Yum! Brands, Inc. (YUM) Q1 2024 Earnings Call Transcript

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Q1: 2024-05-01 Earnings Summary

EPS of $1.15 misses by $0.05 | Revenue of $1.60B (-2.86% Y/Y) misses by $112.29M

Yum! Brands, Inc. (NYSE:YUM) Q1 2024 Earnings Conference Call May 1, 2024 8:15 AM ET

Company Participants

Matt Morris - Head, Investor Relations
David Gibbs - Chief Executive Officer
Chris Turner - Chief Financial Officer
Dave Russell - Senior Vice President and Corporate Controller

Conference Call Participants

Jon Tower - Citigroup
Brian Bittner - Oppenheimer & Co
David Palmer - Evercore ISI
John Ivankoe - JPMorgan
Brian Harbour - Morgan Stanley
Dennis Geiger - UBS
Sara Senatore - Bank of America
David Tarantino - Baird

Operator

Hello, everyone and welcome to the Yum! Brands, Inc. 2024 First Quarter Earnings Call. My name is Nadia and I will be coordinating the call today. [Operator Instructions] I will now hand over to your host, Matt Morris, Head of Investor Relations to begin. Matt, please go ahead.

Matt Morris

Thanks, operator. Good morning, everyone and thank you for joining us. On our call today are David Gibbs, our CEO; Chris Turner, our CFO; and Dave Russell, our Senior Vice President and Corporate Controller. Following remarks, we will open the call to questions.

Before we get started, please note that this call includes forward-looking statements that are subject to future events and uncertainties that could cause our actual results to differ materially from these statements. All forward-looking statements are made only as of the date of this call and should be considered in conjunction with the cautionary statements in our earnings release and the risk factors included in our filings with the SEC. In addition, please refer to our earnings release and the relevant sections of our filings with the SEC to find disclosures, definitions and reconciliations of non-GAAP financial measures and other metrics used on today's call.

Please note that during today's call, all system sales growth and operating profit growth results exclude the impact of foreign currency. On our last earnings call, we announced that we signed an agreement to acquire 218 KFC franchise restaurants in UK and Ireland. The transaction closed on April 29. As a reminder, several of Yum! Brands business units, report on a period calendar basis, including all U.S. and Canada brands, KFC UK and KFC Australia. For business units that report on a period basis, first quarter same-store sales growth excludes the benefit from the additional day of sales owing to Leap Day. When forecasting 2024, please keep in mind this year will include an extra week in the fourth quarter for those entities. For more information on our reporting calendar for each market, please visit the Financial Reports section of the IR website.

We are broadcasting this conference call via our website. This call is also being recorded and will be available for playback. We would like to make you aware of upcoming Yum! investor events and the following. Our second quarter earnings will be released on August 6 with the conference call on the same day. Finally, please mark your calendars for an in-person Taco Bell Consumer Day on December 10 at the Taco Bell headquarters in Irvine, California. Stay tuned for more details and invitations to follow.

Now, I'd like to turn the call over to David Gibbs.

David Gibbs

Thank you, Matt and good morning everyone. I am pleased to report that Yum! grew core operating profit 6% this quarter despite a challenging operating environment, demonstrating the resilience of our business. As we communicated last earnings, 1Q should represent our most challenging sales quarter this year as we work through tough year ago lapse returned to a more normal inflationary environment and navigated discrete consumer demand pressures. While the impacts from the Middle East conflict have been scattered and difficult to measure, we have begun to see improvement in the most impacted markets.

Taco Bell U.S. outperformed the industry on same-store sales and delivered industry-leading margins, while 1Q unit openings at KFC International set us up for a strong unit growth story in 2024. We continued to make significant progress scaling our proprietary digital and AI-powered platforms and are excited by plans to accelerate deployment. Digital sales continued an upward trajectory approaching $8 billion and were up 11% year-over-year. Through continued kiosk deployment, greater adoption of click-and-collect and stable third-party aggregator sales, digital mix improved 5 points and for the first time ever, represented over 50% of system sales in Q1. We now have $30 billion in annualized digital sales, which by itself would represent one of the largest restaurant companies in the world. Overall, despite a more challenged operating environment, we have reached impressive new milestones and remain on track to deliver on our long-term growth algorithm target of at least 8% core operating profit growth for the full year.

Now I'll discuss our Relevant, Easy and Distinctive brands, or R.E.D. for short, followed by our Unrivaled Culture and Talent and Good Growth strategy. Chris will then provide an update on our first quarter results, followed by our bold restaurant development, unmatched operating capabilities and balance sheet position.

