Case Study

YUM - KFC’s in China

Introduction

Homogenization has made it easy for fast-food joints to circle the globe, spitting out carbon copies of themselves, their burgers, and their fries along the way. But in the most populous country in the world, a fast-food giant stepped off the conveyor belt and found unprecedented success by being different, not by being the same.

Vision:
“We want to build three global iconic brands that people trust and champion. We’re going to get there by having very clear brand truths, very clear brand personalities and very clear filters through which we make all of our decisions. To reach our destination, we’re going to make our brands more relevant, more engaged, more connected and we’re going to demonstrate that we care as much as our customers care. This will be an evolution, not a revolution, as we build on the shoulders of giants. We want to build on everything that David Novak has done all of these years to make Yum! the Defining Global Restaurant Company That Feeds The World.”

Culture:
“We have a famous recognition culture where everyone counts. It’s our biggest competitive advantage and we’ve done an amazing job with the culture in our Restaurant Support Centers around the globe. However, I believe the customer experience will never exceed the team member experience. That’s why we’re going to continue to focus on driving our unique culture to our restaurant team members. It’s also important that the leaders in our company are Smart with Heart and have the Courage to make the big decisions that will drive success in the future.”

Community:
“We are a company with a huge heart. In order to build brands that people trust and champion, we have to demonstrate that we care more than anyone else. Our brands have great initiatives around the globe to give back to the communities in which we operate, making a positive difference in the lives of our customers, associates,
franchisees and their families. We also believe it’s our privilege and responsibility to address world hunger. That’s why we created World Hunger Relief in 2007 to raise awareness, volunteerism and funds for the U.N. World Food Programme and others. I’m enormously proud we’ve raised $600 million in cash and food donations, providing 2.4 billion nutritious meals for women and children thanks to the generosity of our customers, associates and franchisees.”

**Innovation:**

“We are going to lead with innovation. Our brands are the global leaders in their respective categories, and we expect to build on this strength with breakthrough product innovation, insight-driven marketing and digital leadership in the years ahead.”

Future Growth: “We expect to open over 2,100 new international restaurants in 2015, further strengthening our lead in emerging markets. We remain focused on the three keys to driving shareholder value: same-store sales growth, new-unit development and generating high returns on invested capital. I’m confident we’ll deliver full-year EPS growth of at least 10% in 2015 and produce consistent double-digit EPS growth over the long term.”

**A matter of scale**

Both KFC and Pizza Hut restaurants in China differ markedly in many ways from their Western counterparts. And while Pizza Hut has done very well for itself with nearly 500 restaurants in 120 cities (as of December 2010), KFC's performance has been finger-lickin' incredible. Since the first piece of fried chicken (available in dark meat only, to the disappointment of many an American tourist) was served at a Beijing KFC in 1987, the number of KFCs in China has grown to over 3,000, in 650 cities, with one new restaurant opened a day.

"If I could have written any case in the world, this would have been the one I would have picked," says Shelman, a Kentucky native with more than a passing interest in Colonel Sanders. "Not only is this the story of a successful entry into China by a Western company, this case provides a glimpse of how quickly Chinese diets are
changing as incomes improve. Because China is so big this has a huge impact on the rest of the global food system. What happens in China, what Chinese people eat, impacts what you and I pay for food."

What happened in China with Yum! Brands, and with KFC in particular, had a lot to do with China division chairman and CEO Sam Su. "He really flexed the model," says Shelman. This was in part due to KFC being owned by PepsiCo when it first came to China. PepsiCo was not a fast-food company, so Su was given more managerial freedom.

Along with being lucky, Su is smart, driven, and visionary—a classic entrepreneur. But he's also humble. "There's no room for ego," Su explained in the case. "China doesn't have the same culture of individualism that is present in the United States."

Su's strategy was that KFC "would not be seen as a foreign presence but as part of the local community… Our opportunity was to take the best ideas from the US fast-food model and adapt them to serve the needs of the Chinese consumer."

Initially this involved hiring the right people. For Su this meant Chinese managers who read and spoke the language, who understood the restaurant business and the Chinese consumer, but who also had experience in the Western way of doing business. "It was a foot in both worlds," Shelman says. "They knew firsthand the Western model but they also understood the challenges of operating in this Chinese, very traditional, very evolving market."

The people Su brought on board were also close in a way Shelman found surprising when she spent time with them when researching the case.

