-based compensation ^(c)	Long-lived assets impairment ^(d)	Redeemable noncontrolling interest ^(e)	Amounts under IFRS
Current Assets						
Accounts receivable, net	\$ 64	5				\$ 69
Total Current Assets	3,940	5				3,945
Property, plant and equipment, net	2,118	(9)		(12)		2,097
Operating lease right-of-use assets	2,219	(54)				2,165
Deferred income taxes	113		6	3		122
Other assets	343	9				352
Total Assets	11,826	(49)	6	(9)		11,774
Current Liabilities						
Accounts payable and other current liabilities	2,098	1				2,099
Total Current Liabilities	2,166	1				2,167
Non-current operating and finance lease liabilities	1,948	2				1,950
Deferred income tax liabilities	390	(11)				379
Other liabilities	162				12	174
Total Liabilities	4,666	(8)			12	4,670
Redeemable Noncontrolling Interest	12				(12)	—
Equity						
Additional paid-in capital	4,390		3	11		4,404
Retained earnings	2,191	(27)	(3)	(5)	(9)	2,147
Accumulated other comprehensive loss	(103)	(5)		1		(107)
Total Yum China Holdings, Inc. Stockholders' Equity	6,482	(32)	—	6	(8)	6,448
Noncontrolling interests	666	(9)			(1)	656
Total Equity	7,148	(41)	—	6	(9)	7,104
Total Liabilities, Redeemable Noncontrolling Interest and Equity	\$ 11,826	\$ (49)	\$ —	\$ 6	\$ (9)	\$ 11,774

Notes:

(a) Lease

Lease Amortization

Under U.S. GAAP, there is a dual-classification lease accounting model for lessees: finance leases and operating leases. For operating leases, unless the right-of-use asset has been impaired, the amortization of right-of-use assets and the interest expense of lease liabilities are recorded together as a single lease cost on a straight-line basis over the remaining lease term.

Under IFRS, all leases are classified as finance leases, where right-of-use assets are amortized on a straight-line basis and recorded in Costs and Expenses, Net above Operating profit, while interest expense of lease liabilities are recorded in Interest income (expense), net under the effective interest method, which results in higher expenses at the beginning of the lease term and lower expenses near the end of the lease term.

Sublease classification

Under U.S. GAAP, an intermediate lessor classifies a sub-lease as a finance lease or as an operating lease by reference to the underlying asset. Under IFRS sub-lease classification is determined by reference to the right-of-use asset arising from the head lease, which may more frequently result in finance lease classification under IFRS.

An intermediate lessor in an operating lease continues to amortize the underlying right-of-use asset, and records lease income on a straight-line basis over the lease term. An intermediate lessor in a finance lease derecognizes the leased asset and records a net investment in the lease at lease commencement, in addition to any selling profit or loss. The lessor records lease income on its net investment in lease under the effective interest method.

(b) Share-based compensation

Share-based compensation with graded vesting feature

Under U.S. GAAP, the Company has elected to recognize compensation expense over the service period on a straight-line basis for all employee equity awards with a graded vesting schedule. Under IFRS, share-based compensation with graded vesting feature is recognized based on each tranche, which results in an accelerated expense recognition.

Share-based compensation with IPO condition

The Company's Lavazza joint venture granted equity awards to key employees vested and exercisable upon the consummation of a qualified successful IPO. Under U.S. GAAP, a performance condition that may be met after the requisite service period is a vesting condition and compensation cost is recognized only if IPO becomes probable of being achieved. Under IFRS, performance condition that may be met after the requisite service period is a non-vesting condition and reflected in the measurement of the grant date fair value of an award, which may result in earlier expense recognition.

(c) Deferred taxes on share-based compensation

Under U.S. GAAP, deferred taxes are calculated based on the cumulative share-based compensation expense recognized in the financial statements, and it required all excess tax benefits and tax deficiencies to be recorded in the consolidated statement of income in the period in which tax deduction arises.

Under IFRS, deferred tax asset is recorded based on estimate of the future tax deduction in accordance with the stock price at the end of each reporting period. If the estimated future tax deduction exceeds cumulative compensation cost for an individual award, deferred tax based on the excess is credited to shareholders' equity. If the estimated future tax deduction is less than or equal to cumulative compensation cost for an individual award, deferred taxes are recorded in consolidated statement of income.

(d) Long-lived assets impairment

Under U.S. GAAP, two-step approach is used in the measurement and recognition of impairment loss of long-lived assets of our restaurants (primarily PP&E and ROU). During step one recoverability test, the carrying amount is first compared with the undiscounted cash flows, using entity specific assumptions. During step two measurement test, if the carrying amount is higher than the undiscounted cash flows, an impairment loss is measured as the difference between the carrying value and fair value. Under IFRS, only one-step approach is used in impairment testing. The carrying amount is compared with the recoverable amount, which is the higher of fair value less costs of disposal or the asset's value in use based on the net present value of future cash flows. Therefore, the difference in impairment assessment results in difference in impairment loss under IFRS. In addition, the lease accounting difference leads to difference in ROU carrying amounts and thus results in difference in impairment loss, which is included in Note (a) together with all other lease related GAAP differences.

(e) Redeemable non-controlling interest

Under U.S. GAAP, when the noncontrolling interest is redeemable at the option of the noncontrolling shareholder, or contingently redeemable upon the occurrence of a conditional event that is not solely within the control of the Company, the noncontrolling interest is separately classified as mezzanine equity which is neither liability nor equity. The redeemable non-controlling interest is initially recorded at fair value and subsequently measured at the higher of initial fair value, increased or decreased for the non-controlling interest's share of net income or loss, or the redemption value of the non-controlling interest.

Under IFRS, redeemable noncontrolling interest is presented as liability, as the Company does not have the unconditional right to avoid delivering cash or another financial asset. Redeemable non-controlling interest is measured at fair value subsequently.

Management's Discussion and Analysis of Financial Condition and Results of Operations.

All Note references in this Management's Discussion and Analysis ("MD&A") refer to the Notes to the Consolidated Financial Statements included in this announcement. Tabular amounts are displayed in millions of U.S. dollars except per share and unit count amounts, or as otherwise specifically identified. Percentages may not recompute due to rounding. Throughout this announcement when we refer to the "financial statements," we are referring to the "Consolidated Financial Statements," unless the context indicates otherwise.

Overview

Yum China Holdings, Inc. is the largest restaurant company in China in terms of 2023 system sales, with \$11 billion of revenues in 2023 and 14,644 restaurants as of year-end 2023. Our growing restaurant network consists of our flagship KFC and Pizza Hut brands, as well as emerging brands such as Lavazza, Huang Ji Huang, Little Sheep and Taco Bell. We have the exclusive right to operate and sublicense the KFC, Pizza Hut and, subject to achieving certain agreed-upon milestones, Taco Bell brands in China, (excluding Hong Kong, Macau and Taiwan), and own the intellectual property of the Little Sheep and Huang Ji Huang concepts outright. We also established a joint venture with Lavazza Group, the world-renowned family-owned Italian coffee company, to explore and develop the Lavazza coffee concept in China. KFC was the first major global restaurant brand to enter China in 1987. With more than 35 years of operations, we have developed extensive operating experience in the China market. We have since grown to become the largest restaurant company in China in terms of 2023 system sales, with 14,644 restaurants covering over 2,000 cities primarily in China as of December 31, 2023. We believe that there are significant opportunities to further expand within China, and we intend to focus our efforts on increasing our geographic footprint in both existing and new cities.

KFC is the leading and the largest quick-service restaurant ("QSR") brand in China in terms of system sales. As of December 31, 2023, KFC operated 10,296 restaurants in more than 2,000 cities across China. KFC primarily competes with western QSR brands in China, such as McDonald's, Dicos and Burger King, among which we believe KFC had an approximate two-to-one lead over its nearest competitor in terms of store count as of the end of 2023.

Pizza Hut is the leading and the largest casual dining restaurant ("CDR") brand in China in terms of system sales and number of restaurants. As of December 31, 2023, Pizza Hut operated 3,312 restaurants in over 700 cities. Measured by number of restaurants, we believe Pizza Hut had an approximate four-to-one lead over its nearest western CDR competitor in China as of the end of 2023.

We have two reportable segments: KFC and Pizza Hut. Our non-reportable operating segments, including the operations of Lavazza, Huang Ji Huang, Little Sheep and Taco Bell (and for 2022, also including COFFii & JOY and East Dawning), our delivery operating segment and our e-commerce business, are combined and referred to as All Other Segments, as these operating segments are insignificant both individually and in the aggregate. The Company decided to wind down the operations of the East Dawning brand in 2021, and closed all stores by March 2022. In addition, the Company decided to wind down the operations of COFFii & JOY and closed all stores in 2022. The Company will leverage its experience in COFFii & JOY to better capture growing coffee market opportunities in China. Additional details on our reportable operating segments are included in Note 17.

