

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Unless otherwise noted, the section references to (i) "us", "our", "we", "the Company" and "YUM" refer to YUM Brands, Inc. and its consolidated subsidiaries, (ii) "the Parent" refers to YUM Brands, Inc., on a stand-alone basis, (iii) "the Issuers" refers to KFC Holding Co., Pizza Hut Holdings, LLC and Taco Bell of America, LLC, which are direct wholly-owned subsidiaries of the Parent and co-issuers of \$1.05 billion of 5.00% Senior Notes due 2024, \$1.05 billion of 5.25% Senior Notes due 2026, and \$750 million of 4.75% Senior Notes due 2027 (collectively, the "Subsidiary Senior Unsecured Notes") and co-borrowers under the Credit Agreement, as defined in our annual report on Form 10-K for the year ended December 31, 2017 filed with the SEC (the "2017 10-K") on February 22, 2018; (iii) "the Specified Guarantors" refers to collectively Yum Restaurant Services Group, LLC, Restaurant Concepts LLC and Taco Bell Corp. (including their subsidiaries except for Taco Bell Funding, LLC and its special-purpose, wholly owned subsidiaries), which are directly wholly-owned subsidiaries of the Parent and guarantors of the Notes and under the Credit Agreement; (iv) "the Companies" refers to collectively the Issuers and the Specified Guarantors, (v) "the Taco Bell Securitization Entities" refers to collectively Taco Bell Funding, LLC, a Delaware special purpose limited liability company and wholly owned subsidiary of Taco Bell Corp, and its special-purpose, wholly owned subsidiaries, and (vi) the "Restricted Group" refers collectively to the Companies and their subsidiaries, other than the Taco Bell Securitization Entities which will not be subject to the covenants under the Indenture governing the Subsidiary Senior Unsecured Notes and the Credit Agreement, and also excludes the Parent and ABR Insurance Company which will not be subject to such covenants as well.

This discussion should be read in conjunction with the Condensed Consolidated Financial Statements ("Financial Statements") and the section "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in our quarterly report on Form 10-Q for the quarter ended September 30, 2018 as filed with the SEC on November 7, 2018 (the "Third Quarter 10-Q") and contains additional information related to the pro forma results of operations and financial condition of the Restricted Group. None of the financial information in this discussion has been audited or reviewed by our auditors. This discussion has been prepared and posted to our website in accordance with our reporting obligations under the Indenture governing the Subsidiary Senior Unsecured Notes and the Credit Agreement. You should read the following Restricted Group's pro forma results of operation and financial condition together with the information included in our 2017 10-K, especially the information under the heading "Risk Factors".

Pro Forma Results of Operations for the Restricted Group

The following table sets forth certain unaudited financial and operating data of the Restricted Group as of the dates and for the periods indicated after giving pro forma effect to the exclusion of the Taco Bell Securitization Entities from the Restricted Group as if the Securitization Transaction had occurred on the first day of fiscal year 2017.

	Quarter ended			Year to date		
	2018	2017	% B/(W)	2018	2017	% B/(W)
Company sales	\$ 499	\$ 871	(43)	\$ 1,523	\$ 2,682	(43)
Franchise and property revenues	475	449	6	1,404	1,281	10
Franchise contributions for advertising and other services	287	—	N/A	834	—	N/A
Total revenues	<u>\$ 1,261</u>	<u>\$ 1,320</u>	(4)	<u>\$ 3,761</u>	<u>\$ 3,963</u>	(5)
Restaurant profit	\$ 85	\$ 136	(37)	\$ 223	\$ 405	(45)
Restaurant margin %	17.2 %	15.7 %	1.5 ppts.	14.7 %	15.1 %	(0.4) ppts.
G&A expenses	\$ 175	\$ 186	6	\$ 541	\$ 617	12
Operating Profit	\$ 437	\$ 538	(19)	\$ 1,234	\$ 1,236	-

Performance Metrics

Unit Count	9/30/2018	9/30/2017	% Increase (Decrease)
Franchise	38,852	36,353	7
Company-owned	1,173	2,335	(50)
	<u>40,025</u>	<u>38,688</u>	3

	Quarter ended		Year to date	
	2018	2017	2018	2017
System Sales Growth (decline), reported	2%	5%	5%	3%
System Sales Growth, excluding FX	4%	5%	4%	5%
Same-store Sales Growth %	2%	3%	1%	2%

The Securitization Transaction and the exclusion of the Taco Bell Securitization Entities from the Restricted Group had the following pro forma impact on the financial and operating data of the Restricted Group and the Taco Bell Division of the Restricted Group in comparison to the corresponding data of YUM and the Taco Bell Division:

Units

- A total of 5,951 and 5,664 U.S. Taco Bell franchise units were excluded from the Restricted Group as of September 30, 2018 and 2017, respectively, as the Restricted Group no longer receives franchise fees from these restaurants.

Franchise and Property Revenues

- Franchise and property revenues decreased \$130 million and \$116 million during the quarters ended September 30, 2018 and 2017, respectively, due to the exclusion of the franchise fees paid by all U.S. Taco Bell franchise restaurants as a result of the Securitization Transaction.
- Franchise and property revenues decreased \$369 million and \$338 million for the years to date ended September 30, 2018 and 2017, respectively, due to the exclusion of the franchise fees paid by all U.S. Taco Bell franchise restaurants as a result of the Securitization Transaction.

Company Restaurant Expenses

- Company restaurant expenses increased \$15 million and \$18 million during the quarters ended September 30, 2018 and 2017, respectively, due to the payment of royalty fees of 5.5% of annual sales to the Taco Bell Securitization Entities by all U.S. Company-owned Taco Bell restaurants (which are part of the Restricted Group).
- Company restaurant expenses increased \$42 million and \$54 million for the years to date ended September 30, 2018 and 2017, respectively, due to the payment of royalty fees of 5.5% of annual sales to the Taco Bell Securitization Entities by all U.S. Company-owned Taco Bell restaurants (which are part of the Restricted Group).