Starting with the KFC division, which accounts for 51% of our divisional operating profit. KFC grew system sales 4% this quarter, owing to an 8% unit growth and a 2% decline in same-store sales. The same-store sales pressure was partially attributable to impacts from the conflict in the Middle East, which have begun to ease and we expect a 2-year trend for KFC International overall to accelerate in the same quarter. We saw strong top line growth in other parts of the world, including Latin America, Africa and Greater Asia. System sales in Latin America grew 22% on the heels of a strong marketing calendar and continued success of the KFC original nuggets.

In Africa, system sales grew 11%, thanks to 5% same-store sales growth driven by product innovation and 6% net new unit growth. In Greater Asia where system sales grew 8%, we recently partnered with a new franchisee in Korea, who is driving transaction growth with a calendar focused on core, value and expanding consumer access, which resulted in a 26% growth in same-store sales. At KFC U.S., same-store sales were pressured from unfavorable weather events and chicken value promotions from QSR competitors.

Moving on to the Taco Bell division, which represents 35% of our divisional operating profit and 75% of our U.S. divisional operating profit. System sales at Taco Bell U.S. grew 4%, led by 2% same-store sales growth and a strong outcome on top of last year's 9% same-store sales growth. Sales improved throughout the quarter after difficult weather events in January. Taco Bell focused on key levers within its magic formula to drive growth, including building brand buzz, providing value to our consumers and expanding into new category entry points. We know that when we execute on this magic formula, Taco Bell puts itself at the center of the cultural conversation. There was no better example of this than the Live Más LIVE event Taco Bell held in Las Vegas to share its upcoming innovation calendar, an industry-first event. Of course, it was not surprising that Fast Company named Taco Bell the Most Innovative Company in Dining and #8 overall.

Early in the quarter, the team launched a new cravings value menu and ended the quarter with a successful launch of the Chicken Cantina menu. The cravings value menu features industry-leading value with 10 items priced under $3 providing consumers with craveable everyday value offering. Nearly one-third of transactions contain an item off the cravings value menu, and when purchased, 80% have at least one other item added, translating to a nearly 10% check uplift compared to non-cravings value menu checks. The impressive performance of such product launches is compounded by Taco Bell's ability to deliver industry leading margins on top of a great consumer experience.

At Taco Bell International, system sales grew 6% this quarter. The team is focused on building brand and category awareness globally. This included markets such as Canada and Latin America, where the team elevated the core menu and launched the Chicken Cantina menu to expand their consumer base.

Next, at the Pizza Hut division, which comprises 15% of our divisional operating profit. During the first quarter, system sales declined 4% with 5% unit growth and a 7% decline in same-store sales. The year-over-year growth rate in same-store sales was suppressed from difficult year ago lapse and the ongoing impact from the conflict in the Middle East. The team continued to focus on the individual meal occasion this quarter with the India market launching the Melts platform. At Pizza Hut U.S., same-store sales declined 6% as we lapped the launch of Melts and Big New Yorker Pizza. However, the 2-year trend was positive and improved from last quarter. Lastly, at The Habit Burger Grill, for the first quarter, system sales declined 2% with 6% unit growth. Margin trends improved throughout the quarter with a combination of initiatives leading to a 60 basis point improvement in store level margins year-over-year.

Now, I will turn to our Good Growth strategy, starting with our people pillar. Effective June 1, Alex Barsk will join KFC Global as the new Chief Financial Officer. Alex is joining from Pizza Hut, where she most recently served as Global CFO. Alex joined Pizza Hut in 2015 and has held several leadership roles across strategy, finance, development and supply chain. Alex's transition is another great example of Yum! leveraging its talent across brands to help share unique learnings and experiences.

To round out our people pillar, I'd like to congratulate and thank Yum!'s Senior Vice President of Finance, Corporate Controller and my friend, Dave Russell, who recently celebrated his 25th anniversary at Yum! with today marking his 100th quarterly earnings announcement. Dave has been with the company since 1999, always serving as a trusted leader who brings his deep knowledge and analytical perspective to our finance and accounting function. Thank you, Dave, for your dedication to our growth over the last 25 years and I look forward to your continued partnership in the future.

Before I hand it over to Chris, I would like to share a few thoughts on the future of our digital and technology strategy given we achieved an important milestone this quarter with more than half of our sales coming from digital. You will recall that the first phase of our journey to become the leading global digital restaurant company began in earnest in 2019. That first phase focused on building or acquiring a comprehensive suite of owned platforms, spanning Easy Experiences, Easy Operations and Easy Insights and accelerating deployment of those platforms across our brands and markets. While we still have further to go in deploying these platforms, we have achieved critical mass in several areas.

Taco Bell U.S., one of our twin growth engines, has achieved the most extensive deployment of key platforms, including the Poseidon POS system, the Yum! e-commerce platform and the AIM inventory management platform. Our other primary growth engine, KFC International, has been accelerating the rollout of those same platforms and is our leader in deploying in-store kiosk technology. Pizza Hut, of course, has been our leader in deploying Dragontail to thousands of restaurants around the globe. Behind the scenes, our global data hub houses data generated from these platforms. The deployment of our capabilities in this first phase of our journey has driven the dramatic increase in our digital sales from approximately 20% in 2019 to over 50% now. The impact of this growth has been significant.

