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Emerging Markets Daily

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May 29, 2014, 2:43 P.M. ET

First Global: Emerging Markets Expansion Fueling Yum Growth

By Teresa Rivas

Last month, **Yum Brands** ([YUM](#)) reported a better-than-expected [first quarter](#), helped by strong margins in China.

Today, **First Global Research's Devina Mehra** and **Rajiv Ghosh** have a note out, reiterating their Outperform rating on the stock, given their thesis that an increasing number of restaurants in emerging markets will drive growth, which isn't being fully accounted for in the p/e.

Some figures from the report:

YUM's sales in China jumped up by 19.8% Y-o-Y and profitability was up by a spectacular 85% Yo-Y, thus taking the region's profit contribution to 46.5% in Q1 CY14. The company's ex-China sales were down 3% Y-o-Y and profit was down 10% Y-o-Y. Reported sales at KFC outside China and India rose marginally by 0.8% Y-o-Y and the reported profit declined slightly by 1.2% Y-o-Y. KFC (excluding China and India) contributed to 26.6% of the segment's profit for YUM in Q1 CY14. China and KFC outside China and India contributed a solid 73% of the company's total profit...YUM's operating margin expanded by 235 bps Y-o-Y, on the back of an improvement of 730 bps Y-o-Y in margins in China, which more than offset the decline of 170 bps Y-o-Y in the company's margins outside China

Given this performance, Mehra and Ghosh believe that China has "clearly turned around and pulled Yum back on the growth path." They see Yum continuing to be a strong growth story, delivering a compound annual growth rate of 20% over the next two years, bolstered by expansion in emerging markets, regions that are still underpenetrated. At less than 18 times their 2015 earnings estimates, they think that the stock remains attractive relative to peers, which are trading closer to 20 times forward.

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