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PRESENTATION

Operator

Thank you for standing by, and welcome to the Yum China Fourth Quarter and Fiscal Year 2023 Earnings Conference Call. (Operator Instructions)

I would now like to hand the conference over to Ms. Michelle Shen, IR Director. Please go ahead.

Michelle Shen ***Yum China Holdings, Inc. - Director of IR***

Thank you, operator. Hello, everyone. Thank you for joining Yum China's Fourth Quarter 2023 Earnings Conference Call. On today's call are our CEO, Ms. Joey Wat; and our CFO, Mr. Andy Yeung.

I would like to remind everyone that our earnings call and investor materials contain forward-looking statements, which are subject to future events and uncertainties. Actual results may differ materially from these forward-looking statements. All forward-looking statements should be considered in conjunction with the cautionary statements in our earnings release and the risk factors included in our filings with the SEC. This call also includes certain non-GAAP financial measures and should carefully consider the comparable GAAP measures. Reconciliation of non-GAAP and the GAAP measures is included in our earnings release. You can find the webcast of this call and the PowerPoint presentation on our IR website. Please note that during today's call, all year-over-year growth results exclude the impact of foreign currency unless otherwise noted.

Now I would like to turn the call over to Joey Wat, CEO of Yum China. Joey?

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Thank you. Hello, everyone, and thank you for joining us today. It's Chinese New Year this coming Saturday. I want to wish everyone a happy and healthy Year of the Dragon. I would like to kick off today's call by expressing my sincere appreciation to all our employees. Their incredible efforts helped Yum China deliver exceptional growth in the fourth quarter and for the full year.

2023 was a pivotal time for our business. The transformation of our business fundamentals in the past few years have enabled us to seize opportunities emerging from China's reopening and evolving market conditions. In 2023, we hit record breaking revenue of $11 billion and grew system sales 21% year-over-year, outperforming the industry. Operating profit soared to $1.1 billion, an all-time high, excluding special items. Core operating profit grew 79%. We opened a record 1,697 net new stores, expanding our total store count to 14,644 stores. KFC reached 10,296 stores, Pizza Hut reached 3,312 stores. On today's call, I would like to walk you through the tremendous growth opportunities we see and discuss our strategies to capture them in 2024 and beyond.

For the past 36 years, we have been the market leader in China. During this time, countless restaurant operators have passed in and out of favor. Instead of being "Wang Hong", or "the flavor of the month", we want to be "Chang Hong" or "the flavor of the decade or even next several decades". In this developing market, where the restaurant industry is still growing double digits even during 2023, we see a long runway of growth for our brands.

KFC still only serves 1/3 of the China population. Our next ambitious target is to extend our reach to 1/2 of the population by 2026. How? By being closer to our customers. This means adding store density in existing cities and entering new cities. KFC currently operates across 2,000 cities in China and is tracking an additional 1,000 cities.

For Pizza Hut and our emerging brands, the white space is even larger. China is vast, with significant regional and city tier differences. In lower-tier cities, urbanization and long-term consumption upgrades are presenting attractive opportunities for us. With lower living costs, consumers in these cities have significant purchasing power for our products. So as an example, premium beef burgers sell well in lower-tier cities, just as in high-tier cities. Over 1/2 of our new stores in recent years are in lower-tier cities. These stores have performed well, benefiting from lower labor costs and rent. And the ticket average is as good as in higher-tier cities. For now, we are mainly serving middle-class consumers in these markets. As we expand, we see further opportunity in widening price points to broaden our addressable customer base.

Our vision is to reach 20,000 stores by 2026. We will continue to protect our new store payback at 2 years for KFC and 3 years for Pizza Hut. Over the past years, we have been improving our fundamental capabilities to reach this target. This is the key reason we can expand at an accelerated speed. Some of these improvements include: first, flexible store format with lower upfront investment open up more site potential across city tiers; second, cost structure rebasing lowered our rent ratio in 2023 to 8.7% of sales, the lowest level in the past 10 years. The majority of our leases are based on variable rent; third, improved operating capabilities. AI-enabled digital tools empower our capable restaurant managers to oversee multiple stores without compromising quality. This also solves the bottleneck of having enough good RGMs as we expand rapidly. Finally, strategic franchise partnerships allow us to gain access to locations that were beyond our reach before, such as highway service centers.

In addition to new store growth, our same-store sales grew 7% in 2023. It was fueled by a 12% increase in transactions, indicating healthy growth. Our innovative menus, excellent value for money and effective online channels captured over 1.7 billion transactions last year.

Now let's talk about food innovation. In 2023, we rolled out more than 500 new or upgraded products. That means we offered something new every week. Some examples include KFC's Beef Wrap with spicy duck blood and Chicken Taco with Bullfrog and Pizza Hut's Black Thorn durian pizza. These may sound a bit exotic, but I can assure you they are very popular in China.

Over the years, many of our most popular products have entered our $100 million club in U.S. dollar sales, and 2023 was no exception. Our Golden SPA Chicken Burger (Huang Jin SPA Ji Pai Bao) launched in quarter 4 of 2022 joined our $100 million club in 2023 with very little spent on marketing. It offers amazing value for money using chicken breast meat and is very popular with younger customers. Chicken breast meat is very high-quality protein, but the cost of breast meat is much cheaper in China than dark meat. Our juicy whole chicken (Mi Zhi Quan Ji) is another remarkable success story. We launched it in 2021. And by 2023, we sold over 50 million whole chickens. Whole chicken and beef burgers combined now contribute close to 6% of our sales, more than the original recipe chicken that we have been selling in the last 36 years.