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

- Certain performance metrics and non-GAAP measures are presented excluding the impact of foreign currency translation ("F/X"). These amounts are derived by translating current year results at prior year average exchange rates. We believe the elimination of the F/X impact provides better year-to-year comparability without the distortion of foreign currency fluctuations.

- System sales growth reflects the results of all restaurants regardless of ownership, including Company-owned and franchise restaurants, except for sales from non-Company-owned restaurants for which we do not receive a sales-based royalty. Sales of franchise restaurants typically generate ongoing franchise fees for the Company at an average rate of approximately 6% of system sales. Franchise restaurant sales are not included in Company sales in the Consolidated Statements of Income; however, the franchise fees are included in the Company's revenues. We believe system sales growth is useful to investors as a significant indicator of the overall strength of our business as it incorporates all of our revenue drivers, Company and franchise same-store sales as well as net unit growth.
- Effective January 1, 2018, the Company revised its definition of same-store sales growth to represent the estimated percentage change in sales of food of all restaurants in the Company system that have been open prior to the first day of our prior fiscal year, excluding the period during which stores are temporarily closed. We refer to these as our "base" stores. Previously, same-store sales growth represented the estimated percentage change in sales of all restaurants in the Company system that have been open for one year or more, including stores temporarily closed, and the base stores changed on a rolling basis from month to month. This revision was made to align with how management measures performance internally and focuses on trends of a more stable base of stores.
- Company sales represent revenues from Company-owned restaurants. Within the analysis of Company sales, Total revenue and Restaurant profit, store portfolio actions represent the net impact from new-unit openings, acquisitions, refranchising and store closures. Net new unit contribution represents net revenue growth primarily from store portfolio actions excluding temporary store closures. Other primarily represents the impact of same-store sales as well as the impact of changes in restaurant operating costs such as inflation/deflation.

Results of Operations

Summary

All comparisons within this summary are versus the same period a year ago. The Company has two reportable segments: KFC and Pizza Hut. Our non-reportable operating segments, including the operations of Lavazza, Huang Ji Huang, Little Sheep and Taco Bell (and for 2022, also including COFFii & JOY and East Dawning), our delivery operating segment and our e-commerce business, are combined and referred to as All Other Segments, as those operating segments are insignificant both individually and in the aggregate. Additional details on our reportable operating segments are included in Note 17.

From 2020 to 2022, the COVID-19 pandemic significantly impacted the Company's operations and financial results and caused significant volatility in our operations. In 2023, the Company captured opportunities emerging from China's reopening and drove significant revenue, operating profit and net income growth.

In 2023, the Company's total revenues increased 15%, or 21% excluding \$589 million F/X impact, mainly attributable to 9% of net new unit contribution, same-store sales growth of 7% and 6% at KFC and Pizza Hut, respectively, and reduced temporary store closures due to lapping of the impact of the COVID-19 pandemic in 2022. Operating profit increased 76%, or 86% excluding \$61 million F/X impact, primarily driven by the increase in Company sales and favorable commodity prices, partially offset by increased value promotions, lower temporary relief and wage inflation in the low single digits. Net income for 2023 increased 87%, or 97% excluding \$46 million F/X impact, mainly due to the increase in Operating profit and higher interest income, net of higher income tax expenses in line with the increase in pre-tax income.

2023 financial highlights are below:

	2023	2022	%/ppts Change	
			Reported	Ex F/X
System Sales Growth ^(a) (%)	21	(5)	NM	NM
Same-Store Sales Growth ^(a) (%)	7	(7)	NM	NM
Operating Profit	1,106	629	+76	+86
Adjusted Operating Profit ^(b)	1,121	633	+77	+87
Core Operating Profit ^(b)	1,121	627	NM	+79
Net Income	827	442	+87	+97
Adjusted Net Income ^(b)	842	446	+89	+99
Diluted Earnings Per Common Share	1.97	1.04	+89	+100
Adjusted Diluted Earnings Per Common Share ^(b)	2.00	1.05	+90	+101

(a) System Sales and Same-Store Sales growth percentages as shown in 2023 financial highlights exclude the impact of F/X. Effective January 1, 2018, temporary store closures are normalized in the same-store sales calculation by excluding the period during which stores are temporarily closed.

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

The Consolidated Results of Operations for the years ended December 31, 2023 and 2022 and other data are presented below:

	2023	2022	% B/(W) ^(a)	
			Reported	Ex F/X
Company sales	\$ 10,391	\$ 9,110	14	20
Franchise fees and income	89	81	11	17
Revenues from transactions with franchisees	372	287	30	36
Other revenues	126	91	39	45
Total revenues	\$ 10,978	\$ 9,569	15	21
Company restaurant expenses	\$ 8,701	\$ 7,829	(11)	(17)
Operating Profit	\$ 1,106	\$ 629	76	86
Interest income, net	169	84	101	103
Investment loss	(49)	(26)	(91)	(91)
Income tax provision	(329)	(207)	(59)	(66)
Equity in net earnings (losses) from equity method investments	4	(2)	NM	NM
Net Income – including noncontrolling interests	901	478	88	99
Net income – noncontrolling interests	74	36	(106)	(116)
Net Income – Yum China Holdings, Inc.	\$ 827	\$ 442	87	97
Diluted Earnings Per Common Share	\$ 1.97	\$ 1.04	89	100
Effective tax rate	26.9%	30.1%		
Supplementary information – Non-GAAP Measures^(b)				
Restaurant profit	\$ 1,690	\$ 1,281	32	38
Restaurant margin %	16.3%	14.1%	2.2 ppts.	2.2 ppts.
Adjusted Operating Profit	\$ 1,121	\$ 633		
Core Operating Profit	\$ 1,121	\$ 627		
Adjusted Net Income – Yum China Holdings, Inc.	\$ 842	\$ 446		
Adjusted Diluted Earnings Per Common Share	\$ 2.00	\$ 1.05		
Adjusted Effective Tax Rate	26.5%	29.9%		
Adjusted EBITDA	\$ 1,611	\$ 1,286		

NM refers to not meaningful.

- (a) Represents year-over-year change in percentage.
- (b) See “Non-GAAP Measures” below for definitions and reconciliations of the most directly comparable GAAP financial measures to the non-GAAP measures.

Performance Metrics

	<u>2023</u> % Change
System Sales Growth	14%
System Sales Growth, excluding F/X	21%
Same-Store Sales Growth	7%

<u>Unit Count</u>	<u>2023</u>	<u>2022</u>	<u>% Increase</u>
Company-owned	12,648	11,161	13
Franchisees	1,996	1,786	12
	<u>14,644</u>	<u>12,947</u>	13

Outlook

In 2024, Yum China plans to:

- Open approximately 1,500 to 1,700 net new stores.
- Make capital expenditures in the range of approximately \$700 million to \$850 million.

Non-GAAP Measures

In addition to the results provided in accordance with GAAP throughout this MD&A, the Company provides the following non-GAAP measures:

- Measures adjusted for Special Items, which include Adjusted Operating Profit, Adjusted Net Income, Adjusted Earnings Per Common Share ("EPS"), Adjusted Effective Tax Rate and Adjusted EBITDA;
- Company Restaurant Profit ("Restaurant profit") and Restaurant margin;
- Core Operating Profit that excludes Special Items, and further adjusted for Items Affecting Comparability and the impact of F/X;

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

With respect to non-GAAP measures adjusted for Special Items, the Company excludes impact from Special Items for the purpose of evaluating performance internally and uses them as factors in determining compensation for certain employees. Special Items are not included in any of our segment results.

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

Restaurant profit (“Restaurant profit”) is defined as Company sales less expenses incurred directly by our Company-owned restaurants in generating Company sales, including cost of food and paper, restaurant-level payroll and employee benefits, rent, depreciation and amortization of restaurant-level assets, advertising expenses, and other operating expenses. Company restaurant margin percentage is defined as Restaurant profit divided by Company sales. We also use Restaurant profit and Restaurant margin for the purposes of internally evaluating the performance of our Company-owned restaurants and we believe they provide useful information to investors as to the profitability of our Company-owned restaurants.

Core Operating Profit is defined as Operating Profit adjusted for Special Items, and further excluding Items Affecting Comparability and the impact of F/X. We consider quantitative and qualitative factors in assessing whether to adjust for the impact of items that may be significant or that could affect an understanding of our ongoing financial and business performance or trends. Items such as charges, gains and accounting changes, which are viewed by management as significantly impacting the current period or the comparable period, due to changes in policy or other external factors, or non-cash items pertaining to underlying activities that are different from or unrelated to our core operations, are generally considered “Items Affecting Comparability.” Examples of Items Affecting Comparability include, but are not limited to: temporary relief from landlords and government agencies; VAT deductions due to tax policy changes; and amortization of reacquired franchise rights recognized upon acquisitions. We believe presenting Core Operating Profit provides additional information to further enhance comparability of our operating results and we use this measure for purposes of evaluating the performance of our core operations.

