

Krause Fund Research

Spring 2019



McDonald's Corporation

Consumer Discretionary

November 15th, 2019

Stock Rating:

BUY

Analysts

Target Price: \$250-260

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Investment Thesis

We recommend a **buy** rating for McDonald's Inc. because their revenue distribution, low prices, industry innovation, and large market share make it a great counter-cyclical stock to own in an economic downturn.

Drivers of Thesis

- McDonald's operates in 110 countries around the world and with only 36% of sales coming from the United States, they can provide steady revenues in the event of a recession in any geographic region.
- We are forecasting a recession to occur in 2020, and McDonald's low-cost menu will attract more customers due to consumers' lower disposable income.
- McDonald's has been on the forefront of technological innovation in the restaurant industry by implementing mobile-ordering, delivery, and in-store kiosks which have increased same-store revenues 6.13%.
- Their stock price has declined 8% in the past month due to a missed earnings call and their C.E.O. getting fired. This represents an excellent opportunity to buy McDonald's at a discount.

Risks to Thesis

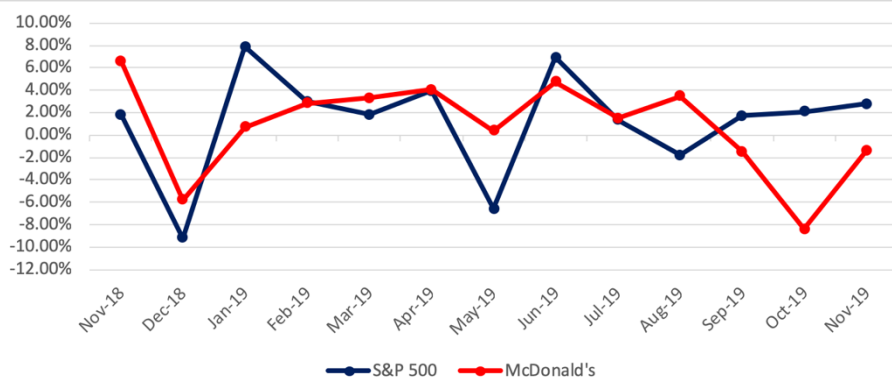
- McDonald's has a BBB+ credit rating, and they will stop repurchasing shares and growing dividends in 2020 to pay down their debt.
- Revenue growth and investor sentiment assumptions are reliant on a recession occurring in 2020 or 2021, and if a recession does not occur, we could fall short of our target price.

Stock Values	
DDM	\$289.37
DCF/EP	\$258.65
Relative Valuation (P/E '20)	\$185.89
Current Price	\$194.28
Key Statistics	
Market Capitalization (MM)	159,000
Shares Outstanding (MM)	794
52 Week High	221.93
52 Week Low	169.04
Dividend Yield	2.58%
Price/Earnings '19	25.7x
Profitability	
ROA '19	0.18
Gross Margin	0.43
Profit Margin	0.28
Financial Ratios	
EV / EBITDA	18.39
Total Debt / EBITDA	4.38

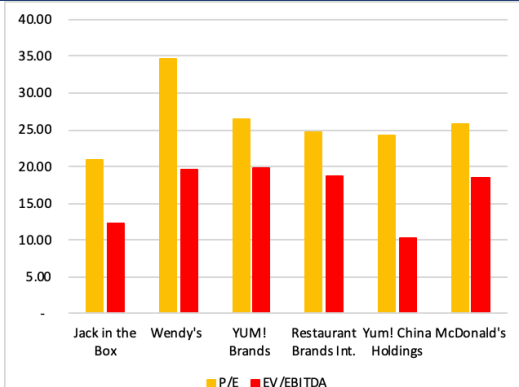
Earnings Estimates

Year	2016	2017	2018	2019	2020	2021
EPS	5.69	5.7	7.73	7.56	7.83	8.16
Growth	0.16	0	0.35	-0.02	0.04	0.04

12-Month Performance



Relative Financial Performance



Macroeconomic Outlook

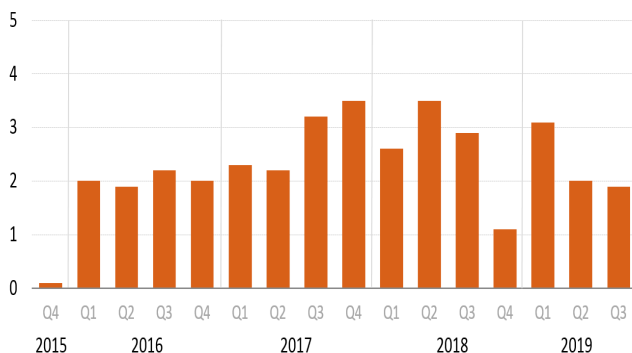
U.S. Real Gross Domestic Product (GDP)

Real GDP is one of the most important indicators of economic health and performance because it values all goods and services produced within the United States on an annual basis. With GDP increasing, it signals that the economy is expanding, which is a good indicator for the Consumer Discretionary Industry. 70% of GDP comes from consumer spending, and if consumer spending continues to increase then the Consumer Discretionary Industry will benefit greatly.

GDP has seen volatility in the past two years. From 2018 third quarter, real GDP has increased to 1.9% in 2019 third quarter GDP. However, it decreased slightly from 2019 second quarter where GDP was 2.0%, and 3.0% growth from 2019 first quarter. This decrease in GDP quarter-over-quarter can be attributed to the ongoing trade war with China which results in margin compression from firms as well as a decrease in capital expenditures.²⁸ The trade war will affect the Consumer Discretionary Industry by increasing the costs of their products due to tariffs, and this will lead to a decrease in revenues because less consumers will buy products due to increased costs.

In the short-term, we forecast a decrease in Real GDP of 0.5% to 1.4% in the next quarter due to the continuing trade uncertainty with China and a global economic slowdown. In the long run, we expect GDP to decrease to 1.0% because of the effects of a global recession and decreasing corporate profits due to margin compression from the trade war and employment market.

Real GDP: Percent change from preceding quarter



U.S. Bureau of Economic Analysis

Seasonally adjusted at annual rates

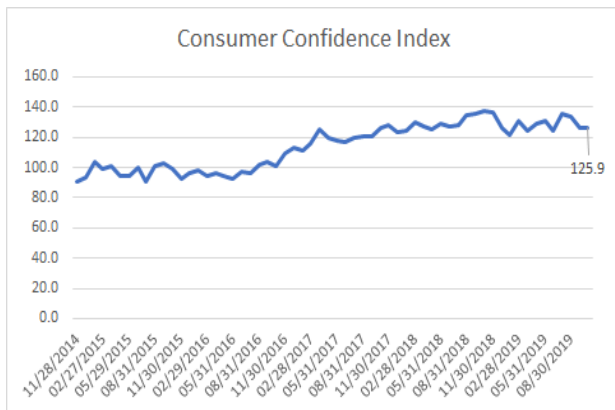
Consumer Price Index (CPI)

The Consumer Price Index (CPI) is a measure of inflation which is the rate at which prices are rising as it relates to purchasing power. When inflation increases, the price of goods and services becomes more expensive for the consumer. This causes the consumer to spend less on goods and services because they do not have the purchasing power to afford them. The CPI is an important indicator when analyzing the Consumer Discretionary Industry because the industry is heavily dependent on consumer purchasing activity, which could be halted if inflation increases. The inflation rate is currently at 1.8% which is an increase of 0.1% for the period ending September 2019. We expect inflation to increase to 2.0% in the short run due to record low unemployment and record high wages which give consumers more money to spend.² In the long run the CPI will decrease to 1.0% due to lower consumer spending during a recession.⁵

Consumer Confidence Index (CCI)

The Consumer Confidence Index is an important macroeconomic indicator because it reflects how optimistic consumers are about the direction of the economy. This measure is important in the Consumer Discretionary Industry because the industry is very dependent on disposable income and consumer spending. Optimistic consumers tend to spend more while pessimistic consumers will spend less because they fear that they will be facing financial hardship in the near future and will then save their money instead of spending it.

The CCI dropped slightly in October to 125.9 from a 126.3 reading in September, but this is a very strong reading regardless of the drop. While this is a significant drop from the October 2018 reading of 137.6, we expect the CCI to decrease slightly to 126.4 due to consumers expecting increased wage growth and low unemployment soon. IBISWorld, a private research company, projects CCI will decrease to 122.47 by 2021 due to the recessionary environment.⁶



Unemployment Rate & Labor Force Participation Rate

The unemployment rate has steadily decreased from 6.2% to a record low 3.6% since 2014.²² The unemployment rate has remained low over the past six months centering around the current unemployment rate of 3.6%. During this time period the labor force participation rate has remained just under 63% and has jumped up to 63.3% as of October.⁹ This indicates that people entering the workforce are quickly finding jobs and the labor market is very strong. This is displayed in the most recent Job Opening and Labor Turnover Survey (JOLTS) which shows a ratio of 0.8 unemployed people to job openings.⁹ Strong labor markets have historically been a good indicator for the consumer discretionary industry compared to less elastic industries.

We expect that the unemployment rate will increase by 0.1% by year end and will increase by 0.2% over the next year due to recessionary trends.⁹ While this may harm the Consumer Discretionary Industry, more countercyclical sectors such as the fast-food sector within the restaurant industry will be impacted less due to their low-cost options that consumers will gravitate to when incomes decrease.



Retail Trade Sales and Food Services Sales

Retail trade sales and food services sales reflect the amount of consumer spending for personal consumption. Approximately two-thirds of U.S. GDP is comprised of personal consumption which is largely reflected in retail and food services sales. Since 2010 these sales have grown at an average rate of 4.5%, however in 2009 sales dropped 7.5%.¹² This is a direct indication of the recession's effects on consumer spending. While consumer spending is largely affected by recession, the restaurant industry revenues only decreased by 0.72% in 2009 and have seen average growth of 5.5% growth since 2010.¹² This shows stability within the restaurant industry and makes McDonald's an attractive business when predicting an economic slowdown. A study by the Financial Times found that fast-food restaurants perform better during recession while most segments of the Consumer Discretionary Industry see a decline in sales.¹⁰ For this reason we predict that Retail Trade Sales and Food Service Sales will decrease by 4% in line with historical sales, but fast-food restaurants will experience a slight increase of 2% in the short run.

Foreign Currency

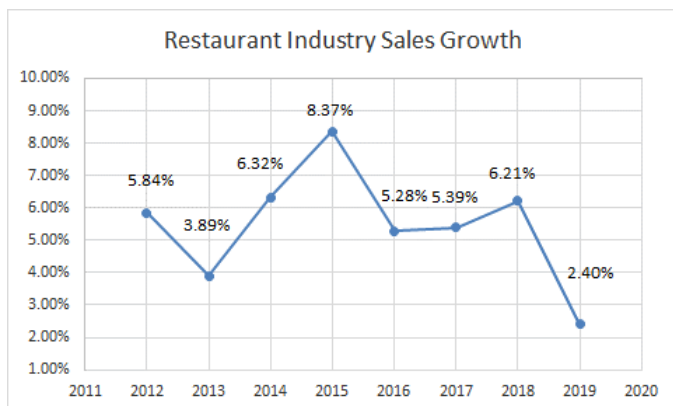
The U.S. Dollar per Euro ratio is important to the Consumer Discretionary Industry because it is an indicator of the attractiveness of U.S. exports. A strong U.S. dollar makes it more costly for other countries to import American goods and will make Europeans less likely to buy discretionary items. The USD/Euro has decreased 4.3% this year to 1.10 USD from 1.15 USD. The EU ranks 1st as an export market for the United States in 2018.²⁹ A strong U.S. dollar will negatively impact the Consumer Discretionary Industry and the economy. We expect the U.S. dollar per Euro ratio to decrease within the next year because of Germany's declining economy, the persisting delay of a Brexit deal, and Europe's negative interest rates. Germany has the largest economy in the EU, and the country's real GDP has decreased in 2019 due to industrial production decreasing 4.2% since July 2018.³⁰ Since the European market is the biggest importer of U.S. goods, the Consumer Discretionary Industry will be negatively impacted by a stronger U.S. dollar because they will not

have as high of purchasing power to buy items that they do not need.