KCOFFEE also grew rapidly in 2023, driven by product innovation and improving accessibility. 190 million cups were sold last year, a 35% increase year-over-year. Our coffee offers great value for money at below RMB 9.9 per cup. Great value for money remains a key factor to drive traffic. In addition to the great food that I just mentioned, we have strategically enriched our menus with entry price point products to attract incremental customers. Our superb in-house supply chain empowers us to innovate and offer fantastic value while protecting margins.

At KFC, apart from our long-lasting value platform, Crazy Thursday (Feng Kuang Xing Qi Si), we identified entry price combos as huge underserved market segments. Last year, KFC expanded the choices of its RMB 20 combo, including our recent Chinese burgers (Bing Han Bao), which has been well received by customers. For pizza, the under RMB 50 segment represents a significant portion of the market but is underserved at Pizza Hut. In November last year, we launched 4 entry priced pizzas, including the delicious Texas barbeque chicken pizza. We will continue to add more cost-conscious choices to our menu this year to capture incremental sales. We also see amazing potential to further grow delivery sales. We are adjusting our delivery pricing structure to be more aligned with market norms. This will help us capture incremental traffic, especially in the smaller ticket segment and from more price-sensitive customers.

Our third traffic driver is the effective use of our own and third-party online channels. In 2023, our digital sales surpassed $9.2 billion. Of that, about 1/3 came from our own SuperAPP, 1/3 from mini programs and 1/3 from aggregators. Our own SuperAPP sales grew rapidly last year, up 35%. We continue to actively recruit and engage members. Our loyalty programs exceeds 470 million members, who contributed a record 65% of our sales. The purchase frequency of our K-Friends, our most loyal customers was more than 100 times a year. Our collaborations with major e-commerce and social media platforms extend our reach beyond physical stores. This allows us to attract new customers and promote new offers in a cost-effective manner. We consistently led the industry in terms of sales generated on these platforms. Our brands are deeply ingrained in China, well-loved and trusted by consumers. We continued to deliver amazing growth despite operating in a challenging environment. KFC is thriving and remains our key growth engine with a record operating profit of $1.2 billion in 2023. Pizza Hut is taking off, adding 409 stores in 2023 alone compared to just 41 stores in 2019. Their 2023 core operating profit tripled year-over-year. Lavazza is on the right track with sales doubled and notable improvement in store economics. Taco Bell is making notable progress, yet there's more work in store model refinement and menu localization to be done. Little Sheep returned to profitability in 2023. Its innovative store model, which caters to smaller party sizes has achieved initial success. We expect good momentum in opening stores, both in China and overseas. Huang Ji Huang continues to be resilient, maintaining profitability every year since we acquired it in 2020. In 2023, Huang Ji Huang tripled profits and opened 40 net new stores. We will continue expanding our store footprint in China and overseas this year.

Onwards into 2024, we are serving up a combination of exciting menu items, awesome toys and games for Chinese New Year. KFC's newest innovation, the Happy Fried Egg in Spicy Sauce Chicken Burger, (Kuai Le Fei Zhi Zha Dan Kao JI Tui Bao) is absolutely delicious. It's comfort food for your soul. We are also offering our widely popular Golden Bucket again this year. It has a very lucky and down to earth name, (Kaui Fa Cai), which means get rich soon. And the first letters also stand for KFC. So right now, it's getting around, getting more popular to wish each other KFC in China.

Pizza Hut is launching 18 new products, including Wagyu beef pizza (Xue Hua He Niu Pi Sa) at just RMB 69. The abundant choices and value are amazing. Although consumers are more rational and price-sensitive in the current economy, there is a strong desire to indulge, especially during holidays. Our enticing offers are designed to generate excitement and attract traffic. I eagerly anticipate this vibrant trading period.

With that, I will turn the call over to Andy. Andy?

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you, Joey, and happy Chinese New Year, everyone. Today, I will discuss our fourth quarter and full year 2023 financial results followed by our outlook for 2024 as well as our capital allocation strategy. We delivered robust results in the fourth quarter and reached significant milestones for the full year.

In response to current operating environment, we adapted our strategy and launched attractive campaigns. This allow us to drive incremental traffic and sales. We maintained 21% system sales growth in the quarter, same as the full year. Core operating profit in the fourth quarter quadrupled year-over-year and restaurant margin improved on a comparable basis.

As you may have noticed, we have introduced core operating profit to enhance comparability of our results and provide additional transparency on how we evaluate the performance of our core operations. This metric excludes foreign exchange impact, special items and other items affecting comparability. For further details, please refer to the reconciliation table in our earnings release and presentation.

Let's now look at our fourth quarter performance in more detail. System sales increased 21% year-over-year, led by a 12% net new unit contribution, 4% same-store sales growth and lapping temporary closures from the pandemic in the prior year. By brand, KFC system sales increased 20% year-over-year. Same-store sales growth of 3%, mainly came from 16% same-store traffic growth and 11% lower ticket average. To put it into perspective, ticket average in the fourth quarter was RMB 39, the same as last quarter and higher than 2019. Overall ticket average remained stable in the past 5 years, and our focus has been to grow our traffic. A strong rebound of dine-in sales, especially for breakfast daypart and successful expansion of our entry price offerings contributed to lower ticket average. Pizza Hut system sales increased 24% year-over-year. Same-store sales growth of 6% was driven by strong traffic growth of 15% and ticket average decrease of 8%. It is by design and consistent with our revitalization strategy since 2017.

Our recent focus has been to expand pizza offerings below RMB 50 and smaller party-size options. The strategy has proven effective in expanding our addressable market and capturing incremental traffic. Our restaurant margin was 10.7%, 30 basis points higher than last year. On a comparable basis, our restaurant margin grew by 170 basis points. The improvement was mainly from sales leveraging, lower rider costs, more favorable commodity prices and lower advertising expenses. This more than offset increased marketing campaigns and wage inflation.