To share just a couple of examples of impact, our consumers enjoy more convenient and frictionless experiences, leading to high frequency and check sizes. Our franchisees enjoy significant productivity benefits as their team members no longer spend time taking orders and payments for half of all transactions, leading to stronger unit economics. We believe we are still only scratching the surface of the full value creation potential of our capabilities.

While the first phase of work in deploying our platforms will continue, given the critical mass we have achieved, we have initiated a second parallel phase in our technology journey. This second phase will focus on maximizing the value creation potential of our platforms through the acceleration of AI capabilities in combination with fully leveraging the immense data assets we now own. With our platform-driven approach, we can now more easily integrate AI capabilities across our digital ecosystem. We currently have more than 40 AI initiatives in progress across the company spanning marketing, operations, insights, engineering and our internal back-office functions.

While many of these initiatives will remain confidential for now, one example that we have shared publicly is Voice AI to enhance our consumer experience. We have been testing this capability at the drive-thru in 5 Taco Bell stores in California. We are expanding that test to 30 stores in Q2 based on positive consumer feedback. Another example is our piloting of AI-powered technology in our SuperApp restaurant general manager support tool, making it even easier and faster for managers to access critical operational information to make better decisions. Of course, our Dragontail platform was the first AI-enabled next-gen restaurant operational system to enhance the consumer and team member experience in a multi-channel fulfillment environment.

As an example of how we are elevating the use of our data assets, in Q1, we launched the R.E.D. 360 U.S. Consumer Data Insights system. As of Q1, both Pizza Hut U.S. and Taco Bell U.S. have integrated into the system and KFC U.S. will integrate in the second quarter. This system allows us to leverage insights into consumer behavior across our brands in the U.S. After full deployment, R.E.D. 360 will be the first scaled cross-brand U.S. restaurant consumer data engine in the quick service industry and will pave the way for unique insights and personalization opportunities on digital and social channels. For those who may have missed it Joe Park, our Chief Digital and Technology Officer, was recently interviewed in The Wall Street Journal, bringing to life many of these plans as we become more focused on pursuing AI and data-driven innovation. As we do all of this, we are also continually innovating how our technology teams work internally to better leverage our scale so that we can continue to bend the curve on the net investment impact of these digital and technology initiatives.

To sum it up, we are excited about having ramped up this second phase in our journey and are doubling down and pursuing the ultimate goal of our digital and technology strategy, which is to better serve our franchisees, providing them with more, better, faster, cheaper and safer technology while simultaneously delighting consumers and maximizing Yum! shareholders' returns. We will continue to provide updates on both phases of our journey on future calls, organized around our easy capability framework.

In closing, as I look back over the quarter, I am proud of our teams and their ability to navigate any environment as our brands stand for unmatched value and convenience, providing a range of products and price points to meet any consumers' needs. Our resilient business model, coupled with our strategy to leverage our technology platforms on a global scale, gives me confidence we will continue to improve both franchisee and Yum! economics. Looking ahead, our initiatives to become an even more nimble and data-driven organization are underway and I am excited for the shareholder value we will create.

With that, Chris, over to you.

Chris Turner

Thank you, David and good morning everyone. Today, I'll discuss our financial results, our bold restaurant development and unmatched operating capability growth drivers, followed by an update on our balance sheet and capital strategy.

Starting with our results. First quarter system sales grew by 2% driven by 6% unit growth. As we communicated on our last call, we expected the first quarter to be our most challenged from a same-store sales perspective due to prior year lapse, a return to a more normal inflationary environment and discrete consumer demand pressures, including markets impacted by the Middle East conflict. We believe the markets most impacted by the conflict collectively created a low single-digit headwind on Yum!'s overall Q1 same-store sales. Despite these challenges, I'm pleased to report Yum! delivered 6% core operating profit growth exceeding our internal plan and demonstrating the resilience of our profit model.

First quarter ex special general and administrative expenses were $265 million, down 4% year-over-year, a continuation of the G&A momentum we had in the fourth quarter. Reported G&A was $286 million and includes $21 million in special expense related to ongoing resource optimization, which we expect to generate additional savings in the second half. Reported operating profit included a 2-point impact in the quarter from foreign currency translation. First quarter ex-special EPS was $1.15, which includes negative after-tax impacts of $0.08 from investment losses and $0.03 from foreign currency translation.

As a reminder, we shared on our last call the intent to purchase 218 KFC UK and Ireland stores. We're excited to report we officially closed this acquisition at the end of April. These stores have average unit volumes above $2 million and healthy store level cash margins. We expect the addition of these units to provide approximately $40 million of incremental EBITDA in the 12 months after acquisition while the benefit to our operating profit will be largely offset over the next several years due to depreciation and amortization, including amortization of reacquired franchisees.