Restaurant Industry Analysis

Industry Description

The restaurant industry is composed of two broad segments: quick service and casual dining. Casual dining restaurants are classified as sit-down restaurants which tend to have higher prices. The quick service category can be further broken down into the two competing categories; fast-casual and fast-food. McDonald's operates in the fast-food category. Total projected sales for the restaurant industry in 2019 amounted to \$129 billion which is a 2.4% growth from the \$126 billion for year end 2018.¹⁰ The restaurant industry is very reliant on consumer spending and positive market conditions. However, fast-food companies, such as McDonald's, are in a prime position to benefit in the event of an economic downturn due to their affordable menu options for individuals and families. Consumers in times of a recession will eat out less to save money, but when they do eat out, they will opt for low-priced meals that companies in the quick-service segment provide.



Casual Dining

The casual dining segment is composed of traditional restaurants that offer sit-down service and payment at the table. This type of service is the main differentiator between casual dining and the quick service segment. The range of product prices in this segment vary greatly; product prices range from prices in the low teens at a local neighborhood diner, to triple digits at some of the upscale establishments.²³ This segment has no market leader, and the market share is comprised of very small

competing local restaurants. The casual dining segment is expected to see an increase in sales of 3.4% in 2019 which is only a 0.2% increase from a 3.2% increase in 2018.¹³

Quick-Service (Fast Food)

The fast-food segment is defined as food that can be quickly prepared for low prices. According to the largest survey of restaurant owners, Restaurant Business, the quick-service sector should see a slight slowdown in 2019 to 4.9% growth compared to 5.1% growth in 2018.¹³ However, the quick-service sector was projected to grow at the second fastest pace of all segments behind fast-casual which was projected to grow 8.3% this year due to consumers having more disposable income that they can spend on more expensive meals.¹³ The fast-casual sector often charges higher prices than the quick-service sector, and this will lead to an increase in revenues from the quick-service sector in times of a recession of which we are projecting in 2020. This trend during recessions will greatly benefit McDonald's since it sits in the fast-food segment.

Developments and Industry Trends

Health Conscious Consumers

Consumers have become more conscious about changing their diets and committing to healthier lifestyles.¹⁵ This has been the catalyst for more restaurants providing healthier menu options to their customers. Childhood obesity is at a record high of 18.5% in the United States, and this has been the cause of many parents limiting their kids consumption of fast-food.¹⁴ Furthermore, more than 80% of U.S. consumers reported that healthy options on the menu played some role in their decision when choosing a restaurant.¹⁵ This trend made companies in the quick-service segment offer more healthy menu options to draw in more health conscious consumers. McDonald's has been a leader in this trend by offering more salads and posting calorie counts for each of their menu items. McDonald's has also partnered with Beyond Meat to offer a vegan burger for its non-meat-eating customers.¹⁶ The rising trend in eating less meat and transitioning to a plant-based diet has made McDonald's and other quick-service

establishments alter their menus to encompass non-traditional American diets.

Technology

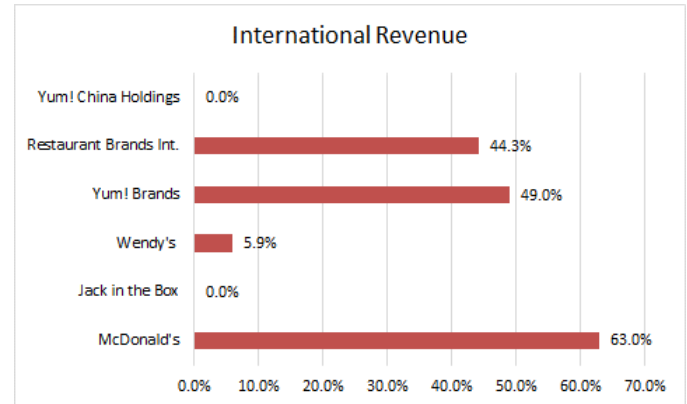
The quick-service industry has been incorporating technology into their business model through mobile ordering, delivery, and updating their restaurants. Customers are increasingly ordering prior to arriving at the restaurant due to convenience and saved time in store. According to Statista, 33% of customers “definitely would” or “probably would” order ahead if given the opportunity.¹⁷ This has strongly influenced restaurants in the entire industry to incorporate mobile delivery. 59% of restaurants surveyed said that they plan to add mobile ordering to their platforms.¹⁸ Food delivery has also experienced an increase over recent years. Digital delivery sales are projected to outpace in-store sales 3x by 2023.¹⁸ McDonald’s has been a market leader for the quick-service industry in this trend. The company has partnered with Uber Eats to expand its food delivery platform which has accounted for 10% of their revenues.¹⁹ However, there is a potential downside to this advancement due to the cases of food tampering from delivery drivers. This could have a negative effect on brand image and customer loyalty. Restaurants are also trying to incorporate technology within the establishment itself. McDonald’s has been implementing order kiosks in their stores to increase efficiency and cut down on overhead, which has led to more positive customer experience.

Competitive Analysis

Competitors

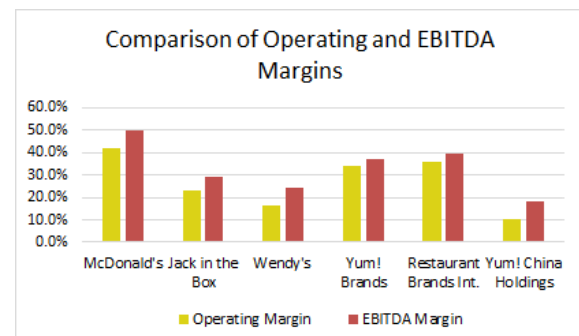
The main competitors of McDonald’s are Jack in the Box Inc., Wendy’s Co., Yum! Brands Inc., El Pollo Loco Holdings, Restaurant Incorporated, and Yum! China Holdings. These companies are in the quick-service restaurant industry and all have large market caps, although McDonald’s has the largest market cap of its comparable peers by some distance. McDonald’s market cap is \$159 billion which is 64.28% of the total market cap of the comparable companies.¹¹ Most of the comparable companies have operations internationally except for Jack in the Box, however, McDonald’s has the most diversified revenue stream. McDonald’s operates

on all 6 continents and has restaurants in 119 countries across the world. This enables McDonald’s to have a steady stream of revenues in times of a recession in the United States compared to companies which operate primarily in the U.S. This is a positive sign for McDonald’s amongst its competitors because we predict U.S. growth to slow in the short-term.



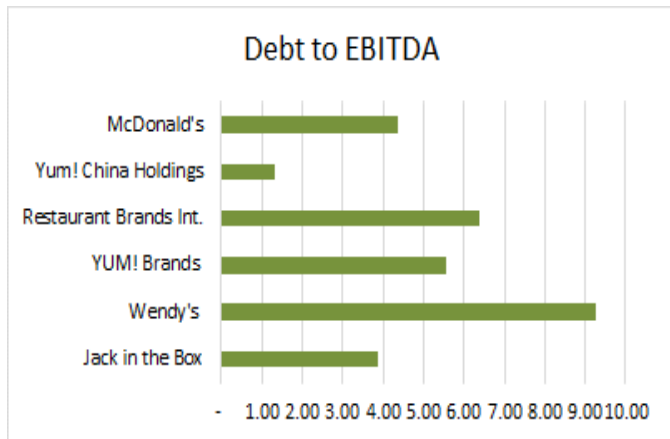
Margin Comparison

McDonald’s prides itself on having a diverse supply chain that buys ingredients from locally sourced farms and companies. The company is able to decrease costs by buying locally due to savings on shipping costs which boosts its bottom line. McDonald’s also saves on costs by franchising the majority of their restaurants, so the cost burden gets shifted onto the franchisee rather than the corporation. This is shown with McDonald’s boasting the highest operating margin of 43%, compared to its next highest peer, Restaurant Brands Inc., of 37%. McDonald’s also has an EBITDA margin percentage of 48% which is the highest amongst its peers by 8% with the next highest being Restaurant Brands Inc.²² The franchise method enables McDonald’s to withstand recessions better than its peers because the decrease in revenue will impact the franchisees more than the corporation due to McDonald’s not having to invest in the restaurants themselves.



Debt to EBITDA Comparison

Having a low Debt/EBITDA ratio is an important metric when analyzing companies in the restaurant industry because it shows how leveraged a company is and whether they can afford their interest payments. McDonald's Debt/EBITDA ratio is 3.17, which is the lowest amongst its comparable peers whose median is 5.24.²² McDonald's has a BBB+ credit rating due to the significant borrowing that they have done over the past few years due to historically low interest rates. While this could be of concern, they have enough cash on hand as well as recurring cash flow to be able to pay down their debt without significant effects to their financials. In McDonald's 10k management said that they would stop buying back shares at their recently record pace in order to pay down debt, which also contributes to their credit rating being not as worrisome for investors.



Share Performance Comparison

When analyzing whether to invest in a company, stock performance is an important metric to consider when valuing comparable companies. Comparing McDonald's P/E ratio to its peers, we found that it has a P/E ratio of 25.70 with the average being 26.12 which is very similar to its peers.²² This shows that McDonald's is the largest company by far compared to its peers which limits its growth potential. Their competitors have increased their stock price by an average of 10% over the previous year which can be attributed to their willingness to expand to overseas markets, whereas McDonald's already has a stable presence in the markets their competitors are breaking into.²⁵ While this does reflect poorly on McDonald's in a bull market, since we predict an economic slowing, McDonald's vast market share and

brand recognition will enable it to produce revenues abroad while their competitors will be impacted more by U.S. revenues decreasing.

Earnings Analysis Comparison

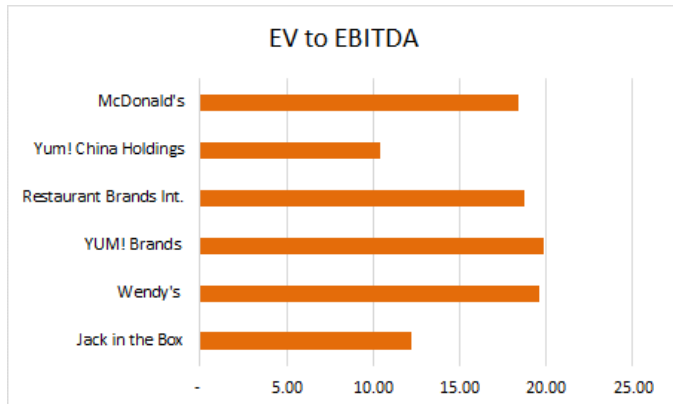
Earnings per share measures a company's profitability, and McDonald's is projected to have the highest EPS compared to its peers of 7.73.²² The company has the highest earnings compared to its peers, this is due to its stock price being larger than their peers which contributes to a lower P/E ratio. We believe that investors have not priced in an economic recession, an economic state in which, historically, McDonald's has seen increases in revenues due to its low cost-structure and diversified revenue stream. Furthermore, investors have been gravitating to high-growth stocks in this record bull market, so its competitors which are growing more rapidly have benefited from this investor sentiment. This has impacted value stocks in recent history, but when market conditions worsen, McDonald's will see an appreciation in share price due to investors switching to more stable companies with attractive dividends and a diversified revenue stream.



EV/EBITDA Comparison

EV/EBITDA is an important comparison because it shows how much a company is valued compared to the free cash flow it produces. McDonald's has the median EV/EBITDA of its comparable companies at 17.88. This shows that the company is neither over or under valued.²² The companies with higher ratios have been growing operations abroad at a faster pace than McDonald's in recent years, however, McDonald's still

has the dominant market share in the international market.²⁷ We believe that McDonald's is accurately valued as of current market conditions, but when the economic downturn hits, investors will invest in McDonald's due to its dominant market share and success overseas.