Now let's go through the key items.

Cost of sales was 32.4%, 50 basis points higher year-over-year. During the quarter, commodity prices were favorable. We passed that to consumers by offering better value for money.

Cost of labor was 29.0%, flattish year-over-year or improved 40 basis points on a comparable basis. Sales leveraging, lower rider cost and efficiency gains more than offset wage increases for frontline staff.

Occupancy and other was 27.9%, improved 100 basis points year-over-year or 180 basis points on a comparable basis. This came from lower rent and depreciation expenses as well as more efficient management of marketing and advertising expenses. G&A expenses increased 6% year-over-year. We tightly managed cost and headcount to keep G&A growth below revenue growth.

Operating profit was $110 million. Core operating profit quadrupled.

Our effective tax rate was 24.2% in Q4 and 26.9% for the full year. Lower effective tax rate on a year-over-year basis was mainly due to more preferential tax benefits and higher pretax income.

Diluted EPS was $0.23. Excluding special items, foreign exchange and Meituan investments, the increase was 164%.

Now let's turn to our outlook. We remain excited about the vast growth opportunities in China. In 2024, we anticipate opening 1,500 to 1,700 net new stores. After 36 years in China, it's amazing that we are still growing our stores at double digits. Our healthy new store payback give us confidence to continue expansion and reach 20,000 stores by 2026.

As we shared at our Investor Day last year, we aim to grow system sales and operating profit by high single-digit to double-digit compound annual growth rate and EPS by double-digit compound annual growth rate from 2024 to 2026. We will continue to capture our new opportunities by innovating new products, launching engaging campaigns and widening price points. This helps us to expand our addressable customer base and drive incremental sales. We are confident in executing our 3-year plan. Cost structure rebasing continues to be a key focus. Our efficient cost management will enable us to pass the savings back to customers and drive traffic while protecting margins.

Before I delve into the first quarter outlook, I would like to remind everyone that first quarter 2023 was a phenomenal quarter during which we achieved record-setting profit. We captured robust demand from the reopening, delivering solid sales. On the cost side, we benefited from substantial temporary relief and VAT deduction benefit, which is not expected to recur this year. We also benefited from labor productivity gain from labor shortage in the first quarter last year.

Looking ahead to the first quarter this year, as Joey mentioned, we are now operating under a new normal. Consumers are more rational in spending, yet have great expectation and appetite for new and exciting products, and that can offer great value for money. In response, we have strategically planned a very intensive number of new product launches and attractive promotions. We have also dedicated more resources to drive sales and capture the peak Chinese New Year traffic. In light of these challenges, we will work hard on productivity improvement and cost control, including G&A expenses. Our aim is to maintain our core operating profit relatively stable on a comparable year-over-year basis in the first quarter. This will exclude temporary relief, VAT deduction benefits and changes in foreign exchange rates.

Now let's turn to capital allocation. There's no better investment than investing in our own organic growth while delivering excellent returns to our shareholders. With a strong focus on efficient capital returns, CapEx in 2023 totaled $710 million at the low end of our original target. In 2024, CapEx is expected to be in the range of $700 million and $850 million. Since the spin-off, we have returned $3 billion to shareholders, and we plan to return another $3 billion in the next 3 years. We accelerated return to shareholders in 2023, returning a record $833 million in cash dividends and share repurchases. In 2024, we plan to further accelerate return to shareholders to around $1.5 billion. We raised our dividend by 23% from $0.13 to $0.16. That would be roughly $250 million for the full year.

As for share repurchases, we already have a $750 million program in place and plan to further increase repurchases by around $500 million. So a total of $1.25 billion share repurchase in 2024. This is equivalent to around 9% of our market cap with the current share price. The stepping up of returns demonstrates our confidence in our cash-generating capabilities and commitment to return excessive cash to our shareholders.

Let me pass it back to Joey for closing remarks. Joey?

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Thank you, Andy. Before we turn to Q&A, I would like to just summarize. In 2023, we reached record top line and bottom line as well as net new store openings, and we returned record level of cash to our shareholders through dividends and buybacks. These achievements were made possible by the transformations we implemented in our fundamental capabilities. Ranging from flexible store formats and food innovation at scale to superb supply chain management and industry-leading AI application. We have showcased our expertise and agility to navigate diverse market conditions. Acknowledging the high expectations our shareholders hold for us, we, in turn, set equally high standards for ourselves. We are fully committed to our 3-year growth target and generating long-term sustainable value for our shareholders. I would like to thank our shareholders for your continued support.

With that, I will pass it back to Michelle.

Michelle Shen ***Yum China Holdings, Inc. - Director of IR***

Thank you, Joey. Now we will open the call for questions. In order to give more people the chance to ask questions, please limit your questions to one at a time. Operator, please start the Q&A.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions) Your first question comes from Michelle Cheng with Goldman Sachs.

Michelle Cheng ***Goldman Sachs Group, Inc., Research Division - Co-head of Asia Consumer Research***

Joey, Andy, congrats for still very resilient result and also the impressive shareholder returns. While we understand the company's strong long-term position, but my question still want to focus a bit on the short term. So can you give us some colors regarding the pre-Chinese New Year traffic and same-store sales trend? And also, I think Andy mentioned about in first quarter, we are looking for more steady core operating profit. So can you clarify does this refer to like profit level or margin? So that's my question.

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you, Michelle. So let me address your question about clarification on our statement on core operating profit in the first quarter. We are looking at the overall level, not the margin side. I think it's important to keep in mind that the first quarter last year was an exceptional, phenomenal quarter that we achieved record profit, which was both by obviously the sales leverage from the initial reopening demand surge and then also some significant temporary relief, VAT deduction and labor gains from labor shortage. So those factors, we don't expect them to repeat again this year. And so I hope I answered that question on clarification.