Now let me share greater detail on our first quarter unit growth in the context of our Bold Restaurant Development growth driver. Yum! opened over 800 units in the first quarter. We reached the incredible milestone of opening KFC's 30,000 restaurant globally. As the number one brand on Entrepreneur Magazine's Top Global Franchise rankings, KFC continues to demonstrate strong desirability among global franchisees with a new store opening every 3 hours. We continue to see an incremental store opportunity of 50,000 KFCs over the long-term. Across the global system, the outlook for development in 2024 is strong. We expect to continue to open units in a broad range of markets, which last year included over 100 markets, and to cross the 60,000 unit milestone. Further solidifying Yum!'s position as the world's leading multi-brand restaurant franchisor.

There are several reasons we remain confident in these trends. First, we entered 2024 with broad-based development momentum. In Q1, we grew units across 81 brand-country combinations. Second, we have large, committed franchisees who have entered into more unit development commitments for 2024 than in each of the prior 2 years. Approximately 80% of 2024 exceeded new builds for KFC outside of China are part of development commitments. Third, the development white space remains massive. We have just 6% of the global QSR market. China is a prolific developer and serves only one-third of the China population. In India, which is the fastest-growing global economy, KFC and Pizza Hut have been the fastest and third fastest-growing QSR chains, respectively, since 2019.

Finally, our brands unit economics remain attractive across key markets where scale and first-mover advantages put our franchisees in a position of strength. Scale leads to unique advantages including access to alternative financing solutions, dedicated development teams and in-depth market knowledge. Scale also offers operating advantages. For instance, our largest partner, Yum China, has AI-enabled digital tools to allow its restaurant general managers to oversee multiple restaurants, creating unmatched savings that can be passed to consumers.

The Serrano Group based in Latin America and Ramcar based in the Philippines run their own poultry processing facilities in addition to distribution capabilities, giving them cost and reliability advantages. At a brand level, KFC has food innovation kitchens in Canada, the U.S., Latin America and the Caribbean, United Kingdom, Thailand, Australia, South Africa, India and Singapore. Perhaps underappreciated, our global innovation capabilities are real sources of differentiation.

Moving now to the digital and technology front. Recall that our vision is to empower our franchisees with leading-edge technology solutions with advantaged economics. As David put it, we want to deliver more, better, faster, cheaper and safer technology to our franchise partners. We are advantaged by owning important foundational platforms such as our Poseidon POS system, Yum! e-commerce, Dragontail, SuperApp and our global data hub, and the impact of these platforms will grow exponentially as we deploy more of them to more stores. Data is becoming a crucial differentiator, enabling us and our franchisees to generate better insights and make better decisions.

On this front, quick service restaurants will benefit disproportionately because of the high frequency nature of our consumer visits, which results in more data. Within quick service, a few characteristics will separate us from our competitors, including our multi-brand portfolio, our scale and global footprint, our ownership of key platforms and the increasing integration between our platforms. We will leverage our data for insights and to drive more effective marketing and loyalty engagement, and we will deploy advanced AI tools to all aspects of our business. As we leverage our scale more and more in these areas, we can be faster, cheaper and safer through consistency and standardization across our environment.

Let me now discuss the digital and technology accomplishments for Q1 across our Easy Experiences, Easy Operations and Easy Insights pillars. Beginning with our Easy Experiences pillar. We continued to onboard Pizza Hut U.S. to the Yum! e-commerce platform with a full cutover planned by Q3, followed by three Pizza Hut international markets by year-end. For Taco Bell U.S., where the Yum! Commerce platform is fully operational, we have accelerated viral promotions and have seen Taco Bell's digital ordering capacity increase tenfold relative to the legacy system.

Within Easy Operations, the expansion of our world-class technology products and platforms continued. We expanded Poseidon to 1,800 Taco Bell U.S. restaurants, bringing our total to over 7,000 restaurants. We onboarded over 500 Pizza Hut restaurants onto the Dragontail AI platform, bringing our system total to over 7,000 restaurants. In the near future, we plan to nationally roll out Dragontail's kitchen display system and Poseidon to our KFC U.S. restaurants. Finally, our custom-built SuperApp, which provides smart, automated routine management tools for our restaurant managers, is now used in nearly 9,500 Pizza Hut and KFC restaurants with significant expansion plans underway for KFC.

For the third pillar of our Easy strategy, Easy Insights, KFC and Pizza Hut have continued to scale a new experienced management program allowing the brands to draw insights from an expanded source of consumer reviews across digital channels, including third-party aggregators and social media in addition to guest survey responses. KFC is now live in 10,000 restaurants and has seen a fivefold increase in per-store data point. Pizza Hut expanded this service to 7,000 restaurants across more than 50 countries. Talking about all of the tremendous advancements underway excites me about the future. This work will be vital as we embark on further innovation behind voice AI, restaurant automation and better leveraging our loyalty programs.