Porter's 5 Forces

Threat of Competition: High

The restaurant industry is highly saturated, and McDonald's competes with multiple name-brand fast-food chains as well as local restaurants for customers and market share. The quick-service segment's niche in the industry is providing low cost options with quick service. McDonald's in this aspect only competes with other fast food establishments and has the name brand recognition and market share to draw more customers when they are eating outside of their place of residence.

Threat of New Entrants: High

The restaurant industry has relatively low barriers to entry and requires very little initial capital to begin operations. New fast food restaurants can compete with large name company's due to low switching costs to consumers. Restaurants are structured based on company owned or franchised stores. Competitors can quickly gain market share through franchising.

Threat of Substitutes: High

There is no lack of substitutes in the food industry. Customers are able to choose between a vast number of upscale and artisanal restaurants, casual dining establishments, and grocery stores to purchase food. As consumers are becoming more health conscious, there is an increasing number of companies to fill this need.

McDonald's is subject to the effects of these new entrants that can compete on a quality over cost basis.

Bargaining Power of Suppliers: Moderate

The food industry has an abundant number of wholesale food suppliers as well as local farms in most geographic regions. Competition in the market prevents suppliers from being able to bargain prices. Some areas internationally are more restricted on the number of local suppliers and therefore allow for some degree of bargaining power. McDonald's 10-K refers to the potentiality of relying more on key suppliers in areas that have limited options for certain food and paper products.

Bargaining Power of Buyers: High

Consumer's purchasing choices determine the success of companies in the restaurant industry. In the quick-service segment there is an abundance of competitors allowing for greater buyer bargaining power. Companies in the industry are also driven by changes in consumer taste preferences and trends. McDonald's has remained a leader in the industry due to their cost-efficient structure and a wide array of menu items resulting in the company being impacted less by changes in consumer preferences.

Catalysts for Growth

Technology and Analytics:

Emerging technologies and analytics are significantly driving growth in the quick-service restaurant industry. A study from Lee Holman, lead retail analyst at IHL Consulting, shows that IT spending amongst restaurants is predicted to increase by 5.4% at the enterprise level and 5.3% at the store level compared to just 1% and 2% in historic industry averages. This uptick in technology spending is largely attributed to increases in digital ordering and delivery options as well as digital engagement and customized convenience initiatives. Business and customer analytics are at the forefront of industry strategic goals with 40% of restaurants claiming this as their lead objective in 2019. According to Hospitality Technology's 2019 Restaurant Technology Study, digital food orders have grown by 23% annually since 2013 and are expected to triple by 2020. The same study indicates that 52% larger companies, revenues over \$50 million, are focused on increasing data analytics measures in 2019, while smaller firms are directing their

focus on improving efficiency. Company IT expenditures are poised to better track customer data to increase a more personalized and convenient eating experience. McDonald's will be implementing these trends by incorporating digital kiosks for in-store orders and partnering with Uber Eats to expand their delivery platform.

International:

As domestic revenue growth has decreased in recent years for the quick-service restaurant industry, companies have shifted their focus on international markets due to higher growth opportunities. Most companies in the industry are smaller businesses that are limited to regional operations and serve a domestic customer base. However, larger businesses have expanded to overseas markets, particularly in Asia and South America that show promising growth. According to an article by Market Realist, in 2017, McDonald's accounted for 0.4% of global outlets in the informal eating out segment, but 7.1% of total segment sales. McDonald's international sales account for 64% of total revenues for its comparable companies. Yum! Brands Inc. is the only company that matches McDonald's in this metric followed by Burger King with only 40% of total sales being derived from international markets.

Company Analysis

Company Overview

McDonald's operates and franchises restaurants which serve local foods in more than 100 countries. The majority of franchised restaurants are operated under the conventional franchise structure, with a small percentage operating under the developmental license or affiliate structure. McDonald's restaurants are 93% franchise owned and this structure enables McDonald's to increase expansion due to entrepreneurial risk taking of their franchisees.³¹ McDonald's operates in 4 different business markets which are classified as: United States, International Lead Markets, High Growth Markets, and Foundational Markets.³¹

Corporate Strategy

McDonald's prides itself by having high-quality and consistent food no matter where they operate in the

world and this contributes to their customer loyalty and success internationally. Using the franchise model has enabled McDonald's to expand their operations, because most of the risk is placed upon the franchisee and not corporate. They also own the land that the franchisees operate on, and this enables them to collect rent and royalties which amount to 21.6% of their total revenue.³¹ McDonald's also relies on brand recognition to attract customers from all over the world. The "golden arches" are one of the most widely recognized symbols in the world, and they are a symbol of local tasty food at a low price. McDonald's has been trying to expand into the Asian and European markets due to the lack of presence in these countries and increased demand for American food abroad.³¹

Life Cycle

McDonald's has been a formidable presence in fast-food for decades. It is in a mature stage of its life cycle which means its sales are growing at a decreasing rate. Over the past 3 years, McDonald's has been experiencing decreased sales due to a shift in preferences of its typical consumer. The record economy has enabled consumers to increase spending on healthier food and fast-casual establishments.¹⁷ Most analysts expect McDonald's to increase its sales by 2.9% in 2020, and we agree with this estimate due to a projected economic downturn which will lead to consumers spending on cheaper food options. While overall sales are down, McDonald's has seen increased sales in its International Lead Markets due to increased demand for American food in these countries, and a global economic slowdown where McDonald's is the cheapest food available.³¹

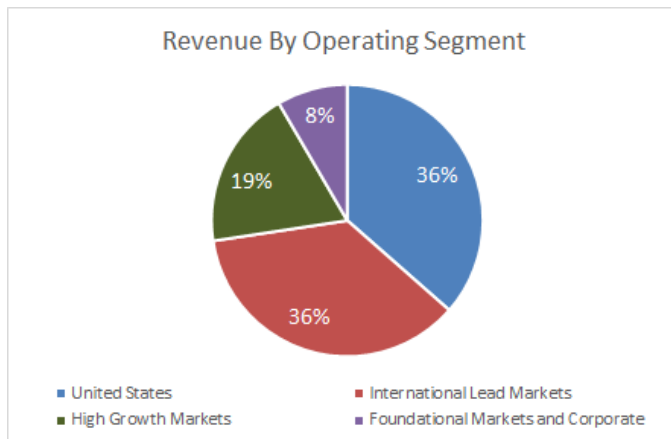
Financial Summary

McDonald's is in the middle of a systemwide restructuring of the company's business model. The company currently franchises out 93% of its stores and is looking to increase this margin by 2%. McDonald's believes a franchise-leveraged model will decrease risk while providing more steady streams of revenue and cash flows. Management projects positive same-store sales growth within their various geographic markets. Management predicts U.S. same-store sales to increase 2.5% in alignment with recent trends. Comparable sales projections for international lead and high growth segments are anticipated to increase 4%-6% in 2019.

Foundational markets are projected to have the highest same-store growth at 7%. In recent years, McDonald's has aggressively repurchased shares of common stock in an initiative to return cash to shareholders. The company has become increasingly debt-leveraged since 2015 and has been using this debt to buy back shares for its shareholders.

Operating Segments

McDonald's operates in four segments: U.S., International Lead Markets, High Growth Markets, and Foundational Markets and Corporate. McDonald's groups these regional markets based on opportunities for growth and consumer characteristics. Each segment focuses on different geographic regions. By differentiating segments geographically, management believes they can provide better experiences for their highly differentiated customer base and report sales in a way that reflects market differences.



U.S.

The U.S. segment is McDonald's largest segment and accounts for 36% of the company's revenues. In 2018 same-store sales increased 2.5% due to customer check growth and inflation, however guest count decreased 2.2%. McDonald's has focused on increasing customer experience through their Experience of The Future initiative by converting 4,500 to this model. We project McDonald's total revenues from the U.S. segment to decrease slightly in 2019 due to refranchising, followed by an increase of 6% in 2020 mainly due to U.S. economic slowdown. We project total revenues from this segment to have varying increases before reaching a continuing value growth rate of 3% in 2024.

International Lead Markets

The International Lead Markets segment is comprised of established regions including Australia, Canada, France, Germany, and the United Kingdom and related markets. This segment accounts for an additional 36% of total revenues. In 2018 same-store sales increased 5.8% and guest counts increased 2.4%. The increase in same-store sales was reflected for all markets in the segment. McDonald's plans to continue implementing the EOTF initiative in these markets as they are the most comparable with the U.S. According to the company's 10-K, "well over half" of customers in many European markets ordered through kiosks, signaling positive customer feedback to the new ordering systems. We project McDonald's total revenue from international lead markets to increase slightly in 2019 followed by 6.9% growth in 2020 largely due to an increase in franchised store counts. Additionally, we project total revenues to increase by varying amounts before reaching a continuing value growth rate of 4% in 2024.

High Growth Markets

High growth markets are classified as markets with the most optimistic growth. The segment is comprised of: China, Italy, Korea, the Netherlands, Spain, Russia, Poland, Switzerland and related markets. This segment accounted for 19% of sales in 2018. Same-store sales growth for this segment 4.1% and guest counts increased 1.8% in 2018. In 2017 McDonald's franchised all of its stores in China and Hong Kong, sacrificing revenues in exchange for steady future revenues and cash flows as well as increased expansion through franchising. McDonald's plans to increase expansion in these high growth markets through franchising due to higher market volatility. Franchising will allow McDonald's to access a greater portion of these markets and provide steady revenues through rent and royalty payments. We project McDonald's total revenues from high growth markets to increase by 2% in 2019 followed by a 2% decrease in 2020. Additionally, we project continual revenue growth from high growth markets before reaching a continuing value growth rate of 4.5% in 2024.

Foundational Markets and Corporate

Foundational markets include all other foreign markets as well as corporate. Revenues from this segment

accounted for 8% of total company revenues. In 2018 same-store sales increased by 7.1% and same-store guest counts increased 1.5%. Foundational markets are comprised of 80 countries that McDonald's is not established in. We project McDonald's total revenues to decrease by 2% in 2019 following by various growth changes until reaching a continuing value of 2% in 2024.

Market for Products

McDonald's sells their products in 110 countries around the world with 36% of their sales coming from the United States, and another 36% coming from their International Lead Markets which are composed of Australia, Canada, France, Germany, and the United Kingdom.³¹ Other international markets account for the remaining 28% of sales with the majority stemming from Europe and Asia. McDonald's also has 17% of their revenues coming from emerging markets, and the only competing comparable in the industry is YUM! Brands Inc. which have 20% of their revenues come from emerging markets.²⁷ While YUM! does have a larger presence in emerging markets, their share is primarily concentrated in Asia which McDonald's also has a strong presence in.

Foreign Sales and Earnings

McDonald's generates 64% of their revenues internationally. This diversification minimizes overall risk, but still leaves the company vulnerable to currency exchange rates.³¹ To mitigate its risk, McDonald's uses forward exchange contracts to hedge its risk from foreign currency fluctuations. McDonald's benefits when there is a weaker U.S. dollar because foreign sales converted to U.S. dollars are worth more. We project the U.S. dollar to get stronger in the coming years due to the global economic slowdown and negative interest rates abroad which we project will translate to weaker foreign currency translations for McDonald's.

Significant Customers

McDonald's does not rely on any specific customer and serves around 69 million customers daily.³¹ McDonald's expects their customer base to increase in the future due to their expansion efforts in Asia, Europe, and Latin America. This vast customer base reduces McDonald's risk and makes them one of the most stable companies in the world. McDonald's tailors their menu to each country's specific tastes. This tailored menu allows

McDonald's to be popular all over the world and enables them to not be reliant on a specific customer base.