Joey?

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

For the Chinese New Year?

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Yes.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

For the Chinese New Year trading, Andy has mentioned in his presentation earlier, it's a very, very tough lap because last Chinese New Year, we had a phenomenal trading during the 2023 Chinese New Year. But we have prepared a very full and exciting calendar for the Chinese New Year, not only the excitement of the marketing campaign, but products. And this is the first time we launched 5 new burgers, 5 weeks before going into the Chinese New Year. The excitement is there. The trading so far has been solid. But it's still a bit early because we really need to anticipate until the first day of the Chinese New Year. And then right now, the weather to a certain extent, the extreme weather is a bit of a wildcard. So that's where we are. And the focus going into the Chinese New Year after the first day of Chinese New Year is about our golden bucket. That was our total focus of all our operations team. But it's a very, very tough quarter. So we'll be happy if we actually can stay flat with the same-store sales. That's where we are right now.

Operator

Your next question comes from Brian Bittner with Oppenheimer.

Brian John Bittner ***Oppenheimer & Co. Inc., Research Division - MD & Senior Analyst***

As it relates -- I understand the first quarter is a very difficult comparison versus last year, but your goal is to keep the operating profit flat as I heard it. So what type of sales trends or same-store sales do you need in order to keep those operating profits flat? And then, Andy, once we get past this first quarter difficult comparison, how do you think about the way the year will build? How do you think about the second half of the year and the opportunity to grow sales there versus, say, maybe the first half of the year, which seems to be a more challenging setup?

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you, Brian. Yes. So I guess there's a lot of question about the first quarter outlook, rightly so. But before I, again, like dive into more detail on the first quarter outlook, let me just point out a couple of things, right. Overall, consistent with our 3-year plan, we are confident that we will maintain stable operating margins in the long run. As I mentioned, emphasis here is the long run because in the near term, we're going to have certain factors that affect the near-term situation. And then over the long term, we also would look into potential opportunity as we have been doing so to restructure our cost base, looking into improving our occupancy and other costs and then also leveraging our digital capability to better manage --that you have more effective advertising and also G&A expenses.

Now when we look at in 2023, restaurant margins and OP improved quite meaningfully. That's driven by same-store sales growth, right, and -- as well as cost restructuring. So KFC, it's already operating at very high level in terms of margins. And then Pizza Hut has a little bit more room for improvement in the long term.

Now if we look at the quarterly fluctuations, no, that's to be expected. As you mentioned, this is the first year, so normalizing operation post reopening. And then the first quarter and every quarter will be driven by some seasonality and then also it will be driven by obviously the sales trends and other factors because sales is always a very important factor in determining margin for us.

And as you mentioned last year, it was the high days. We achieved, again, a phenomenal quarter with record-setting [adjusted] operating profit (added by company after the call). And so -- and then there was also some one-off, as we mentioned, you can look at the reconciliation table roughly $30 million of one-time temporary relief that we received last year. So that has set up a high base for us this year.

Obviously, we'll work hard to manage our costs and drive sales. And in the first quarter, we are working under a new normal, right? And as we have mentioned in our prepared remarks, consumers are more rational in terms of their spending and eager for new and good value for money products. And so as Joey just mentioned, we have set up a number of -- very intensive number of product launches in our calendar. And then we also make sure that we have significant resources and campaigns to drive that sales and traffic, especially around Chinese New Year, okay? So, again, like Chinese New Year right now, it's too early to give a very solid outlook because this year Chinese New Year is a bit later compared to last year. So right now, as we look at our plan under the new normal is on track. However, as Joey mentioned, there's quite a few uncertainties with Chinese New Year because millions -- hundreds of millions of people are traveling in a very short period of time. And so the weather conditions as we have observed recently may or may not have an impact there. So we will continue to monitor the situation and adjust our plan as we always have been quickly to respond to any changes if necessary.

And so on the cost side, as I mentioned, obviously, we'll focus on productivity improvement and cost control. And then the goal is really to maintain a stable core operating profit after adjusting for the non-recurring items and foreign exchanges.

Operator

Your next question comes from Xiaopo Wei with Citi.

Xiaopo Wei ***Citigroup Inc. Exchange Research - Research Analyst***

I'd just look a little bit longer term in terms of business. And the first thing is if you look at the financials, in 2023, actually, a very good control G&A. If we look at the G&A to sales ratio, actually going down. If we look at the '24 as Joey and Andy mentioned, there are some factors which you cannot control in short term, like weather, like macro. So shall we be certain that the G&A to sales ratio will continue to go down in '24 because that we have more control on management of our admin cost at headquarter level? That is the first question.

The second question is, Andy, and Joey mentioned that the consumers are more rational this year. So could you comment on your competitors? Will -- competitor will be more rational as well with more rational consumers?

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

You handle the G&A. I'll handle the other one.

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Okay. I will just quickly talk a little bit about our cost efforts in conjunction with the G&A. So you can see that over the past few years and last year, we have put a lot of efforts to restructure our cost base. Our overall target for COS has been trying to keep it stable, and we have kept it stable at around 31% over the past few years. Obviously, COS moves seasonally somewhat. And we generally kept it around like, 31% plus or minus 1% for the full year.

And then the other one is labor cost. Labor cost, obviously, over the past few years because of the pandemic, we did see some impact on cost inflation and also delivery mix shift that drive up the labor cost. But we're able to more than offset that through the reductions in occupancy and other costs, a significant improvement compared to even pre-pandemic level by almost like 350 basis points. Our rent is at a record low right now as a percentage of sales. And so that's the longer-term trend. And our depreciation costs also came down because we have improved CapEx efficiencies and then also optimized our portfolio. So those are the longer-term trends.