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

Non-GAAP Reconciliations	2023	2022
Reconciliation of Operating Profit to Adjusted Operating Profit		
Operating Profit	\$ 1,106	\$ 629
Special Items, Operating Profit	(15)	(4)
Adjusted Operating Profit	<u>\$ 1,121</u>	<u>\$ 633</u>
Reconciliation of Net Income to Adjusted Net Income		
Net Income – Yum China Holdings, Inc.	\$ 827	\$ 442
Special Items, Net Income – Yum China Holdings, Inc.	(15)	(4)
Adjusted Net Income – Yum China Holdings, Inc.	<u>\$ 842</u>	<u>\$ 446</u>
Reconciliation of EPS to Adjusted EPS		
Basic Earnings Per Common Share	\$ 1.99	\$ 1.05
Special Items, Basic Earnings Per Common Share	(0.03)	(0.01)
Adjusted Basic Earnings Per Common Share	<u>\$ 2.02</u>	<u>\$ 1.06</u>
Diluted Earnings Per Common Share	\$ 1.97	\$ 1.04
Special Items, Diluted Earnings Per Common Share	(0.03)	(0.01)
Adjusted Diluted Earnings Per Common Share	<u>\$ 2.00</u>	<u>\$ 1.05</u>
Reconciliation of Effective Tax Rate to Adjusted Effective Tax Rate		
Effective tax rate (See Note 16)	26.9%	30.1%
Impact on effective tax rate as a result of Special Items	0.4%	0.2%
Adjusted effective tax rate	<u>26.5%</u>	<u>29.9%</u>

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

	<u>2023</u>	<u>2022</u>
Reconciliation of Net Income to Adjusted EBITDA		
Net Income – Yum China Holdings, Inc.	\$ 827	\$ 442
Net income – noncontrolling interests	74	36
Equity in net (earnings) losses from equity method investments	(4)	2
Income tax provision	329	207
Interest income, net	(169)	(84)
Investment loss	49	26
Operating Profit	<u>1,106</u>	<u>629</u>
Special Items, Operating Profit	15	4
Adjusted Operating Profit	<u>1,121</u>	<u>633</u>
Depreciation and amortization	453	602
Store impairment charges	37	51
Adjusted EBITDA	<u>\$ 1,611</u>	<u>\$ 1,286</u>

Details of Special Items are presented below:

Details of Special Items	<u>2023</u>	<u>2022</u>
Share-based compensation expense for Partner PSU Awards ^(a)	\$ (15)	\$ (4)
Special Items, Operating Profit	(15)	(4)
Tax effect on Special Items ^(b)	—	—
Special Items, net income – including noncontrolling interests	(15)	(4)
Special Items, net income – noncontrolling interests	—	—
Special Items, Net Income – Yum China Holdings, Inc.	<u>\$ (15)</u>	<u>\$ (4)</u>
Weighted-average Diluted Shares Outstanding (in millions)	420	425
Special Items, Diluted Earnings Per Common Share	<u>\$ (0.03)</u>	<u>\$ (0.01)</u>

- (a) In February 2020, the Company granted Partner PSU Awards to select employees who were deemed critical to the Company's execution of its strategic operating plan. These PSU awards will only vest if threshold performance goals are achieved over a four-year performance period, with the payout ranging from 0% to 200% of the target number of shares subject to the PSU awards. Partner PSU Awards were granted to address increased competition for executive talent, motivate transformational performance and encourage management retention. Given the unique nature of these grants, the Compensation Committee does not intend to grant similar, special grants to the same employees during the performance period. The impact from these special awards is excluded from metrics that management uses to assess the Company's performance.
- (b) Tax effect was determined based upon the nature, as well as the jurisdiction, of each Special Item at the applicable tax rate.

Reconciliation of GAAP Operating Profit to Restaurant Profit

2023						
	<u>KFC</u>	<u>Pizza Hut</u>	<u>All Other Segments</u>	<u>Corporate and Unallocated</u>	<u>Elimination</u>	<u>Total</u>
GAAP Operating Profit (Loss)	\$ 1,202	\$ 142	\$ (31)	\$ (207)	\$ —	\$ 1,106
Less:						
Franchise fees and income	62	7	20	—	—	89
Revenues from transactions with franchisees	45	4	74	249	—	372
Other revenues	17	21	624	44	(580)	126
Add:						
General and administrative expenses	263	118	43	214	—	638
Franchise expenses	31	4	1	—	—	36
Expenses for transactions with franchisees	39	4	67	246	—	356
Other operating costs and expenses	15	19	614	42	(578)	112
Closures and impairment expenses, net	12	8	9	—	—	29
Other expenses (income), net	2	—	—	(2)	—	—
Restaurant profit (loss)	\$ 1,440	\$ 263	\$ (15)	\$ —	\$ 2	\$ 1,690
Company sales	8,116	2,214	61	—	—	10,391
Restaurant margin %	17.7%	11.8%	(25.1)%	N/A	N/A	16.3%

2022						
	<u>KFC</u>	<u>Pizza Hut</u>	<u>All Other Segments</u>	<u>Corporate and Unallocated</u>	<u>Elimination</u>	<u>Total</u>
GAAP Operating Profit (Loss)	\$ 787	\$ 70	\$ (50)	\$ (178)	\$ —	\$ 629
Less:						
Franchise fees and income	56	7	18	—	—	81
Revenues from transactions with franchisees	33	4	39	211	—	287
Other revenues	10	10	563	42	(534)	91
Add:						
General and administrative expenses	254	110	46	184	—	594
Franchise expenses	29	4	1	—	—	34
Expenses for transactions with franchisees	30	3	35	211	—	279
Other operating costs and expenses	7	8	557	39	(533)	78
Closures and impairment expenses, net	16	4	12	—	—	32
Other expenses (income), net	97	—	—	(3)	—	94
Restaurant profit (loss)	\$ 1,121	\$ 178	\$ (19)	\$ —	\$ 1	\$ 1,281
Company sales	7,120	1,939	51	—	—	9,110
Restaurant margin %	15.7%	9.2%	(37.6)%	N/A	N/A	14.1%

Reconciliation of GAAP Operating Profit to Core Operating Profit

2023						
	<u>KFC</u>	<u>Pizza Hut</u>	<u>All Other Segments</u>	<u>Corporate and Unallocated</u>	<u>Elimination</u>	<u>Total</u>
GAAP Operating Profit (Loss)	\$ 1,202	\$ 142	\$ (31)	\$ (207)	\$ —	\$ 1,106
Special Items, Operating Profit	—	—	—	15	—	15
Adjusted Operating Profit	\$ 1,202	\$ 142	\$ (31)	\$ (192)	\$ —	\$ 1,121
Items Affecting Comparability						
Temporary relief from landlords ^(a)	(9)	(2)	—	—	—	(11)
Temporary relief from government agencies ^(b)	(5)	(2)	—	—	—	(7)
VAT deductions ^(c)	(36)	(6)	(2)	—	—	(44)
Amortization of reacquired franchise rights ^(d)	2	—	—	—	—	2
F/X impact	57	11	(2)	(6)	—	60
Core Operating Profit (Loss)	\$ 1,211	\$ 143	\$ (35)	\$ (198)	\$ —	\$ 1,121

2022

	Corporate and					Total
	KFC	Pizza Hut	All Other Segments	Unallocated	Elimination	
GAAP Operating Profit (Loss)	\$ 787	\$ 70	\$ (50)	\$ (178)	\$ —	\$ 629
Special Items, Operating Profit	—	—	—	4	—	4
Adjusted Operating Profit	<u>\$ 787</u>	<u>\$ 70</u>	<u>\$ (50)</u>	<u>\$ (174)</u>	<u>\$ —</u>	<u>\$ 633</u>
Items Affecting Comparability						
Temporary relief from landlords ^(a)	(32)	(6)	(1)	—	—	(39)
Temporary relief from government agencies ^(b)	(34)	(14)	—	—	—	(48)
VAT deductions ^(c)	(12)	(2)	(2)	—	—	(16)
Amortization of reacquired franchise rights ^(d)	97	—	—	—	—	97
F/X impact	—	—	—	—	—	—
Core Operating Profit (Loss)	<u>\$ 806</u>	<u>\$ 48</u>	<u>\$ (53)</u>	<u>\$ (174)</u>	<u>\$ —</u>	<u>\$ 627</u>

Details of Items Affecting Comparability are presented below:

- (a) In relation to the effects of the COVID-19 pandemic, the Company was granted lease concessions from landlords. The lease concessions were primarily in the form of rent reduction over the period of time when the Company's restaurant business was adversely impacted. Such concessions were primarily recognized as a reduction of Occupancy and other operating expenses within Company restaurant expenses included in the Consolidated Statement of Income in the period the concession was granted. See Note 11 for additional information.
- (b) In relation to the effects of the COVID-19 pandemic, the government issued a policy in 2020 on reducing enterprise social security contribution, pursuant to which the Company recorded one-time relief of \$33 million in 2022. In addition, this also includes government subsidies for employee benefits and providing training to employees, with higher amounts received during 2022 impacted by the COVID-19 pandemic. The temporary relief was primarily recognized as a reduction to Payroll and employee benefits within Company restaurant expenses included in the Consolidated Statement of Income. See Note 2 government subsidies for additional information.
- (c) Pursuant to the tax policy issued by relevant government authorities, general VAT taxpayers in certain industries that meet certain criteria are allowed to claim an additional 10% or 15% input VAT, which will be used to offset their VAT payables. This VAT policy was further extended to December 31, 2023 but the additional deduction was reduced to 5% or 10% respectively. VAT deductions were primarily recorded as a reduction to Food and paper and Occupancy and other operating expenses within Company restaurant expenses included in the Consolidated Statements of Income. Based on the information currently available to the Company, such preferential policy is not expected to be extended. See "Significant Known Events, Trends or Uncertainties Expected to Impact Future Results" session within MD&A for additional information on VAT deductions.
- (d) As a result of the acquisition of our previously unconsolidated joint ventures of Hangzhou KFC, Suzhou KFC and Wuxi KFC, \$66 million, \$61 million and \$61 million of the purchase price were allocated to intangible assets related to reacquired franchise rights, respectively, which were amortized over the remaining franchise contract period of 1 year, 2.4 years and 5 years, respectively. The reacquired franchise rights were fully amortized as of March 31, 2023. The amortization was recorded in Other Expenses (Income), net included in the Consolidated Statements of Income. See Note 6 for additional information.

Segment Results

KFC

KFC delivered strong performance in 2023 by accelerating store expansion with attractive returns, achieving solid same-store sales growth and expanding profitability. KFC continued to focus on innovative products, creating abundant value for our customers, updating ingredients and tastes to meet Chinese consumers' needs, as well as on introducing entry price point products. KFC also continued its digital and delivery initiatives to enhance the customer experience. KFC's loyalty program members exceeded 440 million at year-end 2023 and contributed approximately 64% of system sales at KFC in 2023. Delivery sales accounted for approximately 36% of Company sales at KFC in 2023 with store and city coverage of 89% and 98%, respectively, at the end of 2023.

	2023	2022	% B/(W)	
			Reported	Ex F/X
Company sales	\$ 8,116	\$ 7,120	14	20
Franchise fees and income	62	56	10	16
Revenues from transactions with franchisees	45	33	37	44
Other revenues	17	10	60	67
Total revenues	<u>\$ 8,240</u>	<u>\$ 7,219</u>	14	20
Company restaurant expenses	\$ 6,676	\$ 5,999	(11)	(17)
G&A expenses	\$ 263	\$ 254	(4)	(9)
Franchise expenses	\$ 31	\$ 29	(2)	(7)
Expenses for transactions with franchisees	\$ 39	\$ 30	(33)	(40)
Other operating costs and expenses	\$ 15	\$ 7	(91)	(98)
Closures and impairment expenses, net	\$ 12	\$ 16	28	25
Other expenses, net	\$ 2	\$ 97	98	98
Operating Profit	\$ 1,202	\$ 787	53	60
Restaurant profit	\$ 1,440	\$ 1,121	29	35
Restaurant margin %	17.7%	15.7%	2.0 ppts.	2.0 ppts.

	2023
	% Change
System Sales Growth	14%
System Sales Growth, excluding F/X	20%
Same-Store Sales Growth	7%

Unit Count	2023	2022	% Increase
Company-owned	9,237	8,214	12
Franchisees	1,059	880	20
	<u>10,296</u>	<u>9,094</u>	13

	2022	New Builds	Acquired	Closures	Refranchised	2023
Company-owned	8,214	1,246	2	(222)	(3)	9,237
Franchisees	880	193	(2)	(15)	3	1,059
Total	<u>9,094</u>	<u>1,439</u>	<u>—</u>	<u>(237)</u>	<u>—</u>	<u>10,296</u>

Company Sales and Restaurant Profit

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

<u>Income (Expense)</u>	Store Portfolio				<u>2023</u>
	<u>2022</u>	<u>Actions</u>	<u>Other</u>	<u>F/X</u>	
Company sales	\$ 7,120	\$ 902	\$ 529	\$ (435)	\$ 8,116
Cost of sales	(2,208)	(302)	(138)	136	(2,512)
Cost of labor	(1,797)	(219)	(153)	112	(2,057)
Occupancy and other operating expenses	(1,994)	(168)	(61)	116	(2,107)
Restaurant profit	<u>\$ 1,121</u>	<u>\$ 213</u>	<u>\$ 177</u>	<u>\$ (71)</u>	<u>\$ 1,440</u>

In 2023, the increase in Company sales, excluding the impact of F/X, was primarily driven by net unit growth, same-store sales growth and reduced temporary store closures. The increase in Restaurant profit, excluding the impact of F/X, was primarily driven by the increase in Company sales and favorable commodity prices, partially offset by increased value promotions, wage inflation in the mid-single digits and lower temporary relief.

Franchise Fees and Income/Revenues from Transactions with Franchisees

In 2023, the increase in Franchise fees and income and Revenues from transactions with franchisees, excluding the impact of F/X, was primarily driven by net unit growth and same-store sales growth.

G&A Expenses

In 2023, the increase in G&A expenses, excluding the impact of F/X, was primarily driven by higher compensation costs and higher travel expenses from the resumption of business travel.

Other Expenses, net

In 2023, the decrease in Other expenses, net, excluding the impact of F/X, was primarily due to intangible assets related to reacquired franchise rights of Hangzhou KFC, Suzhou KFC and Wuxi KFC being substantially amortized as of December 31, 2022. See Note 6 for detail.

Operating Profit

In 2023, the increase in Operating profit, excluding the impact of F/X, was primarily driven by the increase in Restaurant profit and decrease in Other expenses, net, partially offset by higher G&A expenses.

Pizza Hut

Pizza Hut delivered strong performance in 2023 by accelerating store expansion with healthy returns, achieving solid same-store sales growth and expanding profitability. During 2023, we continued to focus on innovating products, investing in value-for-money strategy, strengthening digital capabilities, fortifying delivery, expanding into new occasions and consumer segments and enhancing our asset portfolio to drive growth. Pizza Hut's loyalty program members exceeded 150 million at year-end 2023 and contributed approximately 66% of system sales at Pizza Hut in 2023. Delivery sales accounted for approximately 37% of Company sales at Pizza Hut in 2023 with store and city coverage of 96% and 99%, respectively, at the end of 2023.

	2023	2022	% B/(W)	
			Reported	Ex F/X
Company sales	\$ 2,214	\$ 1,939	14	20
Franchise fees and income	7	7	9	15
Revenues from transactions with franchisees	4	4	11	17
Other revenues	21	10	114	123
Total revenues	<u>\$ 2,246</u>	<u>\$ 1,960</u>	15	21
Company restaurant expenses	\$ 1,951	\$ 1,761	(11)	(17)
G&A expenses	\$ 118	\$ 110	(7)	(13)
Franchise expenses	\$ 4	\$ 4	(8)	(14)
Expenses for transactions with franchisees	\$ 4	\$ 3	(11)	(17)
Other operating costs and expenses	\$ 19	\$ 8	(124)	(134)
Closures and impairment expenses, net	\$ 8	\$ 4	(135)	(142)
Operating Profit	\$ 142	\$ 70	102	117
Restaurant profit	\$ 263	\$ 178	46	55
Restaurant margin %	11.8%	9.2%	2.6 ppts.	2.6 ppts.

	2023
	% Change
System Sales Growth	14%
System Sales Growth, excluding F/X	20%
Same-Store Sales Growth	6%

Unit Count	2023	2022	% Increase
Company-owned	3,155	2,760	14
Franchisees	157	143	10
	<u>3,312</u>	<u>2,903</u>	14

	2022	New Builds	Closures	Refranchised	2023
Company-owned	2,760	515	(118)	(2)	3,155
Franchisees	143	16	(4)	2	157
Total	<u>2,903</u>	<u>531</u>	<u>(122)</u>	<u>—</u>	<u>3,312</u>

Company Sales and Restaurant Profit

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

Income (Expense)	2022	Store Portfolio			2023
		Actions	Other	F/X	
Company sales	\$ 1,939	\$ 277	\$ 118	\$ (120)	\$ 2,214
Cost of sales	(612)	(88)	(29)	37	(692)
Cost of labor	(572)	(70)	(42)	35	(649)
Occupancy and other operating expenses	(577)	(60)	(7)	34	(610)
Restaurant profit	<u>\$ 178</u>	<u>\$ 59</u>	<u>\$ 40</u>	<u>\$ (14)</u>	<u>\$ 263</u>

In 2023, the increase in Company sales, excluding the impact of F/X, was primarily driven by net unit growth, same-store sales growth and reduced temporary store closures. The increase in Restaurant profit, excluding the impact of F/X, was primarily driven by the increase in Company sales and favorable commodity prices, partially offset by lower temporary relief, wage inflation in the low single digits and increased value promotions.