Suppliers and Distribution

McDonald's uses a Food Safety Advisory Council composed of the company's internal food safety experts to monitor every distribution center which promotes consistent standards and quality assurance.³¹ Having a diverse supply chain with over 100 suppliers across the world enables McDonald's to decrease its costs by not having to spend as much money on shipping, and keeps costs down due to suppliers not having as much bargaining power.³¹ This increase in supply chain logistics has made McDonald's decrease its costs over time, and enables them to be less reliant on a small amount of suppliers which eliminates shortages.

Government Regulation

Having operations in 110 countries subjects McDonald's to many government regulations. There has been an increased focus on environmental matters from governments, and many governments have implemented a tax on plastics which is used in a lot of McDonald's packaging.³¹ Being more environmentally friendly also impacts their suppliers, because they now face more regulations that could impact the price of their goods. More governments have implemented a higher minimum wage and employee benefits, and this has impacted McDonald's margins due to it costing more to operate their stores.³¹ McDonald's has stayed ahead of these regulations, but management warns that they have the potential to limit growth and expansion into foreign markets in the future.³¹

Company Structure and Debt Leverage

McDonald's debt leverage is the biggest weakness of the company, but it is the most financially sound amongst its competitors. With an EBITDA margin of 54% McDonald's is able to generate strong cash flows to pay off its debt, so its BBB+ credit rating is not as worrisome.²⁷ They also have an interest coverage ratio of 8.85 and they do not have any debt maturing until 2023 so they are not in any danger of a credit crunch in the near future.²⁷

McDonald's has had negative shareholder's equity for the past 3 years due to their record share repurchasing. Historically, McDonald's has used debt and strong cash

flows from operations as its primary source of liquidity.³¹ Due to recent technology pushes, McDonald's uses its cash to invest in new properties and equipment. The company's other uses of liquidity have typically been dividends and share repurchases. McDonald's will stop buying back stock in 2019 and will instead use that capital to pay down debt. Its dividends will remain at a steady state for the foreseeable future due to McDonald's priding itself in being a value stock with excellent dividend payments.³¹

Key Investment Positives/Negatives

Positives

- McDonald's operates internationally and has a diverse revenue stream which creates stability in economic downturn in any of the regions of operations. McDonald's also has great customer loyalty and a great brand image because of their ability to have great quality control and uniform taste all over the world. Their menu is also specifically tailored to each country, and this has made it possible for them to grow into foreign markets.
- The low-cost menu attracts consumers in time of an economic downturn due to consumers having less disposable income. With a projected recession, McDonald's will attract customers that might have typically opted for fast-casual places or sit-down restaurants.
- McDonald's uses the franchise model to operate its business and this enables them to grow in new markets. Furthermore, 21% of its revenues coming from rent and royalty fees charged to their franchisees, and this makes McDonald's a De facto real estate company.
- McDonald's has been at the forefront of investing into technology in the fast-food industry. Its ability to integrate kiosks and partner with Uber Eats has made it more attractive to consumers by staying on top of the delivery and mobile ordering trends.

Negatives

- McDonald's has been buying back shares at a record pace in previous years. Their stock price has increased substantially due to the buybacks, but they are going to stop buying back shares in

2019 which could lead to a decrease in stock price.

- McDonald's has a BBB+ debt rating which limits its ability to allocate its capital to other sources. If the company falls below a BBB rating, McDonald's would have to access debt from junk markets which would be more expensive. This will limit McDonald's ability to buy back shares and increase its dividend in future years because all the liquidity has to go to paying down debt.
- McDonald's has been adversely affected in recent years due to consumers wanting healthier foods. This has influenced McDonald's into providing healthier menu options in recent years, but McDonald's has not gained market share in this due to health-conscious consumers not being its target market.

Valuation Analysis

Methods of Valuation

Our target stock price was calculated by considering the various financial, economic, and industry specific factors that drive McDonald's equity value in our forecasts. We analyzed and projected trends in the restaurant industry that would impact our financial forecasts. We used four valuation methodologies: discounted cash flow, economic profit, dividend discount model, and relative valuation.

Discounted Cash Flow and Economic Profit Analysis

We analyzed McDonald's operating segments to determine our growth forecasts. We believe the discounted cash flow model is the most accurate model to capture McDonald's intrinsic value because we were able to dissect the various operating segments to more accurately analyze and project its financials. Our discounted cash flow and economic profit analysis calculated our target stock price of \$255.58. When constructing the discounted cash flow model, we forecasted our free cash flow for six years, and then calculated the continuing value to calculate McDonald's growth into perpetuity. For our continuing value, we used a constant growth rate of 2.00% which we believed best projected McDonald's growth into the future most

accurately. We then discounted the continuing value and free cash flows by the weighted average cost of capital to find the present value of the cash flows and continuing value. Once the present value was found, we subtracted their non-operating assets to get the value of equity which we then divided by the shares outstanding to get McDonald's intrinsic value per share. This intrinsic value per share was the end of year price target, so we then had to adjust for the portion of the year that has already occurred. This valuation is a rather large premium to their current stock price of \$194.28, but we believe this is due to analysts underestimating McDonald's revenues into the future due to an upcoming recession. Furthermore, we are buying McDonald's at a discount due to the markets reacting to McDonald's recent earnings miss which was the first one in two years, and the firing of their CEO and head of human resources in recent history.

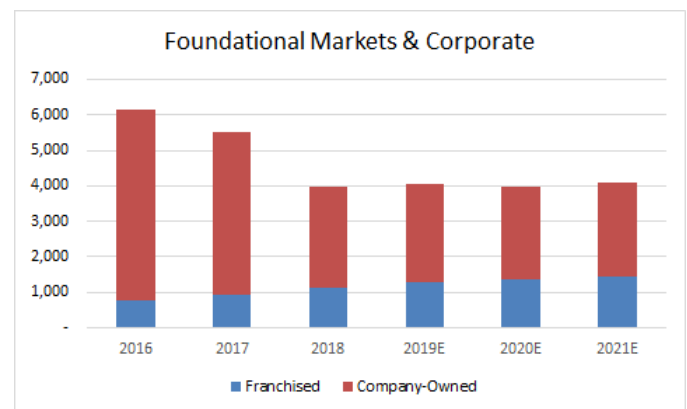
Dividend Discount Model

When using the dividend discount model, we projected a target price of \$290.85, but we believe that the dividend discount model is a very inaccurate way of projecting McDonald's stock price. We are projecting our dividends to grow at 1% every year in our model, and this is because they have a lot of debt to pay down so they cannot allocate the cash to dividends. McDonald's pays a 2.58% dividend which is the highest amongst their comparable companies, and they have had negative shareholder's equity for the past three years. Their shareholder's equity is only projected to turn positive in 2023, which is the year before the continuing value. It is for these reasons that we believe the dividend discount model to be an inaccurate projections of McDonald's equity valuation.

Revenue Decomposition

We decided to break McDonald's revenues down and forecast them based on their four operating segments: United States, International Lead Markets, High Growth Markets, and Foundational Markets and Corporate, as well as franchise versus corporate owned store revenues. Each segment has varying revenue growth based on market characteristics, regional trends, and regional preferences. Revenues from corporate and franchised stores also vary greatly due to the nature of the revenue

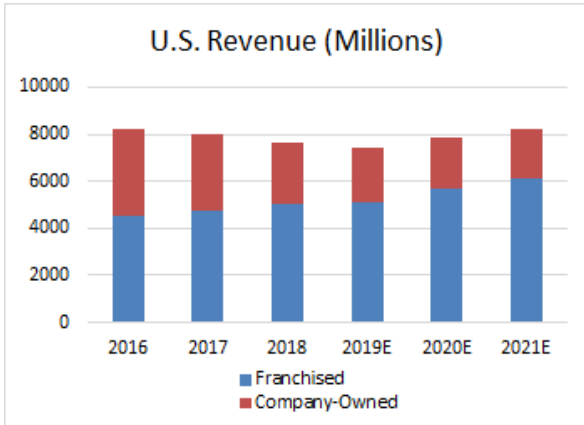
from each. Corporate-owned store revenues are derived from sales of food and drinks, while franchised revenues are derived from rent and royalty payments. Revenues are greatly impacted by the ratio of company owned to franchised stores. Company owned stores generate larger revenues and incur far greater operating costs, resulting in far lower margins than franchised stores. Since McDonald's plans to continue refranchising company owned stores to franchised stores, we project revenue growth of -0.77% in 2019, which is slightly offset by expansion in total number of stores. By our continuing value year of 2024, we predict that McDonald's will be nearing the end of their refranchising efforts allowing for stable revenue growth of 3.47%. These predictions were made by weighting same-store revenue growth amongst franchised stores and company owned stores within each operating segment.



United States Revenue Forecast

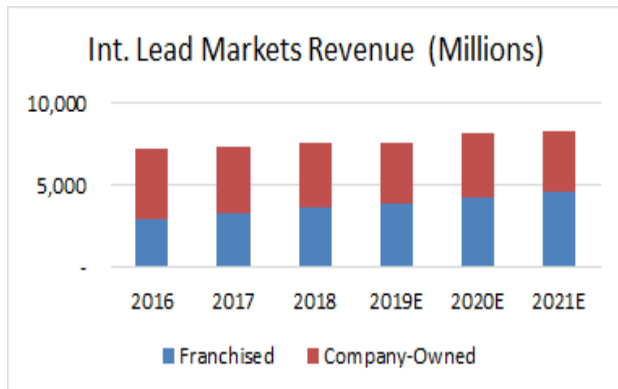
McDonald's revenues in the United States have steadily declined in the United States primarily due to refranchising, however same-store revenues have seen growth amongst company owned and franchised stores. We project company-owned store counts to decrease an additional 13.5%, due to refranchising, and same-store sales to increase by 1% in 2019. Additionally, we project franchised store counts to increase 1.5% and same-store sales to increase by 1% in 2019. Our forecasted weighted average of company versus franchised restaurant store counts and same-store sales result in a projected revenue decrease of 2.75% in 2019. By our continuing value year of 2024. We project total revenues to increase by 3.02% each year in the United States. This reversal to positive revenue growth is largely due to McDonald's nearing the end of their refranchising efforts and

implementing new technologies that create a more customer-centric experience.



International Lead Markets Revenue Forecast

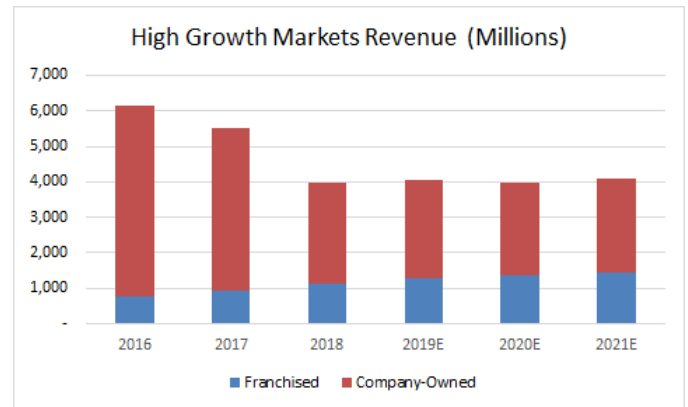
McDonald’s revenues in international lead markets have seen low constant growth constant growth in recent years. Same-store sales have seen very high growth in recent years, however these revenues have been offset by refranchising. We project company-owned store counts to decrease 6.33% and same-store sales to increase 2% in 2019. Additionally, we project franchised store counts to increase 2% and same-store revenues to increase 3% in 2019. These forecasts result in a projected revenue increase of 0.1%. This projection reflects the revenue sensitivity that results from refranchising. Beginning in 2024 we project revenues from international lead markets to increase by 4.03% each year.



