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Secondary Offering

Why Yum China's secondary offering will be a game changer

Ironically, Yum China may be able to utilise the current health pandemic for their listing advantage as they consider following fellow ADRs JD.com and NetEase to Hong Kong.

By **Christopher Chu**
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Yum China, the US-listed Chinese operator for KFC, Pizza Hut and Taco Bell, is reportedly exploring a secondary offering in Hong Kong.

Alibaba raised $13 billion in November last year.

The appeal towards raising money in Hong Kong comes as relations between the United States and China further deteriorates amid ongoing trade tensions and criticisms over the novel coronavirus. Aggressive rhetoric has spilled into financial markets, where the US Congress plans to require Chinese companies listed in New York to comply with US auditing regulations.

“By doing so, the US legislature has probably triggered a chain effect that will accelerate the growth of Chinese equity markets, Hong Kong, Shanghai and Shenzhen, at the expense of US markets,” according to Fabrice Jacob, Founder of JK Capital Management in Hong Kong.

Bipartisan support follows the Luckin Coffee scandal after the company admitted to reporting fabricated sales back in April. Tougher actions towards Chinese companies coincide as nearly two-thirds of Americans have a negative opinion of China, the highest percentage recorded since the survey began in 2005 according to the Pew Research Centre.

The Benefits Of Being Home

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Yum China is part of a listing emigration that could add more than $550 billion into Hong Kong, according to estimates by Jefferies. The pickup in secondary listing overlaps new eligibility rules on the Hang Seng Index to include companies with weighted voting rights.

Inclusion benefits not only attracts passive fund liquidity but would allow mainland investors to buy shares in domestic leaders, particularly those with strong commercial branding and are well known in China. This would be particularly valuable to Yum China which operates more than 9,000 restaurants in over 1,400 cities.

The pickup in trading volumes is noticeable. Shanghai Connect Southbound total turnover exceeded HKD $1 billion during the first five months of 2020, compared to HKD $700 million over the same period last year, according to data from the Hong Kong exchange.

The timing of Yum China's potential secondary offering measures investor appetite during a global health crisis, as recent deals have predominately focused on healthcare and biotechnology names.

Among notable IPO deals over the past three months include bio-tech company Akeso which raised $380 million and Peijia Medical which raised $350 million. InnoCare Pharma, the Chinese clinical stage biopharmaceutical firm focused on cancer drug discovery, raised $330 million.

The post Covid-19 operating environment acts as a greater challenge to quick service restaurants, where social distancing keeps fewer customers inside and store closures are unpredictable. Food safety and supply chains are renewed worries, while pre-coronavirus challenges include rising demand for healthier eating options.

Investor Largesse

Ironically, Yum China may be able to utilise the current health pandemic to their advantage. Like other ADRs, Yum China's brand and management reputation are already well-known by institutional investors, thus removing the necessity to conduct any new roadshows. Asia-based fund managers are already aware of the political headwinds New York listed Chinese companies face, having heard the same script from JD.com and NetEase earlier.

Seasonally, larger deals tend to take place in the second half of the year, allowing companies to show two quarters of financial results and can provide guidance for the remaining six months says Cecilia Lee, Managing Director of a New York-based boutique placement firm.

Raising money would also bode well for Yum China after the group rejected a $18 billion offer in August 2018, which at the time showed that bidders were prepared to pay a lofty valuation of 14 times consensus EBITDA estimates.

Investors have accepted that 2020 is a wash year, as Yum China currently trades at almost 18 times consensus EBITDA estimates for this year and 12 times for 2021. Shares in Yum

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Like other Chinese ADRs looking back to Hong Kong, the opportunity window to list while investors are forgiving may close suddenly. “There is a home bias for both the US and in China, which Chinese companies are aware of. Geopolitical sentiment could change after the November elections, but companies are taking action now,” says Lee.

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