G&A Expenses

In 2023, the increase in G&A expenses, excluding the impact of F/X, was primarily driven by higher compensation costs and higher travel expenses from the resumption of business travel.

Operating Profit

In 2023, the increase in Operating profit, excluding the impact of F/X, was primarily driven by the increase in Restaurant profit, partially offset by higher G&A expenses.

All Other Segments

All Other Segments reflects the results of Lavazza, Huang Ji Huang, Little Sheep and Taco Bell (and for 2022, also including COFFii & JOY and East Dawning), our delivery operating segment and our e-commerce business.

	2023	2022	% B/(W)	
			Reported	Ex F/X
Company sales	\$ 61	\$ 51	20	26
Franchise fees and income	20	18	14	21
Revenues from transactions with franchisees	74	39	89	99
Other revenues	624	563	11	16
Total revenues	<u>\$ 779</u>	<u>\$ 671</u>	16	22
Company restaurant expenses	\$ 76	\$ 70	(9)	(15)
G&A expenses	\$ 43	\$ 46	8	3
Franchise expenses	\$ 1	\$ 1	9	4
Expenses for transactions with franchisees	\$ 67	\$ 35	(93)	(102)
Other operating costs and expenses	\$ 614	\$ 557	(10)	(16)
Closure and impairment expenses, net	\$ 9	\$ 12	25	21
Operating Loss	\$ (31)	\$ (50)	39	36
Restaurant loss	\$ (15)	\$ (19)	20	15
Restaurant margin %	(25.1)%	(37.6)%	12.5 ppts.	12.5 ppts.

Total Revenues

In 2023, the increase in Total revenues, excluding the impact of F/X, was primarily driven by inter-segment revenue generated by our delivery team for services provided to Company-owned restaurants as a result of increased delivery sales, as well as revenue generated from delivery services provided to franchisees.

Operating Loss

In 2023, the decrease in Operating loss, excluding the impact of F/X, was primarily driven by the decrease in Operating loss from certain emerging brands.

Corporate & Unallocated

			% B/(W)	
	2023	2022	Reported	Ex F/X
Revenues from transactions with franchisees ^(a)	\$ 249	\$ 211	18	24
Other revenues	\$ 44	\$ 42	7	12
Expenses for transactions with franchisees ^(a)	\$ 246	\$ 211	(17)	(23)
Other operating costs and expenses	\$ 42	\$ 39	(10)	(16)
Corporate G&A expenses	\$ 214	\$ 184	(17)	(20)
Other unallocated income, net	\$ 2	\$ 3	(6)	(1)
Interest income, net	\$ 169	\$ 84	101	103
Investment loss	\$ (49)	\$ (26)	(91)	(91)
Income tax provision (See Note 16)	\$ (329)	\$ (207)	(59)	(66)
Equity in net earnings (losses) from equity method investments	\$ 4	\$ (2)	NM	NM
Effective tax rate (See Note 16)	26.9%	30.1%	3.2 ppts	3.2 ppts

(a) Primarily includes revenues and associated expenses of transactions with franchisees derived from the Company's central procurement model whereby food and paper products are centrally purchased and then mainly sold to KFC and Pizza Hut franchisees. Amounts have not been allocated to any segment for purposes of making operating decisions or assessing financial performance as the transactions are corporate revenues and expenses in nature.

Revenues from Transactions with Franchisees

In 2023, the increase in Revenues from transactions with franchisees, excluding the impact of F/X, was mainly due to the increase in system sales for franchisees.

Corporate G&A Expenses

In 2023, the increase in Corporate G&A expenses, excluding the impact of F/X, was primarily driven by higher compensation costs.

Interest Income, Net

In 2023, the increase in interest income, excluding the impact of F/X, was primarily driven by higher interest rates and higher investment balance during the year.

Investment Loss

The investment loss mainly relates to the change in fair value of our investment in Meituan Dianping ("Meituan"). See Note 3 for additional information.

Income Tax Provision

Our income tax provision primarily includes tax on our earnings generally at the Chinese statutory tax rate of 25% with certain Chinese subsidiaries qualified at preferential tax rates, withholding tax on planned or actual repatriation of earnings outside of China, Hong Kong profits tax, and U.S. corporate income tax, if any. Our effective tax rate was 26.9% and 30.1% in 2023 and 2022, respectively. The lower effective tax rate in 2023 compared with that in 2022 was primarily due to a reduction in valuation allowance for improved performance at certain subsidiaries, an increase in benefits from preferential tax treatment at qualified subsidiaries and the impact of higher pre-tax income.

Key Balance Sheet Items

Cash and Cash Equivalents

As of December 31, 2023 and 2022, the Company's cash and cash equivalents were denominated in the following currencies:

	<u>2023</u>	<u>2022</u>
RMB	\$ 534	\$ 571
USD	590	555
Hong Kong dollar ("HK\$")	4	4
Total	<u>\$ 1,128</u>	<u>\$ 1,130</u>

For discussion of changes in Cash and Cash Equivalent, see Consolidated Cash Flows section below.

Short-term Investments, Long-term Bank Deposits and Notes

As of December 31, 2023, the decrease of short-term investments and increase of long-term bank deposits and notes were primarily due to more investments on bank deposits and notes with remaining maturity over one year in order to enhance the investment return.

PP&E, Operating Lease ROU Assets and Liabilities

As of December 31, 2023, excluding the impact of F/X, the increase of PP&E and operating lease ROU assets was mainly due to the increase in the number of our stores, partially offset by depreciation of PP&E and amortization of ROU assets. Excluding the impact of F/X, the increase of lease liabilities was consistent with the increase of ROU assets.

Short-term Borrowings

As of December 31, 2023, the increase of short-term borrowings was primarily due to the working capital management at its operating subsidiaries. The outstanding short-term borrowings are RMB denominated and bear a weighted-average interest rate of 1.7%, and are due within one year from their issuance dates. (See Note 9 for additional information).

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

Tax Examination on Transfer Pricing

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

PRC Value-Added Tax ("VAT")

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

Entities that are general VAT taxpayers are permitted to offset qualified input VAT paid to suppliers against their output VAT upon receipt of appropriate supplier VAT invoices on an entity-by-entity basis. When the output VAT exceeds the input VAT, the difference is remitted to tax authorities, usually on a monthly basis; whereas when the input VAT exceeds the output VAT, the difference is treated as a VAT asset which can be carried forward indefinitely to offset future net VAT payables. VAT related to purchases and sales which have not been settled at the balance sheet date is disclosed separately as an asset and liability, respectively, on the Consolidated Balance Sheets. At each balance sheet date, the Company reviews the outstanding balance of any VAT asset for recoverability, giving consideration to the indefinite life of VAT assets as well as its forecasted operating results and capital spending, which inherently includes significant assumptions that are subject to change. As of December 31, 2023 and 2022, the Company has not made an allowance for the recoverability of VAT assets, as the balance is expected to be utilized to offset against VAT payables or be refunded in the future.

On June 7, 2022, the Chinese Ministry of Finance ("MOF") and the STA jointly issued Circular [2022] No. 21, to extend full VAT credit refunds to more sectors and increase the frequency for accepting taxpayers' applications. Beginning on July 1, 2022, entities engaged in providing catering services in China are allowed to apply for a lump sum refund of VAT assets accumulated prior to March 31, 2019. In addition, VAT assets accumulated after March 31, 2019 can be refunded on a monthly basis.

As the benefits of certain VAT assets are expected to be realized within one year pursuant to Circular [2022] No. 21, \$303 million of VAT assets as of June 30, 2022 were reclassified from Other assets to Prepaid expenses and other current assets. As of December 31, 2023, VAT assets of \$91 million, VAT assets of \$6 million and net VAT payable of \$5 million were recorded in Prepaid expenses and other current assets, Other assets and Accounts payable and other current liabilities, respectively, on the Consolidated Balance Sheets.