High Growth Markets Revenue Forecast

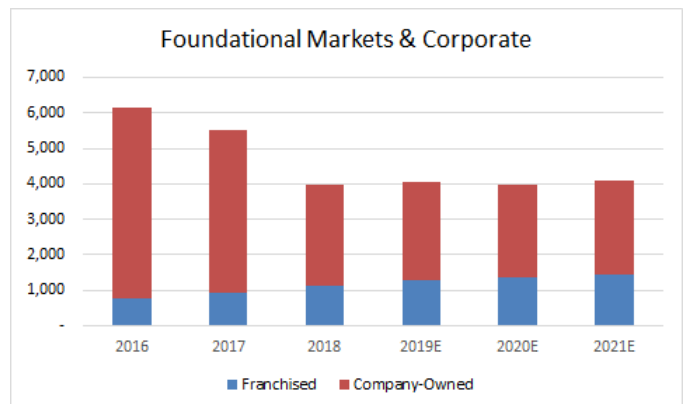
The high growth markets segment is defined as markets that have the highest potential of growth at the expense of increased volatility. In recent years total revenues in high growth markets have decreased due to refranchising and volatile same-store sales. In 2018

McDonald’s sold all its stores in China and Hong Kong, resulting in a significant revenue decrease in 2018. In 2019 we project franchised store counts to increase 8% and same-store sales to increase 5%. We project company-owned store counts to decrease 3.76% and same-store sales to increase 1%. This results in total projected revenues to increase 1.83% in 2019. Due to expansion and promising growth we project continuing revenue growth of 4.65% beginning in 2024 for the high growth markets segment.



Foundational Markets and Corporate Forecast

McDonald’s revenues in foundational markets and corporate have seen decreasing revenues in recent years, although same-store sales have been positive. This is largely due to McDonald’s refranchising initiative resulting in massive decrease in company-owned stores. We project franchised store counts to increase 2.5% and same-store sales to increase 2% in 2019. Additionally, we project company-owned store counts to decrease 22.5% and same-store sales to increase 2% in 2019. Our team forecasts continuing value growth for this segment at 1.67%. McDonald’s initiative to refranchise nearly all its company-owned stores in this segment is the most significant driver of low revenue continuing value growth.



Cost of Goods Sold as a Percentage of Sales

Our Cost of Goods Sold were based on McDonald's five-year historical average, but with a slight decrease which we obtained from management's indication that further automation and increased supply chain would lower costs. Management's projection coupled with its five-year historical average got us to a Cost of Goods Sold percentage of sales of 45%.

Selling General and Administrative Expense (SG&A)

We used a constant 12% of sales to project our SG&A expense, and we based this off the SG&A expense increasing historically and management projecting the increase to decrease soon due to the implementation of technology. However, McDonald's management also indicated that they might have to pay their employees more in the future due which is why we chose a constant rate of 12% of sales which is a slight increase from their current percentage.

Capital Expenditures

McDonald's relies on capital expenditures to expand into new markets through opening stores and increase sales through reinvestments in existing stores. In 2019 McDonald's capital expenditures budget plans to spend \$1.9 billion. \$1.2 billion will be allocated to U.S. businesses. Nearly two-thirds of this U.S. budget will be used on about 2,000 Experience of the Future Projects. The remaining \$700 million will be largely allocated toward opening nearly 1,000 restaurants globally. Our team forecasted capital expenditures in alignment with management guidelines, and projected capital expenditures to grow proportional to depreciation and expenditures related to EOTF and technology.

Weighted Average Cost of Capital (WACC)

We calculated the Weighted Average Cost of Capital for McDonald's to be 4.26%. We arrived at this number by using a 4.69% cost of equity and an after-tax cost of debt of 2.70%. This Weighted Average Cost of Capital was used to discount our free cash flows in both the Economic Profit and Discounted Free Cash Flow models. McDonald's has a Weighted Average Cost of Capital Compared to its peers because they have strong cash

flows to pay down their debt despite them having a BBB+ credit rating.

Cost of Debt

McDonald's has a very low cost of debt due to their strong cash flows. To get this forecast we used a McDonald's 30-year bond which is the longest bond McDonald's has. The yield on this bond was 3.514% and McDonald's marginal tax rate of 23.2% which brought our after-tax cost of debt to be 2.70%.

Cost of Equity

We arrived at McDonald's cost of equity by using the Capital Asset Pricing Model. We used an unadjusted raw beta of 0.56 which we got off Bloomberg and a risk-free rate of 1.84% which is the 10-year treasury yield. Our market risk premium of 5.09% was obtained from Aswath Damodaran, and this is the excess of the average geometric returns of the stock market over the risk-free rate.

Sensitivity Analysis

CV ROIC vs. WACC

When projecting future free cash flows these variables are very important, and we compared them to see if they are affecting our cash flows significantly. We can see that change in WACC is especially sensitive with a change in 0.25% impacting the stock price by \$67.77, and this is due to WACC affecting both the future free cash flows and the terminal value. On the other hand, a 0.25% change in CV ROIC impacts the stock price by \$0.79 due to it being a smaller part in calculating the capital structure.

Beta vs. Risk Premium

We compared these variables because they are two of the three main points in the cost of equity calculation. The price was not very sensitive to both variables because McDonald's has such a low beta of 0.56, and this low beta limits the volatility of the stock despite the large weight of equity in the capital structure at 78.51%. A change in the beta of 0.05 changes the stock price \$0.53 while a change in the equity risk premium of 0.25% changes the stock \$0.29.

Marginal Tax Rate vs. Pre-Tax Cost of Debt

These two variables have a large impact on the DCF and EP models, and it is for this reason why we analyzed them. The marginal tax rate impacts net income and the pre-tax cost of debt impacts the WACC calculation because it is used to calculate the cost of debt. An increase in the marginal tax rate of 0.1% will sway the stock price \$0.46, while the pre-tax cost of debt impacts it by \$0.59.

Revenue Growth vs. COGS as a Percentage of Sales

We projected these two metrics because they are very important when calculating DCF and EP due to them eventually flowing into NOPLAT. The COGS percentage is especially sensitive, and when you change it by 0.10% the stock price changes by \$1.69 as supposed to the revenue growth which changes the stock price by \$0.97 anytime it changes by 0.10%

Risk-Free Rate vs. CV Growth

We sensitized these two variables to how sensitive our growth into perpetuity is to changes on the interest rate of the U.S. 10-year bond. We can see that when the CV growth rate changes by 0.10 that the stock price increases by \$10.36 which is exponentially larger than the \$0.20 increase in price when the risk-free rate changes.

Target Price

We arrived at our target price \$236 per share for McDonald's by projecting a slowly increasing growth of revenues and conservative operating margins. We used these conservative assumptions to make sure to not over-value the stock. While our target price is 21% higher than the current stock price, we believe this to be accurate due to McDonald's stock being valued at \$210 less than a month ago. This substantial drop in price was due to McDonald's missing their quarterly earnings estimate for the first time in 2 years, and a scandal that made their CEO, Steve Easterbrook, leave along with their head of Human Resources. These two factors are the markets reacting to news instead of their intrinsic worth leading to McDonald's being valued at a discount.

Important Disclaimer

This report was created by students enrolled in the Security Analysis (6F:112) class at the University of Iowa. The report was originally created to offer an internal investment recommendation for the University of Iowa Krause Fund and its advisory board. The report also provides potential employers and other interested parties an example of the students' skills, knowledge and abilities. Members of the Krause Fund are not registered investment advisors, brokers or officially licensed financial professionals. The investment advice contained in this report does not represent an offer or solicitation to buy or sell any of the securities mentioned. Unless otherwise noted, facts and figures included in this report are from publicly available sources. This report is not a complete compilation of data, and its accuracy is not guaranteed. From time to time, the University of Iowa, its faculty, staff, students, or the Krause Fund may hold a financial interest in the companies mentioned in this report.

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McDonald's

Revenue Decomposition

<i>Fiscal Years Ending Dec. 31</i>	2,016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
Company-operated Revenues (Millions)									
United States	3,743	3,260	2,665	2,328	2,221	2,088	2,088	2,087	2,150
% Change		-12.88%	-18.27%	-12.63%	-4.60%	-5.96%	-0.04%	-0.01%	3.02%
Int'l Lead Markets	4,279	4,080	3,962	3,785	3,917	3,708	3,728	3,879	4,035
% Change		-4.64%	-2.90%	-4.46%	3.49%	-5.33%	0.53%	4.04%	4.03%
High Growth Markets	5,378	4,592	2,848	2,768	2,625	2,635	2,627	2,351	2,408
% Change		-14.62%	-37.98%	-2.80%	-5.18%	0.40%	-0.32%	-10.49%	2.42%
Foundational Markets and Corporate	1,896	787	539	426	439	466	400	347	259
% Change		-58.49%	-31.55%	-20.95%	3.17%	6.08%	-14.23%	-13.12%	-25.55%
TOTAL	15,295	12,719	10,013	9,307	9,202	8,898	8,842	8,664	8,852
% Change		-16.84%	-21.28%	-7.05%	-1.13%	-3.30%	-0.63%	-2.01%	2.16%
Franchised Revenues									
United States	4,510	4,746	5,001	5,127	5,676	6,109	6,605	6,538	6,735
% Change		5.23%	5.38%	2.52%	10.70%	7.64%	8.12%	-1.02%	3.02%
Int'l Lead Markets	2,945	3,260	3,639	3,823	4,214	4,535	4,765	4,957	5,157
% Change		10.71%	11.60%	5.06%	10.00%	12.00%	8.00%	2.00%	2.00%
High Growth Markets	783	942	1,141	1,294	1,350	1,461	1,594	1,757	1,891
% Change		20.30%	21.15%	13.40%	-10.00%	-15.00%	-13.00%	5.00%	5.00%
Foundational Markets and Corporate	1,089	1,154	1,232	1,313	1,400	1,485	1,503	1,571	1,667
% Change		5.91%	6.80%	6.60%	-5.00%	-8.00%	-10.00%	2.00%	2.00%
TOTAL	9,327	10,102	11,013	11,557	12,640	13,590	14,467	14,824	15,451
% Change		8.31%	9.02%	4.94%	9.38%	7.52%	6.45%	2.47%	4.23%
Total Revenues									
United States	8,253	8,006	7,666	7,455	7,896	8,198	8,693	8,625	8,886
% Change		-2.98%	-4.25%	-2.75%	5.92%	3.82%	6.04%	-0.78%	3.02%
Int'l Lead Markets	7,223	7,340	7,600	7,608	8,131	8,244	8,493	8,836	9,192
% Change		1.62%	3.54%	0.10%	6.88%	1.39%	3.02%	4.04%	4.03%
High Growth Markets	6,161	5,533	3,989	4,062	3,975	4,096	4,221	4,108	4,299
% Change		-10.19%	-27.91%	1.83%	-2.14%	3.04%	3.05%	-2.66%	4.65%
Foundational Markets and Corporate	2,985	1,941	1,771	1,739	1,840	1,951	1,903	1,918	1,925
% Change		-34.99%	-8.76%	-1.78%	5.78%	6.08%	-2.50%	0.83%	1.67%
TOTAL	24,622	22,820	21,025	20,863	21,842	22,488	23,309	23,488	24,302
% Change		-7.32%	-7.87%	-0.77%	4.69%	2.96%	3.65%	0.77%	3.47%
Total Restaurants									
U.S.	14,155	14,036	13,914	14,018	14,299	14,728	15,022	15,172	15,324
% Change		-0.84%	-0.87%	0.75%	2.00%	3.00%	2.00%	1.00%	1.00%
Int'l Lead Markets	6,851	6,921	6,987	7,057	7,304	7,377	7,488	7,637	7,714
% Change		1.02%	0.95%	1.00%	3.50%	1.00%	1.50%	2.00%	1.00%
High Growth Markets	5,552	5,884	6,305	6,683	6,951	7,159	7,231	7,375	7,597
% Change		5.98%	7.15%	6.00%	4.00%	3.00%	1.00%	2.00%	3.00%
Foundational Markets and Corporate	10,341	10,400	10,649	10,862	11,025	11,245	11,302	11,471	11,689
% Change		0.57%	2.39%	2.00%	1.50%	2.00%	0.50%	1.50%	1.90%
TOTAL	36,899	37,241	37,855	38,621	39,578	40,509	41,042	41,656	42,324
% Change		0.93%	1.65%	2.02%	2.48%	2.35%	1.32%	1.50%	1.60%
Franchised Restaurants									
U.S.	13,023	13,194	13,218	13,417	13,752	14,233	14,518	14,663	14,810
% Change		1.31%	0.19%	1.50%	2.50%	3.50%	2.00%	1.00%	1.00%
Int'l Lead Markets	5,755	6,021	6,149	6,272	6,522	6,685	6,819	6,956	7,025
% Change		4.63%	2.11%	2.00%	4.00%	2.50%	2.00%	2.00%	1.00%