In terms of the other margin lever for us, it's marketing and advertising because we have invested a lot in digital. And we -- in our member base right now is very large, 470 million members account for almost 65% of our sales already. So we think we'll be able to work on that in the future.

In terms of G&A, G&A expense as a percentage of sales has improved this year, like, to 5.8%. We continue to aim to continue to sustain that trend by ensuring that G&A growth would remain significantly lower than sales. To do that, obviously, we'll continue to improve labor cost, like our efficiencies in-house, new technologies and other automation tools to help automate some of those administrative tasks.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Xiaopo, I think I'm going to address your question by taking a step back by looking at the trends, the industry trend, the competitive trend, the consumer trend and then our own observation of our trading trend, and that hopefully will give you a holistic sense of our long-term view. First, industry. It's widely reported everywhere the China economy is growing at mid-single digits, but it's rarely reported that in 2023, our industry actually grew at double digits, actually 20%. So the recovery of the restaurant industry was very vibrant for 2023, and we are doing slightly better than the industry average.

However, for 2023, it was not easy to disaggregate many factors, including the growth or the recovery. One reason is sometimes the headlines could be misunderstood. I'll give you an example. For quarter 3, Yum China performance, the headline was reported that we grew revenue by 9%, missed the expectation by 5.7%. In reality, that is due to the foreign exchange difference. In our operating currency, which is in renminbi in China, our sales growth was 15%. But the reporting currency is the U.S. dollars, so it's reported at 9%. So if we disaggregate the foreign exchange from the operating currency, we see the difference. But fundamentally, our industry is growing very nicely. And then, of course, quarter 2, actually recovery in terms of the system sales was as much as 32%. So net-net, the industry recovered by 20% for 2023.

And that explains why other than Yum China so many competitors have been so aggressive to open new stores because opportunities are there. Is it competitive? Yes, absolutely. But fortunately, let's not forget, it has always been competitive in the last 36 years as well, and we have always been able to stay as a market leader in the last 30-some years as well. That's point 1.

Point 2, consumption trend. What I'm going to share is not the mainstream thinking. So we can agree to disagree. The mainstream thinking is China is going through consumption downgrade with many challenges. To a certain extent, it's true, but to a certain extent, customers are just getting more rational. However, what has not been mentioned at all is even with 5% GDP growth or mid-single-digit GDP growth, consumption upgrade is still also happening. Urbanization in China is still happening and we don't even need to look at the restaurant industry. We can look at China's top 6,000 shopping malls, which we track because we opened a lot of stores in those shopping malls. Within the segment of top 6,000 shopping malls, 2023 alone, there were 400 new shopping malls opened, not a small number, and 2/3 of them opened during the second half of the year, quarter 3 and quarter 4. And we are happy to report to our shareholders that these shopping mall location stores are better -- are trading better than the rest, well, apart from the tourist and transportation locations.

So when a shopping mall opens near the high street or close to high street, you can imagine the traffic moves to shopping mall and that itself is consumption upgrade. So come back to the rationalization of the customer, how do we respond to it? We are the market leader. We -- our focus in the last 30-some years and our ongoing focus is how to build a brand with a combination of good value, amazing products and opening up the price point. It's the combination of all of these, good food is always #1, and you can see why we continue to roll out so many good food. But at the same time, we are very cautious about the price point. That's the reason why original recipe chicken, after 36 years, the price is less than 5x of the price we launched 36 years ago. Only if the China housing price increased by the same ratio of original recipe than I think many Chinese people are even happier. So we do arrange of the product launch. We launched Wagyu Beef Burger that is priced as much as RMB 50, but at the same time, we also introduced the entry price value combo at RMB 20. This is the range we're going for and it's working.

Point 3, come to the trading pattern, what have we seen during quarter 4, and that will give us some idea about 2024 going forward. We celebrated 10,000 stores of KFC during December 15 this year. It was very meaningful for us. And it also, I hope, gives some confidence to our investors that Western QSR is solid and has nice growth. Quarter 4 started with a bit of softness. We don't have to reiterate again. But the trading improved in November and then improved a bit more in December. Good to know the trend is all right. And then the rebound of dine-in is very strong. However, delivery remains popular. It's still 36% of our business. Customers like the convenience. By trade zone, all improved.

As I mentioned earlier, tourist location and transportation hubs are recovering very well. Other than that, shopping malls are doing better than the others.

By region, recovery happened across all regions for quarter 4 and full year. Northern part of China recovery -- recovered the best because last year COVID lapping -- they were very difficult last year. And across the year, eastern part of China, which is the most important part of our business, it's still the most resilient region.

In city tier, Tier 2 inland, central part of China are recovering the best -- doing the best. They are the regional hub, vibrant economy, the living expenses are lower. One good example is Changsha. It's the destination for foodie in China. A lot of amazing food concept there. People go to Changsha just to enjoy different foods but little do people know, Changsha's rent is only about 10% to 15% of Shanghai, and yet ticket average is not too different. And these are the examples of the cities that are doing the best and going forward.

And Pizza Huts are doing very well in lower-tier cities, and that proves that the Pizza Hut business model works for lower-tier city.

Last, last but not least, our weekend trading right now is better than weekday. This is phenomenal for our team because if you remember in the previous earnings call, our weekend traffic was more challenged after the pandemic. People's behavior changed. The traffic during weekend dropped. What did we do? We launched the whole chicken and that product -- the whole chicken product targets very, very -- has a very clear focus to drive the delivery business during the weekend. Customers can buy the whole chicken, put it on the table, have a veggie and some rice, and this is a very nice meal and it worked. So now our weekend sales actually are better than weekday, huge milestone for our team's ability to build new product and new skills to grow with the change of customers. It's -- thank you for indulging me. It's a long answer, but I hope that gives you some sort of long-term view of the way that we trade our business. Thank you, Xiaopo.