Next, I'll provide an update on our balance sheet and liquidity position. Net capital expenditures for the quarter were $38 million, reflecting $49 million in gross CapEx and $11 million in refranchising proceeds. Our net leverage ratio ended the quarter at 4.1x. In the quarter, we sold our minority investment in Devyani for $104 million, representing a $73 million increase in value since acquisition. Our cash balance ended at $652 million, reflecting proceeds from the Devyani investment sale and modest accumulation in cash to finance the KFC UK acquisition.

With the KFC UK deal behind us, our cash balance will return to a normalized rate of around $400 million, excluding the unrepatriated Devyani proceeds. Thereafter, with no significant debt maturities in 2024 or 2025, we plan to use our excess free cash flow primarily to fund share repurchases, absent accretive investments we choose to make. I will reiterate that our capital priorities are guided by maximizing shareholder value. This includes investing in the business, maintaining a resilient balance sheet, offering a competitive dividend and returning excess cash to our shareholders. Subsequent to the quarter end, we renewed our pro rata credit facility, including our revolving credit facility and Term Loan A. We were pleased to renew the $2 billion facility with the same pricing and terms that we achieved in 2021 while also increasing the revolver from $1.25 billion to $1.5 billion.

Now let me discuss our latest outlook on full year 2024. We are confident that 2024 will showcase a strong unit development story at or above 5% unit growth, led by KFC International as franchisees capitalize on our brand's attractive paybacks. In the U.S., Taco Bell continues to balance core everyday value to cater to a more discerning consumer across income groups with premium innovation to attract new consumers. We expect full year Taco Bell company-operated margins to be in the range of 23% to 24%. Excluding the 53rd week, we now expect ex special G&A to be flat to down slightly for the year, including incremental G&A associated with the KFC UK acquisition. Finally, we are confident we will deliver at least 8% core operating profit growth excluding the benefit of the 53rd week.

To close, I am incredibly proud of the progress we have made over the last few years in the areas to which we dedicated our focus and internal resources. Our team continues to manage through industry challenges to position us for a strong year and deliver our long-term operating profit plan, reinforcing the resilience of our business, strength of our talent and commitment to our shareholders. Going forward, we are moving to solidify ourselves as the multi-brand franchisor of choice through a more efficient adaptable, data-driven organization. We are only in the early innings of unlocking the value of our unmatched data, which will help power our aspirations and deliver sustained above-market shareholder returns.

With that, operator, we are ready to take any questions.

Question-and-Answer Session

Operator

Thank you. [Operator Instructions] Our first question goes to Jon Tower of Citigroup. Jon, please go ahead, you line is open.

Jon Tower

Great. Thanks for taking the questions. Encouraging to see the G&A curve bending. I was hoping you could maybe drill into some of the puts and takes there. Obviously, there were some offsets this quarter with some charges. But curious if you could give us a little bit of context around what's flowing through that line to help move it lower and maybe where you anticipate this moving over the long-term for the business. I think historically you've talked about the idea of potentially reaching – or at one point in time, having that sit at about 1.7% system-wide sales. Is that still a target that you think is reasonable? Or do you feel like you can even move that further as we continue to grow this digital business over time?

Chris Turner

Yes. Thanks, Jon. Good question. First, let me just reiterate a couple of details on the G&A guidance. So we expect that ex special G&A on a 52-week basis will be flat to slightly down. As we mentioned on the last call, that assumes a target level of incentive compensation. So that's one factor that could move as we go through the year. But on the factors and levers that help us to achieve that plan first, there are some one-time factors at play. Examples of that include lapping the cyber event last year, a couple of small remnants of the Russia overlap and some lapse of incentive-based compensation last year. Now on the other side, we do have some expenses related to the acquisition of the stores in the UK. We expect that will add just under $10 million to our G&A in year. But those are the set of factors.

If we go to the longer-term levers that we're pulling, we continue to drive our resource optimization program, which has allowed us to find efficiencies in legacy parts of the business, part of which we've used to fund investments in the D&T strategy. You saw some special charges this quarter which included the impact of some of those moves that we make, but that helps to drive productivity in the business going forward. And finally, as you say, we continue to bend the curve on the impact of our D&T investments on the P&L. This happens as we deploy more and more of our technology through increased franchisee adoption. And of course, we're continuing to better leverage our scale and how we operate internally in digital and technology, which is allowing us to do more together across the business. All of that is in service, delivering more, better, faster, cheaper and safer technology to our business, as David said earlier, but bending that curve is a part of the long-term plan.