High Growth Markets	2,665	4,766	5,233	5,652	6,019	6,260	6,385	6,641	6,873
% Change		78.84%	9.80%	8.00%	6.50%	4.00%	2.00%	4.00%	3.50%
Foundational Markets and Corporate	9,721	10,192	10,436	10,697	10,863	11,080	11,324	11,494	11,723
% Change		4.85%	2.39%	2.50%	1.55%	2.00%	2.20%	1.50%	2.00%
TOTAL	31,163	34,173	35,036	36,037	37,156	38,259	39,046	39,753	40,431
% Change		9.66%	2.53%	2.86%	3.11%	2.97%	2.06%	1.81%	1.71%

Company-Owned Restaurants

U.S.	1,132	842	696	602	547	494	504	509	514
% Change		-25.63%	-17.39%	-13.50%	-9.15%	-9.58%	2.00%	1.00%	1.00%
Int' Lead Markets	1,096	900	838	785	781	691	668	682	689
% Change		-17.92%	-6.81%	-6.33%	-0.49%	-11.52%	-3.33%	2.00%	1.00%
High Growth Markets	2,887	1,118	1,072	1,031	931	899	846	735	724
% Change		-61.28%	-4.12%	-3.76%	-9.70%	-3.46%	-5.96%	-13.10%	-1.52%
Foundational Markets and Corporate	620	208	213	165	162	165	143	121	87
% Change		-66.48%	2.39%	-22.50%	-1.74%	2.00%	-13.36%	-15.65%	-28.42%
TOTAL	5,736	3,068	2,819	2,584	2,422	2,250	1,996	1,903	1,892
% Change		-46.52%	-8.11%	-8.35%	-6.26%	-7.08%	-11.30%	-4.64%	-0.59%

Revenue Per Company-Owned Restaurant

U.S	3.31	3.87	3.83	3.87	4.06	4.22	4.14	4.10	4.18
% Change		17.14%	-1.07%	1.00%	5.00%	4.00%	-2.00%	-1.00%	2.00%
Int'l Lead Markets	3.90	4.53	4.72	4.82	5.01	5.36	5.58	5.69	5.86
% Change		16.18%	4.20%	2.00%	4.00%	7.00%	4.00%	2.00%	3.00%
High Growth Markets	1.86	4.11	2.66	2.68	2.82	2.93	3.11	3.20	3.33
% Change		120.48%	-35.31%	1.00%	5.00%	4.00%	6.00%	3.00%	4.00%
Foundational Markets and Corporate	3.06	3.78	2.53	2.58	2.71	2.82	2.79	2.87	2.99
% Change		23.82%	-33.15%	2.00%	5.00%	4.00%	-1.00%	3.00%	4.00%
TOTAL	12.13	16.30	13.74	13.95	14.60	15.34	15.61	15.86	16.36
% Change		34.39%	-15.68%	1.53%	4.65%	5.03%	1.81%	1.58%	3.12%

Revenue Per Franchised Restaurant

U.S	0.35	0.36	0.38	0.38	0.41	0.43	0.45	0.45	0.45
% Change		3.86%	5.18%	1.00%	8.00%	4.00%	6.00%	-2.00%	2.00%
Int'l Lead Markets	0.51	0.54	0.59	0.61	0.65	0.68	0.70	0.71	0.73
% Change		5.81%	9.29%	3.00%	6.00%	5.00%	3.00%	2.00%	3.00%
High Growth Markets	0.29	0.20	0.22	0.23	0.22	0.23	0.25	0.26	0.28
% Change		-32.73%	10.34%	5.00%	-2.00%	4.00%	7.00%	6.00%	4.00%
Foundational Markets and Corporate	0.11	0.11	0.12	0.12	0.13	0.13	0.13	0.14	0.14
% Change		1.01%	4.30%	4.00%	5.00%	4.00%	-1.00%	3.00%	4.00%
TOTAL	1.26	1.21	1.31	1.34	1.41	1.47	1.54	1.56	1.61
% Change		-4.11%	7.78%	2.84%	5.11%	4.46%	4.14%	1.55%	2.97%

McDonald's
Income Statement

<i>Fiscal Years Ending Dec. 31</i>	2016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
Sales	24,621.90	22,820.40	21,025.20	20,863.25	21,841.69	22,488.19	23,308.91	23,487.86	24,302.38
Growth	-3.11%	-7.32%	-7.87%	-0.77%	4.69%	2.96%	3.65%	0.77%	3.47%
COGS excluding D&A	12,900.70	10,836.20	8,757.20	9,388.46	9,719.55	9,894.80	10,139.38	10,099.78	10,328.51
Depreciation	1,391.00	1,228.00	1,303.00	1,451.51	1,489.64	1,519.79	1,548.87	1,593.73	1,628.28
Amortization of Intangibles	126.00	136.00	179.00	139.89	131.50	123.61	116.19	109.22	102.67
Gross Income	10,204.70	10,620.80	10,786.00	11,474.79	12,122.14	12,593.38	13,169.54	13,388.08	13,973.87
SG&A Expense	2,384.50	2,231.30	2,200.20	2,503.59	2,621.00	2,698.58	2,797.07	2,818.54	2,916.29
EBIT (Operating Income)	7,820.20	8,389.50	8,585.80	8,971.20	9,501.14	9,894.80	10,372.47	10,569.54	11,057.58
Other Income (Expense)	182.60	142.80	264.00	20.86	21.84	22.49	23.31	23.49	24.30
Interest Expense	884.30	920.80	980.00	1,091.99	1,154.46	1,118.18	1,056.23	1,018.31	973.92
Unusual Expense - Net	311.30	(771.30)	209.20	219.06	229.34	236.13	244.74	246.62	255.17
Pretax Income	6,866.00	8,573.50	7,816.10	7,681.01	8,139.18	8,562.98	9,094.81	9,328.09	9,852.79
Income Taxes	2,179.50	3,381.20	1,891.80	1,781.99	1,888.29	1,986.61	2,109.99	2,164.12	2,285.85
Net Income	4,686.50	5,192.30	5,924.30	5,899.02	6,250.89	6,576.37	6,984.81	7,163.97	7,566.94
Per Share									
EPS (recurring)	5.69	5.70	7.73	7.56	7.83	8.16	8.59	8.74	9.15
Total Shares Outstanding	819.30	794.10	767.10	794.49	802.08	809.45	816.62	823.58	830.35
Weighted Average Shares Outstanding	863.05	806.70	780.60	780.79	798.28	805.77	813.04	820.10	826.97
Dividends per Share	3.61	3.83	4.19	4.23	4.27	4.32	4.36	4.40	4.45

All figures in millions of U.S. Dollar except per share items.

McDonald's
Balance Sheet

<i>Fiscal Years Ending Dec. 31</i>	2016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
Assets									
Cash Only	1,223	2,464	866	731	1,689	2,124	3,501	4,639	6,323
Accounts Receivables, Net	1,474	1,976	2,442	2,115	2,214	2,279	2,363	2,381	2,463
Inventories	59	59	51	97	102	105	109	110	113
Other Current Assets	2,092	828	695	1,007	1,054	1,086	1,125	1,134	1,173
Total Current Assets	4,849	5,327	4,053	3,950	5,059	5,594	7,098	8,264	10,073
Net Property, Plant & Equipment	21,258	22,448	22,843	23,269	23,745	24,249	24,798	25,318	25,877
Property, Plant & Equipment - Gross	34,443	36,626	37,194	39,071	41,037	43,061	45,159	47,273	49,460
Accumulated Depreciation and Ammortization	13,186	14,178	14,351	15,802	17,292	18,812	20,361	21,954	23,583
LT Investment - Affiliate Companies	726	1,086	1,203	1,104	1,063	1,023	1,000	1,000	1,026
Intangible Assets	2,337	2,380	2,332	2,192	2,060	1,937	1,820	1,711	1,608
Deferred Tax Assets	804	868	1,219	498	528	555	590	605	639
Other Assets	1,051	1,695	1,162	1,007	1,054	1,086	1,125	1,134	1,173
Total Assets	31,024	33,804	32,811	32,020	33,510	34,444	36,431	38,031	40,396
Liabilities & Shareholders' Equity									
ST Debt & Curr. Portion LT Debt	77	-	-	6	14	13	13	12	12
Accounts Payable	756	925	1,208	836	911	1,008	1,071	1,016	1,068
Income Tax Payable	267	266	228	215	228	240	255	261	276
Other Current Liabilities	2,368	1,700	1,537	1,956	2,048	2,108	2,185	2,202	2,278
Accrued Payroll	1,159	1,146	987	1,522	1,593	1,640	1,700	1,713	1,773
Miscellaneous Current Liabilities	1,209	554	551	434	454	468	485	489	506
Total Current Liabilities	3,468	2,891	2,974	3,013	3,200	3,369	3,524	3,491	3,634
Long-Term Debt	25,879	29,536	31,075	32,853	31,821	30,058	28,979	27,715	26,577
Deferred Tax Liabilities	1,817	1,119	1,216	1,173	1,228	1,264	1,311	1,321	1,366
Other Liabilities	2,064	3,525	3,805	3,129	3,276	3,373	3,496	3,523	3,645
Total Liabilities	33,228	37,072	39,070	40,169	39,525	38,065	37,309	36,050	35,223
Common Equity	(2,204)	(3,268)	(6,258)	(8,149)	(6,015)	(3,620)	(878)	1,981	5,173
Common Stock/Additional Paid-In Capital	6,775	7,089	7,393	7,695	7,998	8,301	8,603	8,906	9,209
Retained Earnings	46,223	48,326	50,487	53,082	55,921	59,019	62,458	66,011	69,900
Cumulative Translation Adjustment/Unrealized For. Exch. Gain	(2,909)	(1,972)	(2,425)	(2,425)	(2,425)	(2,425)	(2,425)	(2,425)	(2,425)
Other Appropriated Reserves	(184)	(207)	(184)	(172)	(179)	(185)	(186)	(181)	(181)
Treasury Stock	(52,109)	(56,504)	(61,529)	(66,329)	(67,329)	(68,329)	(69,329)	(70,329)	(71,329)
Total Shareholders' Equity	(2,204)	(3,268)	(6,258)	(8,149)	(6,015)	(3,620)	(878)	1,981	5,173
Total Liabilities & Shareholders' Equity	31,024	33,804	32,811	32,020	33,510	34,444	36,431	38,031	40,396

All figures in millions of U.S. Dollar except per share items.