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

Pursuant to Circular [2019] No. 39, Circular [2019] No. 87 and Circular [2022] No. 11 jointly issued by relevant government authorities, including the MOF and the STA, from April 1, 2019 to December 31, 2022, general VAT taxpayers in certain industries that meet certain criteria were allowed to claim an additional 10% or 15% input VAT, which would be used to offset their VAT payables. Pursuant to Circular [2023] No. 1 jointly issued by the MOF and the STA in January 2023, such VAT policy was further extended to December 31, 2023 but the additional deduction was reduced to 5% or 10% respectively. Based on the information currently available to the Company, such preferential policy is not expected to be extended. Subsequent to the lump sum refund of VAT assets beginning on July 1, 2022 pursuant to Circular [2022] No. 21, the number of subsidiaries meeting required criteria for additional VAT deductions increased. Accordingly, we recognized such VAT deductions of \$44 million and \$16 million in 2023 and 2022, respectively. The VAT deductions were recorded as a reduction to the related expense item, primarily in Company restaurant expenses included in the Consolidated Statements of Income.

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

Foreign Currency Exchange Rate

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

Consolidated Cash Flows

Net cash provided by operating activities was \$1,473 million in 2023 as compared to \$1,413 million in 2022. The increase was primarily driven by the increase in net income, partially offset by the lapping of refunds of VAT assets in 2022.

Net cash used in investing activities was \$743 million in 2023 as compared to \$522 million in 2022. The increase was mainly due to the net impact on cash flows resulting from purchases and maturities of short-term investments, and long-term bank deposits and notes.

Net cash used in financing activities was \$716 million in 2023 as compared to \$844 million in 2022. The decrease was primarily driven by net proceeds from short-term bank borrowings and lapping of cash consideration paid in 2022 for the acquisition of an additional 20% equity interest in Suzhou KFC, partially offset by the increase in share repurchases.

Liquidity and Capital Resources

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

Our ability to fund our future operations and capital needs will primarily depend on our ongoing ability to generate cash from operations. We believe our principal uses of cash in the future will be primarily to fund our operations and capital expenditures for accelerating store network expansion and store remodeling, to step up investments in digitalization, automation and logistics infrastructure, to provide returns to our stockholders, as well as to explore opportunities for acquisitions or investments that build and support our ecosystem. We believe that our future cash from operations, together with our funds on hand and access to the capital markets, will provide adequate resources to fund these uses of cash, and that our existing cash, net cash from operations and credit facilities will be sufficient to fund our operations and anticipated capital expenditures for the next 12 months. We currently expect our fiscal year 2024 capital expenditures to be in the range of approximately \$700 million to \$850 million.

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

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

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

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

Share Repurchases and Dividends

On November 2, 2023, our Board of Directors increased the share repurchase authorization by \$1 billion to an aggregate of \$3.4 billion. Yum China may repurchase shares under this program from time to time in the open market or, subject to applicable regulatory requirements, through privately negotiated transactions, block trades, accelerated share repurchase transactions and the use of Rule 10b5-1 trading plans. During the years ended December 31, 2023 and 2022, the Company repurchased \$617 million or 12.4 million shares and \$466 million or 10.5 million shares of common stock, respectively, under the repurchase program. The Company plans to repurchase \$1.25 billion of its common stock in 2024, through open market transactions in the U.S. and Hong Kong. This includes two primary components: (i) an aggregate repurchase amount of \$750 million in 2024 under the Rule 10b5-1 of the United States Securities Exchange Act of 1934 (the "Exchange Act") in the U.S. and a similar program in Hong Kong; and (ii) an aggregate repurchase amount of \$500 million in the first quarter of 2024 under the Rule 10b-18 of the Exchange Act in the U.S. and through similar transactions in Hong Kong.

The Company paid a cash dividend of \$0.13 and \$0.12 per share for each quarter of 2023 and 2022, respectively. Total cash dividends of \$216 million and \$202 million were paid to stockholders in 2023 and 2022, respectively.

On February 6, 2024, the Board of Directors declared a cash dividend to \$0.16 per share, payable on March 26, 2024, to stockholders of record as of the close of business on March 5, 2024.

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

Borrowing Capacity

As of December 31, 2023, the Company had credit facilities of RMB7,112 million (approximately \$1,002 million), comprised of onshore credit facilities in the aggregate amount of RMB5,550 million (approximately \$782 million) and offshore credit facilities in the aggregate amount of \$220 million.

The credit facilities had remaining terms ranging from less than one year to three years as of December 31, 2023. Our credit facilities mainly include term loans, overdrafts, letters of credit, banker's acceptance notes and bank guarantees. The credit facilities in general bear interest based on the Loan Prime Rate ("LPR") published by the National Interbank Funding Centre of the PRC, or Secured Overnight Financing Rate ("SOFR") published by the Federal Reserve Bank of New York. Each credit facility contains a cross-default provision whereby our failure to make any payment on a principal amount from any credit facility will constitute a default on other credit facilities. Some of the credit facilities contain covenants limiting, among other things, certain additional indebtedness and liens, and certain other transactions specified in the respective agreements. As of December 31, 2023, we had outstanding short-term bank borrowings of RMB1,189 million (approximately \$168 million), mainly to manage working capital at our operating subsidiaries. Such bank borrowings were secured by \$79 million short-term investments, and are due within one year from their issuance dates. As of December 31, 2023, we also had outstanding bank guarantees of RMB222 million (approximately \$31 million) mainly to secure our lease payments to landlords for certain Company-owned restaurants. Our credit facilities were therefore reduced by outstanding short-term bank borrowings, adjusted for unamortized interest and collateral, and outstanding guarantees. As of December 31, 2023, the Company had unused credit facilities of approximately \$881 million.

Material Cash Requirements

Our material short-term and long-term cash requirements as of December 31, 2023 included:

	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Finance Leases ^(a)	\$ 63	\$ 7	\$ 12	\$ 12	\$ 32
Operating Leases ^(a)	2,757	525	844	625	763
Short-term borrowings ^(b)	169	169	—	—	—
Purchase Obligations ^(c)	417	151	198	32	36
Transition Tax ^(d)	27	12	15	—	—
Total	<u>\$ 3,433</u>	<u>\$ 864</u>	<u>\$ 1,069</u>	<u>\$ 669</u>	<u>\$ 831</u>

- (a) These obligations, which are shown on a nominal basis, relate primarily to over 12,500 Company-owned restaurants. See Note 11 for additional information.
- (b) This represents outstanding principal amount of short-term borrowings, by excluding the impact of debt discounts as of December 31, 2023. See Note 9 for additional information.
- (c) Purchase obligations relate primarily to capital expenditure commitment for infrastructure, as well as supply and service agreements. We have excluded agreements that are cancelable without penalty or have a remaining term not in excess of one year. Such commitments are generally near term in nature, will be funded from operating cash flows, and are not significant to the Company's overall financial position.
- (d) This amount represents transition tax payable on the deemed repatriation of accumulated undistributed foreign earnings after utilizing existing qualified foreign tax credits, which is to be paid over a maximum of eight years beginning in 2018.

We have not included in the table above approximately \$24 million of liabilities for unrecognized tax benefits related to the uncertainty with regard to the deductibility of certain business expenses incurred as well as related accrued interest and penalties. These liabilities may increase or decrease over time as a result of tax examinations, and given the status of the examinations, we cannot reliably estimate the period of any cash settlement with the respective taxing authorities. These liabilities exclude amounts that are temporary in nature and for which we anticipate that over time there will be no net cash outflow.

Contingent Liabilities

We had no material contingent obligations as of December 31, 2023. Please see Note 18 for further discussion.

Gearing Ratio

The gearing ratio of the Company, which was calculated by dividing total interest-bearing loans by total equity as of the end of the year, was 2.4% and nil as of December 31, 2023 and 2022, respectively.

Pledge of Assets

The Company is required to place bank deposits or purchase insurance to secure the balance of prepaid stored-value cards issued by the Company pursuant to regulatory requirements. \$21 million of time deposits in Short-term investments and \$28 million of time deposits in Long-term bank deposits and notes as of December 31, 2023, and \$81 million of time deposits in Long-term bank deposits and notes as of December 31, 2022 were restricted for use. Please see Note 12 for further discussion. As of December 31, 2023 and 2022, we also had \$79 million and \$1 million short-term deposits pledged to secure the \$168 million and \$2 million outstanding bank borrowing, respectively. Please see Note 9 for further discussion.

Significant Investments Held

None of our investments held constituted significant investments required to be disclosed pursuant to Appendix 16 to the Hong Kong Listing Rules (i.e. the new Appendix D2 to the Hong Kong Listing Rules with effect from 31 December 2023). Refer to Note 3 for our business acquisitions and equity investments.

Future Plans for Material Investments and Capital Assets

We currently expect our fiscal year 2024 capital expenditures to be in the range of approximately \$700 million to \$850 million. Please see Liquidity and Capital Resources section for further discussion.

Material Acquisitions and Disposal of Subsidiaries and Joint Venture

During the year ended December 31, 2023 and 2022, we did not have any material acquisitions and disposals of subsidiaries and joint venture.

New Accounting Pronouncements

Recently Adopted Accounting Pronouncements

See Note 2 for details of recently adopted accounting pronouncements.