G&A Expenses

- G&A expenses decreased \$29 million during each of the quarters ended September 30, 2018 and 2017 due to the management fees paid by the Taco Bell Securitization Entities to Taco Bell Corp. as manager of the Taco Bell Securitization Entities. These fees are recorded as a reduction of G&A expenses and, on an annual basis, are equal to the sum of a base fee of \$35 million (subject to 2% per annum escalation, compounded annually) plus 15.1% of total securitization cash revenue paid to the Taco Bell Securitization Entities by company stores and franchisees for the year.
- G&A expenses decreased \$85 million and \$82 million for the years to date ended September 30, 2018 and 2017, respectively, due to the management fees paid by the Taco Bell Securitization Entities to Taco Bell Corp. as manager of the Taco Bell Securitization Entities. These fees are recorded as a reduction of G&A expenses and, on an annual basis, are equal to the sum of a base fee of \$35 million (subject to 2% per annum escalation, compounded annually) plus 15.1% of total securitization cash revenue paid to the Taco Bell Securitization Entities by company stores and franchisees for the year.

Consequently, the overall operating margins of the Restricted Group are negatively impacted due to the loss of franchise and license fees from U.S. franchised restaurants and our obligation to pay franchise fees on U.S. Company-owned restaurants to the Taco Bell Securitization Entities, while maintaining the same level of expenses (other than the reimbursement of a portion of G&A expenses).

Beginning in 2018, amounts transferred to or on behalf of Yum! Brands, Inc. as Parent Entity Expenses (as defined in the Indentures) or operating costs and expenses incurred in the ordinary course of business (as permitted by the Credit Agreement) were excluded from G&A expenses of the Restricted Group. G&A expenses of the Restricted Group were reduced for such costs by less than \$1 million for the quarter ended September 30, 2018 and \$5 million for year to date ended September 30, 2018.

System sales growth was negatively impacted by the refranchising of U.S. Company-owned Taco Bell restaurants. These refranchised units were no longer included in the Restricted Group upon completion of the refranchising transaction.

Restricted Group - Taco Bell Division

	Quarter ended				Year to date			
	2018	2017	% B/(W)		2018	2017	% B/(W)	
			Reported	Ex FX			Reported	Ex FX
System Sales Growth			(10)	(9)			(14)	(15)
Same-Store Sales Growth %			6	N/A			4	N/A
Company sales	\$ 265	\$ 318	(17)	(17)	\$ 761	\$ 991	(23)	(23)
Franchise and property revenues	12	8	69	71	35	20	81	81
Franchise contributions for advertising and other services	106	—	N/A	N/A	\$ 294	\$ —	N/A	N/A
Total revenues	<u>\$ 383</u>	<u>\$ 326</u>	18	18	<u>\$ 1,090</u>	<u>\$ 1,011</u>	8	8
Restaurant profit	\$ 50	\$ 51	(2)	(2)	\$ 132	\$ 165	(20)	(20)
Restaurant margin %	19.3%	16.4%	2.9 ppts.	2.9 ppts.	17.4%	16.7%	0.7 ppts.	0.7 ppts.
G&A expenses	\$ 11	\$ 12	5	4	\$ 36	\$ 40	9	10
Franchise and property expenses	5	6	9	9	17	16	(10)	(10)
Franchise advertising and other services expense	107	—	N/A	N/A	293	—	N/A	N/A
Operating Profit	\$ 45	\$ 42	8	8	\$ 116	\$ 130	(10)	(10)

Unit Count	9/30/2018	9/30/2017	% Increase (Decrease)
Franchise	430	363	18
Company-owned	561	711	(21)
	<u>991</u>	<u>1,074</u>	(8)

Company Sales. The decrease in Company sales for the quarter was driven primarily by refranchising, partially offset by company same-store sales growth of 6% and net unit growth.

The year to date decrease in Company sales was driven primarily by refranchising, partially offset by company same-store sales growth of 3% and net unit growth.

Restaurant Profit. The decrease in Restaurant profit for the quarter was driven primarily by refranchising and higher labor costs, partially offset by company same-store sales growth of 6% and commodity cost deflation.

The year to date decrease in Restaurant profit was driven primarily by refranchising and higher labor costs, partially offset by company same-store sales growth of 3%.

G&A Expenses. The quarterly decrease in G&A expenses was driven primarily by the positive impact of YUM's Transformation initiatives, including reductions in G&A directly attributable to refranchising.

The year to date decrease in G&A expenses was driven primarily by the positive impact of YUM's Transformation initiatives, including reductions in G&A directly attributable to refranchising, the favorable impact of forfeitures related to share based compensation awards and higher management fees paid by the Taco Bell Securitization Entities, partially offset by lapping lower litigation costs.

Operating Profit. The quarterly increase in Operating Profit was driven by same-store sales growth, partially offset by refranchising.

The year to date decrease in Operating Profit was driven by refranchising and higher restaurant operating costs, partially offset by same-store sales growth.

Additional Information Related to Restricted Group:

Adoption of Topic 606

From 2014 through 2017 the FASB issued standards to provide principles within a single framework for revenue recognition of transactions involving contracts with customers across all industries ("Topic 606"). We adopted these standards beginning with the quarter ended March 31, 2018, using the modified retrospective method. The impact on the Restricted Group Operating Profit was not significant.

Refer to Notes 2 and 5 of the Form 10-Q for the quarter ended September 30, 2018 for further discussion.