McDonald's*Cash Flow Statement*

<i>Fiscal Years Ending Dec. 31</i>	2016	2017	2018
Operating Activities			
Net Income / Starting Line	4,687	5,192	5,924
Depreciation, Depletion & Amortization	1,517	1,363	1,482
Depreciation and Depletion	1,391	1,228	1,303
Amortization of Intangible Assets	126	136	179
Deferred Taxes	(539)	(36)	103
Other Funds	228	12	(70)
Changes in Working Capital	167	(981)	(473)
Receivables	(159)	(341)	(479)
Accounts Payable	90	(60)	129
Income Taxes Payable	170	(396)	(33)
Other Accruals	38	(146)	(87)
Other Assets/Liabilities	28	(37)	(2)
Net Operating Cash Flow	6,060	5,551	6,967
Investing Activities			
Capital Expenditures	(1,821)	(1,854)	(2,742)
Net Assets from Acquisitions	(110)	(77)	(102)
Sale of Fixed Assets & Businesses	1,059	2,739	691
Purchase/Sale of Investments	-	-	-
Sale/Maturity of Investments	-	-	-
Other Funds	(284)	(72)	(303)
Other Uses	(284)	(72)	(303)
Net Investing Cash Flow	(1,156)	736	(2,455)
Financing Activities			
Cash Dividends Paid	(3,058)	(3,089)	(3,256)
Common Dividends	(3,058)	(3,089)	(3,256)
Change in Capital Stock	(10,872)	(4,229)	(4,805)
Repurchase of Common & Preferred Stk.	(11,171)	(4,686)	(5,208)
Sale of Common & Preferred Stock	299	457	403
Proceeds from Stock Options	299	457	403
Issuance/Reduction of Debt, Net	2,670	2,028	2,131
Change in Current Debt	(286)	(1,050)	96
Change in Long-Term Debt	2,957	3,078	2,035
Issuance of Long-Term Debt	3,780	4,728	3,795
Reduction in Long-Term Debt	(823)	(1,649)	(1,760)
Other Funds	(3)	(21)	(20)
Other Uses	(3)	(21)	(20)
Other Sources	-	-	-
Net Financing Cash Flow	(11,262)	(5,311)	(5,950)
Exchange Rate Effect	(104)	264	(160)
Net Change in Cash	(6,462)	1,240	(1,598)
Free Cash Flow	4,239	3,698	4,225
Free Cash Flow per Share	5	5	5
Free Cash Flow Yield (%)	4.04%	2.63%	3.03%

All figures in millions of U.S. Dollar except per share items.

McDonald's**Cash Flow Statement**

<i>Fiscal Years Ending Dec. 31</i>	2019E	2020E	2021E	2022E	2023E	2024E
Operating Activities						
Net Income / Starting Line	5,899	6,251	6,576	6,985	7,164	7,567
Depreciation	1,452	1,490	1,520	1,549	1,594	1,628
Amortization	140	131	124	116	109	103
Accounts Receivable	327	(99)	(66)	(83)	(18)	(83)
Inventories	(46)	(5)	(3)	(4)	(1)	(4)
Prepaid Expenses and Other Current Assets	(313)	(47)	(31)	(40)	(9)	(39)
Accounts Payable	(372)	74	97	63	(56)	53
Income Tax Payable	(13)	13	12	15	7	15
Accrued Payroll	535	71	47	60	13	59
Miscellaneous Current Liabilities	(117)	20	13	17	4	17
Deferred Tax Assets	721	(30)	(27)	(34)	(15)	(34)
Deferred Tax Liabilities	(42)	55	36	46	10	46
Other Long-Term Liabilities	(676)	147	97	123	27	122
Net Operating Cash Flow	7,495	8,072	8,396	8,813	8,829	9,450
Investing Activities						
Capital Expenditures	(1,878)	(1,966)	(2,024)	(2,098)	(2,114)	(2,187)
Other Long-Term Assets	154	(47)	(31)	(40)	(9)	(39)
Long-Term Investments - Affiliated Companies	99	40	40	23	1	(26)
Net Investing Cash Flow	(1,624)	(1,973)	(2,015)	(2,114)	(2,122)	(2,252)
Financing Activities						
Long-Term Debt	1,778	(1,032)	(1,763)	(1,079)	(1,263)	(1,138)
ST Debt & Curr. Portion LT Debt	6	7	(0)	(1)	(0)	(1)
Dividends Paid	(3,304)	(3,412)	(3,478)	(3,545)	(3,611)	(3,678)
Proceeds from issuance of common stock	303	303	303	303	303	303
Repurchases of common stock	(4,801)	(1,000)	(1,000)	(1,000)	(1,000)	(1,000)
Other Appropriated Reserves	12	(7)	(6)	(0)	4	1
Net Financing Cash Flow	(6,006)	(5,141)	(5,945)	(5,322)	(5,568)	(5,514)
Net Increase (Decrease) In Cash	(135)	958	435	1,377	1,138	1,684
Cash, Beginning of Year	866	731	1,689	2,124	3,501	4,639
Cash, End of Year	731	1,689	2,124	3,501	4,639	6,323

McDonald's*Common Size Balance Sheet**Fiscal Years Ending Dec. 31*

	2016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
Assets									
Cash Only	4.97%	10.80%	4.12%	3.50%	7.73%	9.45%	15.02%	19.75%	26.02%
Accounts Receivables, Net	5.99%	8.66%	11.61%	10.14%	10.14%	10.14%	10.14%	10.14%	10.14%
Inventories	0.24%	0.26%	0.24%	0.47%	0.47%	0.47%	0.47%	0.47%	0.47%
Other Current Assets	8.50%	3.63%	3.30%	4.83%	4.83%	4.83%	4.83%	4.83%	4.83%
Total Current Assets	19.69%	23.34%	19.28%	18.93%	23.16%	24.88%	30.45%	35.18%	41.45%
Net Property, Plant & Equipment	86.34%	98.37%	108.64%	111.53%	108.71%	107.83%	106.39%	107.79%	106.48%
Property, Plant & Equipment - Gross	139.89%	160.50%	176.90%	187.27%	187.88%	191.48%	193.74%	201.26%	203.52%
Accumulated Depreciation	38.28%	38.71%	38.58%	40.45%	42.14%	43.69%	45.09%	46.44%	47.68%
LT Investment - Affiliate Companies	2.95%	4.76%	5.72%	5.29%	4.87%	4.55%	4.29%	4.26%	4.22%
Intangible Assets	9.49%	10.43%	11.09%	10.50%	9.43%	8.61%	7.81%	7.29%	6.62%
Deferred Tax Assets	3.27%	3.80%	5.80%	2.39%	2.42%	2.47%	2.53%	2.58%	2.63%
Other Assets	4.27%	7.43%	5.52%	4.83%	4.83%	4.83%	4.83%	4.83%	4.83%
Total Assets	126.00%	148.13%	156.06%	153.47%	153.42%	153.17%	156.30%	161.92%	166.22%
Liabilities & Shareholders' Equity	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
ST Debt & Curr. Portion LT Debt	0.31%	0.00%	0.00%	0.03%	0.06%	0.06%	0.05%	0.05%	0.05%
Accounts Payable	3.07%	4.05%	5.75%	4.01%	4.17%	4.48%	4.60%	4.32%	4.40%
Income Tax Payable	1.09%	1.16%	1.09%	1.03%	1.04%	1.07%	1.09%	1.11%	1.14%
Other Current Liabilities	9.62%	7.45%	7.31%	9.37%	9.37%	9.37%	9.37%	9.37%	9.37%
Accrued Payroll	4.71%	5.02%	4.69%	7.29%	7.29%	7.29%	7.29%	7.29%	7.29%
Miscellaneous Current Liabilities	4.91%	2.43%	2.62%	2.08%	2.08%	2.08%	2.08%	2.08%	2.08%
Total Current Liabilities	14.09%	12.67%	14.14%	14.44%	14.65%	14.98%	15.12%	14.86%	14.95%
Long-Term Debt	105.10%	129.43%	147.80%	157.47%	145.69%	133.66%	124.32%	118.00%	109.36%
Deferred Tax Liabilities	7.38%	4.91%	5.78%	5.62%	5.62%	5.62%	5.62%	5.62%	5.62%
Other Liabilities	8.38%	15.45%	18.10%	15.00%	15.00%	15.00%	15.00%	15.00%	15.00%
Total Liabilities	134.95%	162.45%	185.82%	192.54%	180.96%	169.26%	160.06%	153.48%	144.94%
	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
Common Equity	-8.95%	-14.32%	-29.77%	-39.06%	-27.54%	-16.10%	-3.77%	8.44%	21.29%
Additional Paid-In Capital/Capital Surplus	27.51%	31.06%	35.16%	36.88%	36.62%	36.91%	36.91%	37.92%	37.89%
Retained Earnings	187.73%	211.77%	240.13%	254.43%	256.03%	262.44%	267.96%	281.04%	287.62%
Cumulative Translation Adjustment/Unrealized For. Exch. Gain	-11.81%	-8.64%	-11.54%	-11.62%	-11.10%	-10.78%	-10.41%	-10.33%	-9.98%
Other Appropriated Reserves	-0.75%	-0.91%	-0.88%	-0.83%	-0.82%	-0.82%	-0.80%	-0.77%	-0.74%
Treasury Stock	-211.64%	-247.60%	-292.64%	-317.92%	-308.26%	-303.84%	-297.44%	-299.43%	-293.51%
Total Shareholders' Equity	-8.95%	-14.32%	-29.77%	-39.06%	-27.54%	-16.10%	-3.77%	8.44%	21.29%
Total Liabilities & Shareholders' Equity	126.00%	148.13%	156.06%	153.47%	153.42%	153.17%	156.30%	161.92%	166.22%

McDonald's

Weighted Average Cost of Capital (WACC) Estimation

Cost of Equity

Beta	0.56
Risk Free Rate	1.84%
Market Risk Premium	5.09%
Cost of Equity	<u>4.69%</u>

Cost of Debt

Pre-tax Cost of Debt	3.51%
Marginal Tax Rate	23.20%
After-Tax Cost of Debt	<u>2.70%</u>

Market Value of Equity

Share Price	194.28
Shares Outstanding	767
Value of Equity	<u>149,032</u>

Market Value of Debt

BV of Short-Term Debt	0
BV of Long-Term Debt	31,075
PV of Operating Leases	9,715
Value of Debt	<u>40,791</u>

Market Weights

Equity	78.51%
Debt	21.49%

WACC Calculation

Cost of Equity	4.69%
Weight of Equity	78.51%
After-tax cost of debt	2.70%
Weight of Debt	<u>21.49%</u>
WACC	<u>4.26%</u>

McDonald's*Discounted Cash Flow (DCF) and Economic Profit (EP) Valuation Models*

Key Inputs:

CV Growth	2.00%
CV ROIC	12.51%
WACC	4.26%
Cost of Equity	4.69%

<i>Fiscal Years Ending 0.02</i>	2019E	2020E	2021E	2022E	2023E	2024E
DCF Model						
Discount Period	1	2	3	4	5	6
NOPLAT	6,539	6,279	6,536	6,793	6,882	7,237
Beg IC	49,419	51,016	52,628	54,245	56,022	57,859
End IC	51,016	52,628	54,245	56,022	57,859	59,787
Change in IC	1,597	1,611	1,617	1,777	1,838	1,928
ROIC	13.23%	12.31%	12.42%	12.52%	12.28%	12.51%
DCF CV						268,725
FCF	4,942	4,668	4,919	5,016	5,044	5,309
PV of FCF	4,740	4,294	4,340	4,245	4,094	218,106
Value of Operating Assets (PV of FCF)	239,820					
Excess Cash	-					
-Debt	40,791					
-PV of ESOP	1,410					
Value of Equity	197,619					
Shares Outstanding	794					
Target Price	\$ 248.74					
Value Adjusted for Partial Year	\$ 258.65					
EP Model						
NOPLAT	6,539	6,279	6,536	6,793	6,882	7,237
Beg IC	49,419	51,016	52,628	54,245	56,022	57,859
ROIC	13.23%	12.31%	12.42%	12.52%	12.28%	12.51%
EP	4,433	4,105	4,293	4,481	4,494	4,771
Continuing Value						210,865
Discount Periods	1	2	3	4	5	6
PV of Economic Profit	4,251	3,776	3,788	3,792	3,647	171,146
PV of Economic Profit	190,400					
+ Beginning IC	49,419					
Value of Operating Assets	239,820					
+ Excess Cash	-					
- Debt	40,791					
- PV of ESOP	1,410					
Value of Equity	197,619					
Shares Outstanding	794					
Intrinsic Value per Share	\$ 248.74					
Value Adjusted for Partial Year	\$ 258.65					