Operator

Great. Thank you. The next question goes to Brian Bittner of Oppenheimer & Co. Brian, please go ahead. Your line is open.

Brian Bittner

Thank you. Good morning. You reiterated your 2024 target to grow core operating profit in-line with your long-term algorithm of at least 8%. And that's impressive given the first quarter where comps were negative and core operating profit growth was below the full year outlook. And I'm assuming this was always built in the plan because of the tough comparisons, and I realize you have a lot of G&A flexibility to hit your operating profit targets. But the question is what's the global same-store sales base case that you're thinking is required for the rest of the year to comfortably reach your operating profit goals.

David Gibbs

Appreciate the question, Brian, and I agree. Hitting 8% in this choppy environment, we're proud of our ability to expect that kind of a result. And I think it speaks to the resilience of our business model and the competence of our leaders. As you know, we don't provide quarter-to-quarter same-store sales guidance, particularly in an environment like this. We're preparing for various scenarios to get to the 8% number. Obviously, one of the lever – one of the strong levers we have to pull to get to the number is on the development front. And we feel really good about the pipeline that we have in place in development from our partners around the world, and that's something much more so than same-store sales because we can count on to get to the 8%. But as far as forecasting same-store sales growth in this environment, obviously it's very difficult given the impact that we're seeing.

Operator

Thank you. The next question goes to David Palmer of Evercore ISI. David, please go ahead. Your line is open.

David Palmer

Thanks. I was just hoping to get some more color on international, KFC International Pizza Hut International. What were some of the highlights and lowlights on same-store sales trends in terms of your brand geography combinations? And more importantly, I'm curious about your reality for 2024 given the exit rates of brand geography combinations. Has any of these changed for the better or worse? How are you feeling about things versus perhaps just a few months ago? Thanks.

David Gibbs

Thanks, David. Yes. Look, we feel great about our twin engines of growth, right? 80% of our profit comes from Taco Bell U.S. and KFC International. In the international business, to your question, 85% of our profit from KFC International and if you look at the areas of the world that are less impacted by the Middle East, like Africa, for example, our system sales, you will see in our release, was up 22%. Latin America, less impacted, really no impact, up 11% – I am sorry, Latin America, up 22%, Africa, up 11%. I recently actually made a trip to Africa this quarter with our team and was just blown away by the progress we are making on the ground there, where we are the leader in the industry, and we are widening our margin in terms of that leadership. Whether it’s South Africa which we visited or Kenya where we have got franchisees that used to be a part of our – the company’s system, who is building our brand the right way there, launching breakfast, the employer of choice in the country, leveraging menu innovation to take and actually inspiring some of our innovation around the world. So, if you look at places like that, the business is real healthy and doing well. The other – the impacted parts of the world are obviously much more challenged. But we still see impressive results for KFC International growing system sales 6% in this environment. And if you adjust for Middle East, that’s 8%, 9% kind of system sales growth. And very importantly, we highlighted this in the earnings release, KFC International with net new unit growth, up 10% shows the strength of – the quality of the development pipeline that we have, which obviously bodes well for the future of the brand. But as far as the international consumer goes, it’s probably more of an emphasis on value than there has been in past quarters. We are seeing the same thing in the U.S. That’s one that we know with KFC, we are well equipped to navigate.

Operator

Thank you. The next question goes to John Ivankoe of JPMorgan. John, please go ahead. Your line is open.

John Ivankoe

Yes. Hi. Thank you. I was hoping to get maybe just a little bit more color on bending the curve on digital and technology spend, especially how it might influence ‘25 and ‘26 type of total G&A growth. I mean I think this has been one of the more kind of debated topics of this on the Street as, are we just talking about a lower rate of growth, or might we actually see declines in dollars in ‘25 and ‘26 as you leverage the platform? And the follow-up to this, and I think it’s very related, acquiring technology, building technology is one thing. But of course, maintaining technology with best-of-class technology talent, especially kind of at the leadership end, might be something different. So, I just wanted to get your thoughts in terms of acquiring some of this tech talent and Yum!’s ability to both attract and retain this talent going forward as they may have other projects to work on in the future. Thank you.

Chris Turner

Yes. Thanks John. Look, if you go back over the last few years, we saw the importance of digital and technology to Yum!’s future and we invested ahead on behalf of the system to build those capabilities and put them in place across easy experiences, easy operations and easy insights. We thought that was the right thing to do for the business, and it did create some pressure on the G&A line as we did it. As we deploy our platforms to more and more markets and we get increased adoption, of course, that happens when our franchisees see the business cases coming to life and the improvements in their economics and the way the technology impacts their consumers and their team members. And we are – as we shared on the call, continuing to drive those deployments. In fact, we are now starting to bundle some of those deployments. At Taco Bell, for instance, we are driving both the AIM inventory management in addition to the Trax back-of-house system at KFC U.S. We will be deploying the Dragontail kitchen display system along with the Poseidon POS system. So, we are bundling those together. And as we create more and more examples and proof points of the impact, as we talk to franchisees in additional markets, it becomes easier to prove the business case that our technology is delivering. So, that’s what supports the long-term deployment path as we move forward. Obviously, we have to continue to make investments in things like AI, better leveraging our data, as David mentioned, and as you said, in continuing to enhance the existing platforms that we have. But as we bend the curve, that reduces the net P&L impact over time. And so in the long run, we expect us to get increasing leverage on our G&A and the G&A as a percent of system sales should come down over the long-term.