Operator

Your next question comes from Lina Yan with HSBC.

Hau-Yee Yan ***HSBC, Research Division - Hong Kong and China Consumer Analyst***

Management, thanks for the very detailed walk-through of your business and your points are well taken that you are very nimble in reacting to competition. But when I talk to my clients, what I heard most over the last quarter was the market fears you provide the new price point, especially by launching more entry price offerings, it might drag down your ticket size. Obviously, Andy shared some numbers. Your ticket size, RMB 39 was very like a stable quarter-over-quarter Y-o-Y in fourth quarter. But I'm wondering if you could give us more color in terms of how those entry-price offering products are affecting your sales mix? And what's the impact on ASP and the number of transaction per ticket so that you can maintain a relatively stable RMB 39 ticket size. And on top of that, what will be the impact of entry price offering on your GP margin?

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Thank you. Let me reiterate, we have been able to protect ticket size and even grow a little bit over the years. So 2019 pre-pandemic, the ticket average RMB 37, 2020 is RMB 40 and then RMB 39, RMB 42 and then RMB 41 for 2023. So this is the long-term trend. If we even go back even another 5 years, it's not too far away. So this is always our trading strategy to keep the ticket average relatively stable. To go to specifics, the introduction of the entry price product always comes with the new product -- it's a new product and also comes with the introduction of the high-priced product. I mentioned that the beef burger, the beef burger grew by 18% last year, by the way, the category. So RMB 50 for beef burger -- RMB50 for Wagyu beef burger and RMB 20 combo is a good balance. What also helps is when we do promotions like even for Chinese New Year, we always try to help customers to trade up to a higher ticket average by having a very attractive discount. So it's a combination of the marketing campaign that we have been doing to protect ticket average. But specifically for the entry price product, it has 3 purposes, and we are happy to see all 3 purposes there.

One is it does attract incremental customer as we become more and more mass market, particularly for Pizza Hut. By the way, Pizza Hut ticket average moved from RMB 120 to right now RMB 90 over the last 5 years as part of the turnaround strategy, obviously it works, because if we want to open more stores, become more mass market, we need to have product and price point to cater for the incremental customer. And it works. And to what percentage, it's about 5% right now, it's not a huge proportion that will offset the balance of our margin. That's point one.

Point two is, interestingly, when we have the entry price product, does it mean most of the customer will go there? Not necessarily. If you think about customer psyche, many customers will still go for the product above and entry price products to feel good. It feels good to choose something in the middle, not the cheapest one, right? You are the customer yourself, ask yourself, how would you choose?

Third, it really actually improved the price perception by having something very low cost there. I'll give you one example I did 10 years ago with the KFC business. I lowered the small Pepsi coke price in our menu, lowered it because it looks good. It looks very affordable but how many people actually went for it, not that many. But the perception is important. It's almost as important as the reality to a certain extent. So I hope that will give you a sense about how do we treat the entry price product. But certainly, it helps when we go down to Tier 5, Tier 6 cities to introduce our product to certain customers. By the way, it's a fantastic way to recruit young customers such as students as well, particular with amazing products like the Golden SPA chicken burger, it's breast meat. Breast meat in the U.S., you can sell at higher price than dark meat. But in China, it costs us less. So the margin, of course, we protect the margin. The margin is just fine.

Operator

The next question comes from Sijie Lin with CICC.

Sijie Lin ***China International Capital Corporation Limited, Research Division - Analyst***

Joey, Andy, so we have talked a lot about the competition. I want to ask one question about Pizza Hut. So we see that Pizza Hut had quite good performance on margin in Q4, driven partially by the labor productivity gain and lower rider cost. And we also mentioned before that Pizza Hut's margin is still lower than KFC and there is room for improvement. So what else we can do to further reduce cost and improve efficiency?

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you, Sijie. So again, we -- when we look at our cost and the focus, as we have said many times, including what Joey has just earlier mentioned, we generally try to aim for cost of sales to be relatively stable over the long term on a year-over-year basis. And that's because we have a very excellent supply chain team, very disciplined with our pricing. And this also comes from our commitment to continuously innovate and also introduce new products every year. And then -- and also, as we have mentioned many times, we make the best effort to using every part of the chicken or cow so that we can enhance the resource usage, minimize cost. And all these collective efforts have allowed us to provide great value for the money for our consumer while keeping our cost of sales relatively stable. There will be some new quarterly seasonality and fluctuation there. But if you look at our track record, we have been able to keep it around like 31% plus/minus 1% over the past few years, including last year, which was right on the dot 31%.

Now when we look at the overall cost, labor cost, obviously, right now, we're in a soft patch in the economy. So you would be probably more modest in terms of wage increase. But more importantly, over the year, we have utilized digital and automation tool and technology like AI assisted scheduling or inventory that we have mentioned before, to enhance labor productivity and manage cost. We are also with the RGM initiatives, basically, we try to streamline administrative tasks and then like equipment or training, et cetera, to a more centralized process as well as centralize some of the food processing to further improve restaurant labor efficiency. And so obviously, there's some fluctuation, but in the long term, we aim to keep labor costs mostly stable in the long run. Again, the emphasis here is on the long run because in the short term, it's going to be always impacted by the sales leverage.