New Accounting Pronouncements Not Yet Adopted

In March 2023, the FASB issued ASU 2023-01, *Leases (Topic 842) — Common Control Arrangements* (“ASU 2023-01”). It requires all lessees, including public business entities, to amortize leasehold improvements associated with common control leases over their useful life to the common control group and account for them as a transfer of assets between entities under common control through an adjustment to equity when the lessee no longer controls the use of the underlying asset. ASU 2023-01 is effective for the Company from January 1, 2024, with early adoption permitted. We will adopt this standard in the first quarter of 2024, and do not expect the adoption of this standard to have a material impact on our financial statements.

In November 2023, the FASB issued ASU 2023-07, *Segment Reporting (Topic 280) — Improvements to Reportable Segment Disclosures* (“ASU 2023-07”), requiring public business entities to provide disclosures of significant expenses and other segment items. The guidance also requires public entities to provide in interim periods all disclosures about a reportable segment’s profit or loss and assets that are currently required annually. For the Company, ASU 2023-07 is effective for annual periods from January 1, 2024, and for interim periods from January 1, 2025, with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

In December 2023, the FASB issued ASU 2023-09, *Income Taxes (Topic 740) — Improvements to Income Tax Disclosures* (“ASU 2023-09”), requiring public business entities to provide additional information in the rate reconciliation and additional disclosures about income taxes paid. ASU 2023-09 is effective for the Company from January 1, 2025, with early adoption permitted. We are currently evaluating the impact the adoption of this standard may have on our financial statements.

Critical Accounting Policies and Estimates

Our reported results are impacted by the application of certain accounting policies that require us to make subjective or complex judgments. These judgments involve estimations of the effect of matters that are inherently uncertain and may significantly impact our quarterly or annual results of operations or financial condition. Changes in the estimates and judgments could significantly affect our results of operations, financial condition and cash flows in future years. A description of what we consider to be our most significant critical accounting policies and estimates follows.

Loyalty Programs

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

Breakage Revenue

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

Impairment or Disposal of Long-Lived Assets

We review long-lived assets of restaurants (primarily operating lease right-of-use assets and property, plant and equipment ("PP&E")) semi-annually for impairment, or whenever events or changes in circumstances indicate that the carrying amount of a restaurant may not be recoverable. We evaluate recoverability based on the restaurant's forecasted undiscounted cash flows, which are based on our entity-specific assumptions, to the carrying value of such assets. The forecasted undiscounted cash flows incorporate our best estimate of sales growth based upon our operation plans for the unit and actual results at comparable restaurants. For restaurant assets that are deemed not to be recoverable, we write down the impaired restaurant to its estimated fair value. In determining the fair value of restaurant-level assets, we consider the highest and best use of the assets from market participants' perspective, which is represented by the higher of the forecasted discounted cash flows of operating restaurants and the price market participants would pay to sub-lease the operating lease right-of-use assets and acquire remaining restaurant assets, even if that use differs from the current use by the Company. Key assumptions in the determination of fair value include reasonable sales growth assumption in generating after-tax cash flows that would be used by a franchisee in the determination of a purchase price for the restaurant, and market rental assumption for estimating the price market participants would pay to sub-lease the operating lease right-of-use assets. Estimates of forecasted cash flows of operating restaurants are highly subjective judgments and can be significantly impacted by changes in the business or economic conditions. Estimates of the price market participants would pay to sub-lease the operating lease right-of-use assets are based on comparable market rental information that could be reasonably obtained for the property. In situations where the highest and best use of the restaurant-level assets from market participants' perspective is represented by sub-leasing the operating lease right-of-use assets and acquiring the remaining restaurant assets, the Company continues to use these assets in operating its restaurant business, which is consistent with its long-term strategy of growing revenue through operating restaurant concepts.

When we believe it is more likely than not a restaurant or groups of restaurants will be refranchised for a price less than their carrying value, but do not believe the restaurant(s) have met the criteria to be classified as held for sale, we review the restaurants for impairment. Expected net sales proceeds are generally based on actual bids from the buyer.

The discount rate used in the fair value calculations is our estimate of the required rate-of-return that a franchisee would expect to receive when purchasing a similar restaurant or groups of restaurants and the related long-lived assets. The discount rate incorporates rates of returns for historical refranchising market transactions and is commensurate with the risks and uncertainty inherent in the forecasted cash flows.

We evaluate indefinite-lived intangible assets for impairment on an annual basis or more often if an event occurs or circumstances change that indicates impairment might exist. We perform our annual test for impairment of our indefinite-lived intangible assets at the beginning of our fourth quarter. When we evaluate these assets for impairment, we have the option to first perform a qualitative assessment to determine whether an intangible asset group is impaired. If we believe, as a result of the qualitative assessment, that it is more likely than not that the fair value of the intangible asset group is less than its carrying amount, we will then perform a quantitative assessment. Fair value is an estimate of the price a willing buyer would pay for the intangible asset and is generally estimated by discounting the expected future after-tax cash flows associated with the intangible asset. The discount rate is our estimate of the required rate-of-return that a third-party buyer would expect to receive. These estimates are highly subjective, and our ability to achieve the forecasted cash is affected by factors such as changes in our operating performance and business strategies and changes in economic conditions. Our indefinite-lived intangible assets had a book value of \$127 million and \$130 million as of December 31, 2023 and 2022, respectively, representing two material indefinite-lived intangible assets, which are our Little Sheep and Huang Ji Huang trademarks.

In the year ended December 31, 2023, we elected to perform the qualitative impairment assessment for the Little Sheep and Huang Ji Huang trademarks by evaluating all pertinent factors, including but not limited to macroeconomic conditions, industry and market conditions and financial performance and concluded that it was more likely than not that the assets were not impaired. No impairment charges on trademarks related to Little Sheep and Huang Ji Huang were recorded in 2023 and 2022.

Our finite-lived intangible assets that are not allocated to an individual restaurant are evaluated for impairment whenever events or changes in circumstances indicate that the carrying amount of the intangible asset may not be recoverable. An intangible asset that is deemed not recoverable on an undiscounted basis is written down to its estimated fair value, which is our estimate of the price a willing buyer would pay for the intangible asset based on discounted expected future after-tax cash flows. For purposes of our impairment analysis, we update the cash flows that were initially used to value the finite-lived intangible asset to reflect our current estimates and assumptions over the asset's future remaining life.

Impairment of Goodwill

We evaluate goodwill for impairment on an annual basis as of the beginning of our fourth quarter or more often if an event occurs or circumstances change that indicates impairment might exist. When we evaluate goodwill for impairment, we have the option to first perform a qualitative assessment to determine whether it is more likely than not the fair value of a reporting unit is less than its carrying amount. If we believe, as a result of the qualitative assessment, that it is more likely than not that the fair value of the reporting unit is less than its carrying amount, we will then perform a quantitative assessment. Our reporting units are our individual operating segments. Fair value is the price a willing buyer would pay for the reporting unit, and is generally estimated using discounted expected future after-tax cash flows from the business operation of the reporting unit.

Future cash flow estimates and the discount rate are the key assumptions when estimating the fair value of a reporting unit. Future cash flows are based on growth expectations relative to recent historical performance and incorporate sales growth and margin improvement assumptions that we believe a third-party buyer would assume when determining a purchase price for the reporting unit. The sales growth and margin improvement assumptions that factor into the discounted cash flows are highly correlated as cash flow growth can be achieved through various interrelated strategies such as product pricing and restaurant productivity initiatives. The discount rate is our estimate of the required rate-of-return that a third-party buyer would expect to receive when purchasing a business from us that constitutes a reporting unit. We believe the discount rate is commensurate with the risks and uncertainty inherent in the forecasted cash flows. These estimates are highly subjective, and our ability to achieve the forecasted cash is affected by factors such as changes in our operating performance and business strategies and changes in economic conditions.

Our goodwill of \$1,932 million as of December 31, 2023 was related to the KFC, Pizza Hut, Huang Ji Huang and Lavazza reporting units. In the year ended December 31, 2023, we elected to perform a qualitative impairment assessment for each of our individual reporting units of KFC, Pizza Hut, Huang Ji Huang and Lavazza. Based on our qualitative assessment, the Company concluded that no changes in events or circumstances have occurred that indicated impairment may exist and it was more likely than not that the fair value of the reporting units exceeds their carrying amount and therefore no quantitative assessment was required. No impairment charge on goodwill was recorded in 2023 and 2022.

Share-Based Compensation

We account for share awards issued to employees in accordance with Accounting Standards Codification Topic 718 (“ASC 718”), *Compensation-Stock Compensation*. Share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense, net of estimated forfeitures, over the requisite service period, which is generally the vesting period. We recognize share-based compensation expense for awards granted to employees and non-employee directors using the straight-line method.