Operator

Thank you. The next question goes to Brian Harbour of Morgan Stanley. Brian, please go ahead. Your line is open.

Brian Harbour

Yes. Thank you. Good morning. Maybe just following up on that, you spent a lot of time discussing all of these tech initiatives. I think it's probably a little bit harder for us to sort of observe that in terms of comp impact, margin impact. Obviously, we don't kind of see franchisee profitability. But are there any examples you can give of, for example, e-commerce was deployed in certain restaurants and you saw a certain uplift in sales or franchisee profits, what happens to those when you deploy that tech bundle that you just mentioned? I think that would just sort of bring it to life more for us.

Chris Turner

Yes. Great question. Look, in all of these deployments, this is us partnering with our franchisees, and of course, they co-invest to bring these platforms to their businesses and they only do that when they see a strong business case. So, if you take Taco Bell U.S., which is the one market where we deploy the most of our platforms in combination, I think the tremendous sales results there as they have gone from essentially no digital sales in 2018 to well into the 30% mix now demonstrates the power of the combination of those platforms. In every market around the globe, as we shift sales from non-digital to digital channels, we see increases in check size, we see increases in frequency. Now, as you said, you don't see all of our franchisees' P&Ls, but on the productivity side for our franchisees, I think our development momentum is the best proof point that digital is adding to unit economics. That's the driver of us continuing to set records on unit development around the globe, and the digital and technology impacts on their P&L is an important part of that. So, all of that is enhancing the business model. But as we said, we think we are just getting started on the value creation potential from these platforms and capabilities.

David Gibbs

Yes. And just to get in, if you are looking for specifics, as you can imagine, when we move people to digital ordering, we see an uplift in check in almost every case, whether it's kiosk or online. When we move people to things like Dragontail, we know we get a form – for Pizza Hut, we know we get a four-minute savings on delivery time of pizzas and we know we can get drivers up to deliver more orders per hour by using it. So, the method – to the point of your question, the measures and the financial results from the rollout of these things, there are use cases all over the place for how this improves unit economics for franchisees, which ultimately is the heart of our business. The better their unit economics are, the more they build, the more they can afford to offer the right prices and value to customers and so on.

Operator

Thank you. The next question goes to Dennis Geiger of UBS. Dennis, please go ahead. Your line is open.

Dennis Geiger

Great. Thank you. Specific to the U.S., I am wondering if you could speak a bit more to how you think about the trajectory of the brands with some of those tougher comparisons and the weather headwinds behind you, even if it's at sort of a higher level. And sort of maybe how do you think about how the brands are positioned in the U.S. in a seemingly difficult environment and whether there is sort of any notable strategy shifts that you guys contemplate in an environment like this, be it on value or otherwise. Thank you.

David Gibbs

Yes. Thanks Dennis. I think we referred to this somewhere, but I will just for completeness. So, in Q1, obviously we had a lot of impact by the weather during the quarter. Our business generally improved sequentially during the quarter. Taco Bell, as you know, is 75% of our U.S. operating profit. Taco Bell improved throughout the quarter. And into Q2, we are seeing an acceleration of same-store sales growth trends. So, we are feeling good about how Taco Bell is positioned. Remember, they just launched their Cantina Chicken menu at the end of Q1. So, we are excited to share the results of that. But suffice to say, it's been well received by consumers. And we think Taco Bell is incredibly well positioned for what I would describe as a more normal consumer environment today. Customers care more about value in the U.S. Taco Bell, we know from the industry data that value is more important and that others are struggling with value and that Taco Bell is a value leader. You are seeing some low-income consumers fall off in the industry. We are not seeing that at Taco Bell. So, a really favorable setup for Taco Bell, which you probably can say about any environment that they operate in given the strength of the brand. And for Pizza Hut, obviously, the lapse in the quarter were unusually large. We always intend to lap anything with positive sales. We didn't do that at Pizza Hut U.S. But we are positive on a 2-year basis and we actually did see an acceleration of Pizza Hut's 2-year trends in Q1 versus Q4. I am excited about the calendar that Pizza Hut has for the balance of the year as well in the U.S. For KFC, it's a different story. The KFC brand in the U.S. has been struggling. And I think we are excited about some of the work that's going on behind the scenes to really boldly reset the brand in the U.S. We have a great playbook for KFC, which is our global business, our international business on fire, as I talked about before, the underlying business. We know how to bring that brand to life to connect with consumers around the world, and we have to do a better job of that in the U.S. It's a small part of our operating profit. Obviously, it doesn't really move the needle in the Yum! growth equation, but it is something that's a high priority for us as we move forward.