Now occupancy and others is same for KFC and same for Pizza Hut. It's an area where we will have opportunities. And compared to pre-pandemic, as I mentioned earlier, we improved by almost 350 basis points. Now rent to sales ratio is 1 to 10. We have good long-term contracts. And then we also have optimized our store portfolio. As we expand into lower tier cities, they generally also come with lower rent as we mentioned -- as Joey mentioned the rent in Changsha is a lot lower than the Tier 1 cities for example. And then we also have more flexible formats that are targeting delivery and takeaway that are small and also more cost efficient in terms of rent to sales ratio.

Now depreciating cost is another one. We continue to work on it. You can see every year, our CapEx per store has improved compared to a few years ago, it was around like RMB 2.5 million to today around RMB 1.5 million per new store. So our depreciation costs also improved and marketing leverage, et cetera. So I think for Pizza Hut, obviously, labor is potentially an improvement opportunity there, O&O, definitely. As we have mentioned before, KFC is already running at a very high operating level. So the room for improvement potentially will be in the O&O line.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Let me give an overview and take a step back again. We have been very consistent with the Pizza Hut strategy since 2017 when we embarked on the Pizza turnaround. It's sales first, profit later and then resiliency comes after that. Sales is -- obviously, you remember we work on a product, we work on a marketing campaign, we work on the business model, we work on unit economics of each of the store. Now once we turn around the same-store sales within 18 months after we make that promise, then we really turn the focus to profit because sometimes they do the trade-off, particularly at the very beginning of the turnaround of building a brand. The trade-off is always sales first, profit later. So later on, we work on the cost side, all the details Andy just went through with you, a minute earlier, and we'll continue to do that. And we want a bit more profit, bit by bit on every line. What is after, it's resilience. It's more profit. We are going to open more stores, obviously, across all city tiers to improve -- to utilize the scale of our business to get better rent, to get better cost of sales, et cetera, et cetera.

And then next is resiliency. We want to build a very resilient business, even more resilient than now and as resilient as KFC. Well, it's a very challenging goal, but unfortunately, when you have 2 brothers and of course, 2 brothers compete with each other, it's just normal. So for example, one challenge we give to ourselves, which we got it already, 2023 is we want each quarter to be profitable because Pizza Hut is quite a seasonal business, even more seasonal than KFC.

So you can see that in quarter 4 2023, we remained profitable and it's very important because I just don't like businesses that make -- that make a loss, even though there are big and small quarters. And then, we'll continue to improve the seasonality, and we even continue to improve the resource allocation during the peak hour and the slow hours of the day. And that's how we improve the resilience of the business, not only for the shareholders, but for our employees as well.

Operator

Your next question comes from Kevin Yin with JPMorgan.

He Yin *JPMorgan Chase & Co, Research Division - Head of Greater China Consumer Research*

Thank you, Joey and Andy. My question is on the ASP. Okay. So good to see the ticket size was up from RMB 39 to RMB 42, which is very good. But we'd like to better understand if the fourth quarter '23 is it a bit different versus before. So for example, on a like-for-like basis, KFC average ticket size down what percentage and traffic coming by what percentage points. So just trying to quantify in the fourth quarter, ASP down and the traffic are back, okay?

And secondly, I also like to know your thoughts for 2024, your convection level to maintain flattish same-store sales growth in 2024. And if we're considering the contribution from the G&A cost cutting, et cetera, what's the minimum same-store sales growth level for you to maintain the restaurant margin in 2024?

Ka Wai Yeung *Yum China Holdings, Inc. - CFO*

Okay. Kevin, thank you for your questions. So a little bit clarification on the TA and 4Q difference, right? So for KFC, we have same-store sales growth of about 3%, and the transactions, the TC count increased by 16%. And then the average ticket size was down 11%. For Pizza Hut, the same-store sales growth was about 6%. And then the traffic growth was 15%, and then average ticket change was about 8%. So -- but as I mentioned before, the TA trend -- the average ticket trend is pretty consistent with our overall strategy and it's important to our market reach.

And as Joey mentioned, the strategy approach is to expand our store footprint, especially in the small cities expanding our pricing point, and then offer consumers more product options to drive incremental traffic and sales. So there's significant growth that we have observed both in transactions, and overall system sales growth, as I remind everyone, for both KFC and Pizza Hut system sales grew more than 20% and on both -- in the fourth quarter, but also for the full year. So obviously, if you look at the sales number, our strategy, it's working effectively.

Now when we look at the ticket average changes on a year-over-year basis, it's worth noting that 2023, obviously, was the first year of reopening. So this is an important context to keep in mind when we look at the TA movement. And as we have mentioned before, KFC, we're seeing very robust ticket average in the fourth quarter, RMB 39, which is consistent with the third quarter and is above what we have seen in the pre-pandemic.

In fact, ticket average, as we have mentioned earlier, have been pretty consistent over the past 5 years. Obviously, with the recovery of dine-in sales was strong this year, coupled with strong performance in our breakfast and coffee sales has contributed to the year-over-year movement of the average ticket size for KFC. It's also consistent with our approach to expand the pricing range and our product options that, again, effectively drove very robust traffic growth.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Let me just add a little bit here about the quarter 4 ticket average and then Andy can wrap up this question. Kevin, the ticket average for quarter 4 is not very unusual. As Andy just pointed out, 2022 is the unusual year because it was still in lockdown, it's RMB 42. That's very high. If we go back to 2021, quarter 4, it's RMB 38. The 2023 quarter 4 is RMB 39, but 2021 quarter 4 is RMB 38. 2020, quarter 4 is RMB 38. 2019, which is one of our best years, the ticket average for quarter 4 is RMB 37. So it's not that different.

I mean the overall feeling is -- the market is getting more promotional, et cetera, et cetera. But as I went through in great detail that we are the market leader, and when we deal with challenges, which are not new to us, by the way. We always have a combination of good promotion, good product, good mechanism to protect the TA, et cetera, et cetera. Therefore, we are able to maintain the TA even during the quarter 4 across multiple years.