"There was huge camaraderie evident in the way that the top management team interacted with each other … they bantered back and forth and poked fun at each other," Shelman says. "They'd be walking down the hall jostling, pushing, laughing. This is a group that has worked together a long time—unusual in a country where experienced management talent is at a premium."

It turns out that unusual employee interactions, at least in comparison with Western business decorum, are the norm at Yum! Brands, something Shelman experienced
when she accompanied then-COO Mark Chu to one of KFC's Shanghai locations. "You walk into a restaurant and not only do [the employees] recognize him, but they love him as well."

And so the employer-employee relationship has more a feel of family. "In the United States, if you don't show up at work, what happens? You get fired," says Shelman. "In China, where many of the company's 250,000 employees are college students working their first job, it's like, 'Oh we understand that sometimes you feel like skipping class. If you decide to skip work—please call in and let us know, so we can make sure your job is covered.'"

Trained labor, it turns out, is a very valuable asset even in a land of 1.3 billion-plus people.

"Chu's acceptance and appreciation for these young employees is exceptional for Western companies to see," says Shelman. Younger employees, for example, are encouraged to socialize over company-provided video games on their breaks. This practice serves several purposes: It eases the minds of parents anxious about sending their children out into the world, provides crucial social skills for young adults who grew up in single-child households, creates lifelong Yum! Brands customers, and develops a culture of customer service in a country where there was none.

The restaurant management program is similarly focused. "You're a college graduate," says Shelman. "You're recruited for that position. You're very carefully developed to be able to do all these different jobs in the restaurant. And it's perceived as something that you would do your entire life."

Along with training and retaining quality employees, another key factor in KFC's success was Su's early decision to downsize his own career. Originally hired to cover the northern Asia-Pacific region, he departed from the usual managerial growth path of taking on larger geographic assignments and instead argued that he should focus exclusively on China. Early on, he decided that Yum! should develop a national footprint—supported by a company-owned distribution system since third-party suppliers didn't exist—instead of growing in geographic chunks through franchising.
Su sourced products from within China whenever possible. This was no easy feat early on as the supply chain for chicken, for example, included multiple vendors providing a handful of birds each. Food safety is a big concern for Chinese consumers, and it was Su's decision to build the supply chain from the ground to help ensure quality. "We work with our suppliers to build their capabilities. We stress the importance of knowledge transfer, and even arrange for them to go overseas to learn," Su said in the case.

**The Chinese way**

"One of the lessons I take away from this case is that to do China, you have to do China," says Shelman. "It's a large, complex, and dynamic market that deserves single-minded attention." That attitude extends from the boardroom of Yum! Brands to the menus in KFC restaurants. A small number of items would be familiar to Western visitors—mashed potatoes, corn on the cob, fried bone-in chicken—but most would not. The Chinese KFC menu may include fried dough sticks, egg tarts (which Shelman raves are "to die for"), shrimp burgers, and soymilk drinks, as well as foods tailored to the tastes of specific regions within China.

The large selection of menu items is meant to appeal to the Chinese style of eating, in which groups of people share several dishes. But it's also part of the "New Fast Food" initiative Su developed in 2005 in response to concerns about the role of fast-food restaurants in the obesity epidemic—concerns that he shares and takes responsibility for. "We have been too greedy, too shortsighted," Su said, referring to the traditional high-volume, low-choice fast-food model.

Su believes that offering a wider variety of foods will help patrons make healthier choices. The KFCs in China have also limited the amount of money saved on combo meals, and have completely eliminated supersized items. Exercise is actively promoted inside the chain; as of 2010 the youth programs and competition it sponsored had over 260,000 participants in 438 cities.

KFC succeeded in China both because it was not McDonald's and because in many ways it decided it wouldn't be KFC either—which brings up another key question. "With the benefit of 20/20 hindsight…how do you avoid the mistakes of the
American fast-food model?” asks Bell. “Put another way, if McDonald's and KFC were to start over in the United States knowing what they know now, how would their model differ?”

Questions:

1/. What are the similarities and what are the differences between KFCs in China versus fast food restaurants in the U.S. or Greece?

2/. What special challenges did Yum face in exporting the KFC model, and how did Sam solve them?

3/. How can Sam make sure that fast food restaurants in China don't make the same mistakes (you define what those mistakes are!) as in the West?

4/. Is Sam ready to go ahead with another 15,000 stores? What would be the right timeframe for that?