Operator

Thank you. The next question goes to Sara Senatore of Bank of America. Sara, please go ahead. Your line is open. Hi Sara, your line is open.

Sara Senatore

Sorry. First, a quick follow-up and then a question, just about the impact from the Middle East, you said it was dissipating. I was just curious if you are doing anything specific to do that like brand marketing, that type of thing, or if it's just a matter of time. The question is about unit growth over time and sort of how that translates into system-wide sales, maybe this year and beyond. As some of these AUVs are coming in lower as you think about your long-term algorithm, how should we think about that either this year kind of hitting the long-term algorithm from a top line perspective or over time?

David Gibbs

Sure. Thank you, Sara. The first part of your question, no, I don't think we are doing anything special. We have obviously had a lot of experience in the past being – with the global footprint we have of dealing with different issues around the world, and we have a sense for how these things recover. But everyone is different and time is usually the answer to most of those problems. As far as unit growth goes, yes, it is true that a lot of times when we are building, we are building particularly with our footprint and our emphasis on development. We are building in emerging markets which tend to have lower average unit volumes. That's how we built the powerhouse business in China back in the day and it's how we are building out markets like India, which tend to have lower volumes. But we are also excited about a lot of the development agreements and new franchise partners that we are getting in Western Europe, for example, and some other markets around the world, which are much higher volume markets. And I think it will always be a mix and it will probably always tend to be lower volume than our typical average volume. And that's fine because these are markets that tend to start out with lower volumes and grow faster than a traditional market, and we have seen that all around the world over the last few decades as Yum! has built out its footprint. Operator, we have time for one more question.

Operator

Thank you. The next question goes to David Tarantino of Baird. David, please go ahead. Your line is open.

David Tarantino

Hi. Good morning. My question is on your results in the context of the sales performance. I think you mentioned that the operating profit in Q1 was slightly better than your expectations. I was curious to know how the sales are progressing relative to the expectations you might have had when you gave the guidance originally. And then in particular, I guess was Q1 about what you expected, better than what you expected? And then secondly, David, if you could give us some sense of whether you have line of sight to global comps performance turning positive either in the second quarter or in the second half of the year. Thanks.

David Gibbs

Thanks David. Obviously, we didn't anticipate the weather impacts in the U.S., for example, in Q1. So, it generally was in line with what we expected, perhaps just a tad weaker. But to the point of your question, as we go into Q2, as I mentioned earlier, the Taco Bell business is picking up strength. We are generally on track with our projections for the year, which is why we feel comfortable with our operating profit commitment and the long-term algorithm. But it is going to be a challenging year, and we have a great team out there on tackling the challenges. And in any one of these challenging years, it's always an opportunity to grab market share as well. We are doing that through development with the pace of development that you are seeing. And I will just close with a few comments about the business. We talk about this a lot, but I think this was a quarter that really demonstrated how resilient this business is and how we can navigate just about anything thrown our way. The fact that we are sitting here in this first quarter in this choppy environment and we are able to put up 6% core operating profit growth and reconfirm that 8% plus target, I think is a testament to the levers that we have to pull and the talent we have around the world. Our twin growth engines which are 80% plus of our operating profit Taco Bell U.S. and KFC International, their underlying strength of their business is obvious when you look at the 10% unit growth at KFC or you look at Taco Bell's performance with low-income consumers in a value environment and the acceleration we are seeing in 2Q. Our development machine, we actually just put up the second highest quarter for gross development in Yum!'s history, obviously on track to meet or exceed that 5% development target. And then very exciting, the digital inflection point. Passing 50% digital is something I don't think people thought was possible just a few years ago this quickly. It's a real testament to the quality of the teams that we put together. And as you can see from our prepared remarks, we are not at all resting on that as a key accomplishment as we lean in on things like AI and the use of our data to separate ourselves from the rest of the industry. I will leave you with one final fact which I heard just the other day which really goes to the core of what we are and the strength of our business. Since January of 2021, 25% of all the Yum! units in the world have been built. That's how new our asset base is. That's how fast we are developing. Think about the impact that, that has on the consumer in terms of how fresh and modern our brands are. Since January '21, 25% of our store base has been built. We don't see that slowing down at any time soon. And in a choppy environment this year, we are very confident that we can get through it, strengthen our business and come out of it delivering that 8% core operating profit growth. Thank you for your time today.

Operator

Thank you. This now concludes today's call. Thank you all for joining. You may now disconnect your lines.

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