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you, Joey. Like -- again, like it's very important to keep that context in mind because as you remember, it seems like a long time ago, but it was only fourth quarter 2022 that we have this reopening --a big surge in infection. At that time, we also experienced some labor shortage because of infection rise. So -- and then the ticket, I think the delivery mix at that time was 45%, which was very high. And so, those are the contexts for that.

And then turning to Pizza Hut, right? If you look at Pizza Hut, it's a very consistent strategy for us since 2017 with the turnaround strategy, which is to, as Joey mentioned earlier, drive customer traffic, first, then sales and then finally, enhancing profitability. So we have successfully met those 3 goals if you look at our results. Moreover, this approach is very much in line with our latest strategy, which is aimed to reach underserved customer segments by expanding our price range, especially for pizza that is less than RMB 50 subcategory. And we also want to offer more options for consumers that are suitable for smaller size of individual dine-in. So thank you. Thank you, Kevin.

Operator

Your next question comes from Chen Luo with Bank of America.

Chen Luo ***BofA Securities, Research Division - MD***

Thank you, Joey and Andy, and sorry, actually, my line got disconnected just now, although I actually dialed-in to the call at 6:30 a.m. in the morning. So forgive me if I ask some questions that have already been asked previously. So basically, it's actually on margins. So I noticed that our restaurant margins for 2023 actually has already recovered to a level even slightly higher than 2019, so making it the third highest margin since our spin-off. But compared with 5 years ago, our margin structure has significantly changed.

So our labor cost, as a percentage of revenue has risen significantly, but our occupancy and others have reduced significantly. So going forward, do we think that there is room for us to maintain a largely stable labor to sales ratio, especially given that recently, our channel check suggests we have taken a lot of measures to control the rider cost, such as the introduction of Meituan and Eleme, as our future vendors, as well as our continued rollout of the RGM Mega program. So do you think there is room for us to see a largely stable labor cost, as opposed to the rising labor cost trend in the past few years.

And meanwhile, I noticed that our food and paper cost as a percentage of revenue has risen by 50 bps -- 80 bps for KFC and 30 bps for the whole group, given a very promotional environment. Do you think it's going to be a new normal for the entire year of 2024?

And lastly, just now I heard about the guidance for largely flattish OP for the full year, excluding FX and one-off items. But then if you look at the reported level, I remember, last year, we booked a one-off gain of $27 million in our OP. That may actually lead to a mid-single-digit impact. And then given the FX, there's another 5% impact. So is it fair to say that on a reported level, actually, the OP may possibly decline by around 10%-ish. Of course, I think this is -- this should be the worst case. But hopefully, if everything is going in the right direction, the actual decline could be better than that. So these are all my questions.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Thank you, Luo Chen. Let me actually answer one question that the Kevin, and other -- and Brian asked earlier, and then I'll come to your question. It's about the same-store sales growth. Let me just point out that [over 40%] (corrected by company after the call) of our store in our portfolio right now -- portfolio right now are built after 2019. So there's a reason why we really -- we'll continue to drive the same-store sales, but the system sales growth is incredibly important for our business.

And then, we come to the cost side, mainly the labor cost and O&O, the labor cost -- let's talk about O&O first. We have been operating with the guiding principle that we always are sincere about getting the best food to our customers, pass all the savings -- pass a lot of savings to our customers. So if you look at our cost of sales over the last few years, it has been very stable, very, very stable through better time or a more challenging time.

So if I start with 2019, pre-pandemic again or even -- well, 2019 pre-pandemic throughout the time, 2019, 31.3%, 2020, 31.7%, 2021, 31.4%, 2022, 31.1%, 2023, 31%. It's really like less than 1% swing around 31% is always there because whenever we have savings, we pass the savings to the customer through food. So you can be assured that we'll continue to stay around 31% about the cost of sales because if my team goes significantly below that number, they will have a very hard time from myself, and they all know that.

Second is cost of labor. Cost of labor, even in a year like this year, yes, it has increased because there are a lot of sort of the insurance and et cetera, et cetera, all these costs are going up. And labor cost is always sort of going up. I spent 10 years in the U.K. even when the GDP was going south during the 5-years out of 10 years, I was there, labor cost was still going up. So we have to every year find ways to help our staff to become more productive, which we have been doing that, and going forward, you can see we even go as far as one store manager managing multiple stores. It has gone up a few points, 2019 is 22.8% and then go up to 23%, 25%, 26%, now is staying at 26% last 2 years.

And the way that we run this business, we generate savings from O&O, from rent, from depreciation, from everything that we could save, and then pass the savings to our staff, we pay them a fair pay, and we hopefully pay them well. We give them really good health insurance, et cetera, et cetera, because we want to have the best staff to provide the best service for our customers. So that will be the direction we'll continue to drive.

In terms of OP, as a result of foreign exchange, et cetera, I'm sorry, cannot forecast that. It's beyond our company's capability. So we'll do everything we could to generate sales and to manage costs and then produce the result, as a result of our good effort. Thank you, Luo Chen.

Operator

Thank you. That is all the time we have for questions today. I'll now hand back to Ms. Shen for closing remarks.

Michelle Shen ***Yum China Holdings, Inc. - Director of IR***

Thank you, Ashley, and thank you, everyone, for joining the call today. For further questions, please reach out through the contact information in our earnings release in our website. Have a great day.

Ka Wai Yeung ***Yum China Holdings, Inc. - CFO***

Thank you. Bye-bye.

Joey Wat ***Yum China Holdings, Inc. - CEO & Executive Director***

Thank you.

Operator

That does conclude our conference for today. Thank you for participating. You may now disconnect.