We estimated the fair value of stock options and SARs at the grant date using the Black-Scholes option-pricing model (“the BS model”). It should be noted that the option-pricing model requires the input of highly subjective assumptions. Changes in the subjective input assumptions can materially affect the fair value estimate and, as a result, our operating profit and net income. PSUs have market conditions that are based on the closing price of Yum China’s stock or relative total shareholder return against selected indices or the constituents of the indices measured over the performance period. The fair values of PSUs have been determined based on the outcome of a Monte-Carlo Simulation model (the “MCS model”).

Under the BS and MCS models, we made a number of assumptions regarding the fair value of the share-based awards, including:

- the expected future volatility of the price of shares of Yum China common stock;
- the risk-free interest rate;
- the expected dividend yield; and
- the expected term.

We estimated the expected future volatility of the price of shares of Yum China common stock based on the historical price volatility of the publicly traded shares of common stock of comparable companies in the same business as Yum China as well as the historical volatility of the Company’s common stock. The risk-free interest rate was based on the U.S. Treasury zero-coupon yield in effect with maturity terms equal to the expected term or performance measurement period of the awards. The dividend yield was estimated based on the Company’s dividend policy. We use historical turnover data to estimate the expected forfeiture rate.

Income Taxes

Uncertain Tax Positions

We are subject to reviews, examinations and audits by Chinese tax authorities, the IRS and other tax authorities with respect to income and non-income based taxes. We recognize the benefit of positions taken or expected to be taken in our tax returns when it is more likely than not that the position would be sustained upon examination by these tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than 50% likely of being realized upon settlement. At December 31, 2023 and 2022, we had \$20 million and \$21 million, respectively, of unrecognized tax benefits related to the uncertainty with regard to the deductibility of certain business expenses incurred. The ultimate outcome for a particular tax position may not be determined with certainty prior to the conclusion of a tax audit and, in some cases, appeal or litigation process. The actual benefits ultimately realized may differ from the Company’s estimates. We evaluate unrecognized tax benefits, including interest thereon, on a quarterly basis to ensure that they have been appropriately adjusted for events, including change or developments with respect to tax audits, audit settlements and expiration of the statute of limitation, which may impact our ultimate payment for such exposures.

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

Unremitted Earnings of Foreign Subsidiaries

We have investments in our foreign subsidiaries where the carrying values for financial reporting exceed the tax basis. Except for the planned but yet to be distributed earnings, we have not provided deferred tax on the portion of the excess that we believe is indefinitely reinvested, as we have the ability and intent to indefinitely postpone the basis differences from reversing with a tax consequence. The Company's separation from YUM was intended to qualify as a tax-free reorganization for U.S. income tax purposes resulting in the excess of financial reporting basis over tax basis in our investment in the China business continuing to be indefinitely reinvested. The excess of financial reporting basis over tax basis as of December 31, 2017 was subject to the one-time transition tax under the Tax Act as a deemed repatriation of accumulated undistributed earnings from the foreign subsidiaries. However, we continue to believe that the portion of the excess of financial reporting basis over tax basis (including earnings and profits subject to the one-time transition tax) is indefinitely reinvested in our foreign subsidiaries for foreign withholding tax purposes. We estimate that our total temporary difference for which we have not provided foreign withholding taxes is approximately \$3 billion at December 31, 2023. The foreign withholding tax rate on this amount is 5% or 10% depending on the manner of repatriation and the applicable tax treaties or tax arrangements.

See Note 16 for a further discussion of our income taxes.

Quantitative and Qualitative Disclosures About Market Risk

Foreign Currency Exchange Rate Risk

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

As substantially all of the Company's operations are located in China, the Company is exposed to movements in the RMB foreign currency exchange rate. For the year ended December 31, 2023, the Company's Operating profit would have decreased by approximately \$106 million if the RMB weakened 10% relative to the U.S. dollar. This estimated reduction assumes no changes in sales volumes or local currency sales or input prices.

Commodity Price Risk

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

Investment Risk

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

Other Information

Compliance with the Corporate Governance Code

The Board believes that good corporate governance is a critical factor in achieving business success and in fulfilling the Board's responsibilities to stockholders. The Board has adopted corporate governance principles which are intended to embody the governance principles and procedures by which the Board functions. These principles are available on the Company's website. Our corporate governance principles and practices are in line with the principles in the Corporate Governance Code (the "Corporate Governance Code") as set out in Part 2 of Appendix 14 to the Hong Kong Listing Rules (i.e. the new Appendix C1 to the Hong Kong Listing Rules with effect from 31 December 2023).

After the Primary Conversion, we have complied with all the code provisions of the Corporate Governance Code, save for the following.

Code Provisions A.2.1, B.3.1, D.3.3, D.3.7 and E.1.2 of the Corporate Governance Code require the charters of the Audit Committee, the Compensation committee and the Nominating and Governance Committee (collectively, the "Board Committees") to include at least the terms as set out in such paragraphs. Currently, the charters of the Board Committees do not include certain of such terms. The Company has adopted the charters of the Board Committees in accordance with the NYSE listing rules and the rules of the U.S. Securities and Exchange Commission (to the extent applicable), which in material ways are similar to the terms of reference as required under the Corporate Governance Code despite different languages being used. The relevant Board Committees have in practice carried out the relevant responsibilities as required under the Corporate Governance Code.

Code Provisions E.1.2(a), (c) and (d) of the Corporate Governance Code require the remuneration committee to be responsible for Directors' remuneration. Currently, the Nominating and Governance Committee is responsible for reviewing and making recommendations to the Board with respect to the compensation and benefits of the Directors. Given (i) it is customary for U.S. public companies to delegate this responsibility to either the Nominating and Governance Committee or the Compensation Committee, it is also common for the U.S. listed companies to have the Nominating and Governance committee to carry out such responsibility; (ii) the Nominating and Governance Committee has been carrying out such responsibility since the Company's listings on the NYSE and the HKEX; and (iii) the composition of the Nominating and Governance Committee also complies with the composition requirement of the remuneration committee as required under Rule 3.25 of the Hong Kong Listing Rules; the Board believes the current arrangement has achieved good corporate governance with respect to Directors' remuneration.

Purchase, Sale or Redemption of the Company's Listed Securities

During the year ended December 31, 2023, the Company repurchased 12.4 million shares of common stock on the NYSE for an aggregate consideration of \$617 million. All shares repurchased under the current and previous authorizations were retired and resumed the status of authorized and unissued shares of common stock. We have used share repurchases as a means of returning cash to stockholders. Details of shares repurchased during the year ended December 31, 2023 are as follows:

Month of Repurchase	No. of Shares Repurchased* (thousands)	Price paid per share		Aggregate Consideration* (US\$ millions)
		Highest US\$	Lowest US\$	
January	337	\$ 62.43	\$ 55.81	\$ 20
February	316	63.01	56.97	19
March	376	64.56	57.78	23
April	303	64.65	59.82	19
May	365	64.42	54.93	22
June	361	60.44	55.87	21
July	351	61.93	54.71	20
August	2,001	60.17	51.10	109
September	514	58.19	51.38	28
October	601	56.10	50.87	32
November	5,519	47.45	41.25	247
December	1,369	43.59	38.99	56
Total	<u>12,414</u>			<u>\$ 617</u>

*: Shares and aggregate consideration may not add due to rounding

Save as disclosed above, neither the Company nor any of its subsidiaries had purchased, sold or redeemed any of the Company's listed securities during the year ended December 31, 2023.

Audit Committee Review of Financial Statements

The Audit Committee has reviewed the consolidated financial statements and annual results of the Company for the year ended December 31, 2023. The Audit Committee has also discussed matters with respect to the accounting policies and practices adopted by the Company and internal control with members of senior management and the external auditor of the Company, KPMG.

Scope of Work of the Company's auditor

The consolidated financial statements of the Company and its subsidiary companies for the year ended December 31, 2023 prepared in accordance with U.S. GAAP have been audited by the Company's auditor, KPMG. The unqualified auditor's report is set out on pages 2 to 6 of this announcement. The consolidated financial statements of the Company and its subsidiary companies for the year ended December 31, 2023 have also been reviewed by the Audit Committee.

Important Events after the Reporting Period

Save as disclosed in Note 19 to the Consolidated Financial Statements, no important events affecting the Company occurred since December 31, 2023 and up to the date of this announcement.

Publication of Annual Results and Annual Report

This annual results announcement is published on the website of the HKEX (www.hkexnews.hk) and the website of the Company (<http://ir.yumchina.com>). The annual report of the Company for the year ended December 31, 2023 will be published on the aforesaid websites and dispatched to the Company's shareholders in due course.

Language

If there is any inconsistency between the English version and Chinese version of this announcement, the English version shall prevail, provided that if there is any inconsistency between the Chinese names of the entities or enterprises established in the PRC mentioned in this announcement and their English translations, the Chinese names shall prevail.