McDonald's

Dividend Discount Model (DDM) or Fundamental P/E Valuation Model

<i>Fiscal Years Ending</i>	2019E	2020E	2021E	2022E	2023E	2024E
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EPS

Key Assumptions

CV growth						2.00%
CV ROE						146%
Cost of Equity						4.69%

Future Cash Flows

P/E Multiple (CV Year)					\$	36.66
EPS (CV Year)						9.15
Future Stock Price					\$	335.46
Dividends Per Share	4.23	4.27	4.32	4.36	4.40	4.45
Future Cash Flows	4.23	4.27	4.32	4.36	4.40	\$ 335.46
Discount Periods	1	2	3	4	5	5
Discount Rate	1.05	1.10	1.15	1.20	1.26	1.26
Discounted Cash Flows	4.04	3.90	3.76	3.63	3.50	266.75
Intrinsic Value	\$ 281.54					
Partial Year Adjustment	\$ 289.37					

McDonald's

Relative Valuation Models

Ticker	Company	Price	EPS 2019E	EPS 2020E	P/E 19	P/E 20	2018 EV	2018 EBITDA	2018 EV/EBITDA	2018 Total Debt	2018 Debt/EBITDA
JACK	Jack in the Box	\$82.32	\$4.37	\$4.80	20.80	17.80	3206.00	262.50	12.21	1014.70	3.87
WEN	Wendy's Co	\$27.73	\$0.59	\$0.64	34.60	32.20	7884.80	402.50	19.59	3730.60	9.27
YUM	YUM! Brands Inc	\$99.65	\$3.72	\$4.14	26.40	23.70	40212.00	2,027.00	19.84	11297.00	5.57
QSR	Restaurant Brands International	\$65.22	\$3.54	\$3.87	24.60	22.50	40665.30	2,168.20	18.76	13800.00	6.36
YUMC	Yum! China Holdings	\$41.44	\$1.76	\$1.89	24.20	22.50	16534.30	1,592.00	10.39	2112.00	1.33
Average					26.12	23.74	21700.48	1,290.44	16.16	7460.58	6.27
MCD	McDonald's	\$194.28	\$ 7.56	\$ 7.83	25.7	24.8	190569.00	10,363.60	18.39	45435.20	4.38

Implied Relative Value:

P/E (EPS19)	\$ 197.34
P/E (EPS20)	\$ 185.89

Industry EV/EBITDA	16.16
MCD EV/EBITDA	18.39

Industry Debt/EBITDA	6.27
MCD Debt/EBITDA	4.38

MCD EV at Industry Multiple	167439.04
Less: Debt	45435.20
Less: Minority Interest	0
Plus: Cash	866
Equity Value	122869.84
Implied Relative Price Per Share	\$ 160.17

McDonald's*Key Management Ratios*

<i>Fiscal Years Ending</i>	2016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
Liquidity Ratios									
Current Ratio (Current Assets/Current Liabilities)	1.40	1.84	1.36	1.31	1.58	1.66	2.01	2.37	2.77
Quick Ratio (Cash+AR)/CL	0.78	1.54	1.11	0.94	1.22	1.31	1.66	2.01	2.42
Cash Ratio (Cash +Cash Equiv)/CL	0.35	0.85	0.29	0.24	0.53	0.63	0.99	1.33	1.74
Activity or Asset-Management Ratios									
Asset Turnover (Rev/Avg Total Assets)	0.79	0.68	0.64	0.65	0.65	0.65	0.64	0.62	0.60
Receivables Turnover (Rev/Avg Accts Receivable)	16.70	11.55	8.61	9.87	9.87	9.87	9.87	9.87	9.87
Financial Leverage Ratios									
Debt to Assets (Debt/Assets)	0.83	0.87	0.95	1.03	0.95	0.87	0.80	0.73	0.66
Debt to Equity (Debt/Equity)	-11.74	-9.04	-4.97	-4.03	-5.29	-8.30	-33.00	13.99	5.14
Equity Ratio (Total Equity/Total Assets)	-0.07	-0.10	-0.19	-0.25	-0.18	-0.11	-0.02	0.05	0.13
Interest Coverage (EBITDA/Interest Expense)	45.37	39.18	10.44	8.40	8.41	9.04	9.94	10.51	11.49
Profitability Ratios									
Gross Margin (Rev-COGS-SG&A)/Rev	38%	43%	48%	43%	44%	44%	45%	45%	46%
Net Profit Margin (NI/Rev)	19%	23%	28%	28%	29%	29%	30%	31%	31%
Pretax Margin (EBITA/REV)	157%	153%	42%	37%	38%	38%	38%	39%	39%
ROA (NI/Total Assets)	15%	15%	18%	18%	19%	19%	19%	19%	19%
ROE (NI/Shareholder's Equity)	-213%	-159%	-95%	-72%	-104%	-182%	-796%	362%	146%
Payout Policy Ratios									
Dividend Payout Ratio (Dividends/NI)	0.65	0.59	0.55	0.56	0.55	0.53	0.51	0.50	0.49
Total. Payout Ratio (Div+Repurchases)/NI	3.04	1.50	1.43	1.37	0.71	0.68	0.65	0.64	0.62

		CV ROIC						
WACC	\$258.65	11.76%	12.01%	12.26%	12.51%	12.76%	13.01%	13.26%
	3.51%	411.92	413.79	415.58	417.29	418.95	420.54	422.07
	3.76%	344.97	346.56	348.08	349.52	350.94	352.29	353.58
	4.01%	294.69	296.06	297.37	298.62	299.85	301.01	302.14
	4.26%	255.20	256.40	257.56	258.65	259.73	260.75	261.74
	4.51%	224.19	225.26	226.29	227.26	228.22	229.13	230.01
	4.76%	198.52	199.49	200.41	201.29	202.15	202.97	203.76
	5.01%	177.13	178.00	178.84	179.63	180.41	181.16	181.87

		Beta						
Equity Risk Premium	\$258.65	0.41	0.46	0.51	0.56	0.61	0.66	0.71
	4.34%	256.40	256.85	257.31	257.77	258.23	258.68	259.14
	4.59%	256.61	257.10	257.58	258.06	258.55	259.03	259.51
	4.84%	256.83	257.34	257.85	258.36	258.87	259.38	259.89
	5.09%	257.04	257.58	258.12	258.65	259.19	259.73	260.26
	5.34%	257.26	257.82	258.39	258.95	259.51	260.07	260.63
	5.59%	257.48	258.07	258.65	259.24	259.83	260.42	261.01
	5.84%	257.69	258.31	258.92	259.54	260.15	260.77	261.38

		Marginal Tax Rate						
Pre-Tax Cost of Debt	\$258.65	22.90%	23.00%	23.10%	23.20%	23.30%	23.40%	23.50%
	3.214%	258.24	257.78	257.32	256.86	256.40	255.94	255.48
	3.314%	258.83	258.37	257.92	257.46	257.00	256.54	256.08
	3.414%	259.43	258.97	258.51	258.06	257.60	257.14	256.69
	3.514%	260.02	259.57	259.11	258.65	258.20	257.74	257.29
	3.614%	260.62	260.16	259.71	259.25	258.80	258.34	257.89
	3.714%	261.21	260.75	260.30	259.85	259.39	258.94	258.48
	3.814%	261.80	261.35	260.89	260.44	259.99	259.53	259.08

		Revenue Growth						
COGS (% Sales)	\$258.65	2.74%	2.99%	3.24%	3.47%	3.74%	3.99%	4.24%
	41.75%	261.12	262.01	262.90	263.71	264.68	265.57	266.46
	42.00%	259.44	260.33	261.22	262.02	262.99	263.87	264.76
	42.25%	257.77	258.65	259.54	260.34	261.30	262.18	263.06
	42.50%	256.10	256.98	257.85	258.65	259.61	260.49	261.36
	42.75%	254.42	255.30	256.17	256.97	257.92	258.79	259.67
	43.00%	252.75	253.62	254.49	255.28	256.23	257.10	257.97
	43.25%	251.08	251.94	252.81	253.60	254.54	255.41	256.27

		Risk-Free Rate						
CV Growth	\$258.65	1.54%	1.64%	1.74%	1.84%	1.94%	2.04%	2.14%
	1.70%	231.89	232.07	232.25	232.43	232.61	232.78	232.96
	1.80%	239.91	240.09	240.28	240.46	240.64	240.83	241.01
	1.90%	248.60	248.79	248.98	249.17	249.36	249.55	249.75
	2.00%	258.06	258.26	258.45	258.65	258.85	259.05	259.25
	2.10%	268.39	268.60	268.80	269.01	269.22	269.43	269.64
	2.20%	279.73	279.94	280.16	280.38	280.59	280.81	281.03
	2.30%	292.22	292.44	292.67	292.90	293.12	293.35	293.58

McDonald's
Value Driver Estimation

<i>Fiscal Years Ending Dec. 31</i>	2016	2017	2018	2019E	2020E	2021E	2022E	2023E	2024E
NOPLAT									
Sales	24,622	22,820	21,025	20,863	21,842	22,488	23,309	23,488	24,302
Cost of sales	12,901	10,836	8,757	9,388	9,720	9,895	10,139	10,100	10,329
SGA	2,385	2,231	2,200	2,504	2,621	2,699	2,797	2,819	2,916
Depreciation	1,391	1,228	1,303	1,452	1,490	1,520	1,549	1,594	1,628
Amortization	126	136	179	140	131	124	116	109	103
Implied interest on operating leases	336	322	341	342	342	342	240	240	240
EBITA	38,727	34,846	8,927	7,721	8,222	8,593	8,947	9,107	9,567
Adjusted Taxes									
Income Tax Provision	2,180	3,381	1,892	1,782	1,888	1,987	2,110	2,164	2,286
Add: Tax Shield on Interest on Operating Leases	78	75	79	79	79	79	56	56	56
Less: Adjusted Taxes	2,258	3,456	1,971	1,861	1,968	2,066	2,166	2,220	2,342
Deferred Taxes									
Net Deferred Taxes Current Year	1,013	252	(4)	675	700	709	721	716	727
Less: Net Deferred Taxes Prior Year	1,172	1,013	252	(4)	675	700	709	721	716
Total Change in Deferred Taxes	(158)	(762)	(255)	679	25	9	12	(5)	12
NOPLAT	36,311	30,629	6,701	6,539	6,279	6,536	6,793	6,882	7,237
Invested Capital									
Operating Current Assets:									
Normal Cash (2% of Sales)	1,231	1,141	1,051	1,043	1,092	1,124	1,165	1,174	1,215
Accounts Receivable	1,474	1,976	2,442	2,115	2,214	2,279	2,363	2,381	2,463
Inventories	59	59	51	97	102	105	109	110	113
Prepaid Expenses & Other Current Assets	2,092	828	695	1,007	1,054	1,086	1,125	1,134	1,173
Miscellaneous Current Liabilities	1,209	554	551	434	454	468	485	489	506
Operating Current Liabilities:									
Accounts Payable	756	925	1,208	836	911	1,008	1,071	1,016	1,068
Income taxes Payable	267	266	228	215	228	240	255	261	276
Accrued Liabilities	1,159	1,146	987	1,522	1,593	1,640	1,700	1,713	1,773
Net Operating Working Capital	2,674	1,668	1,816	1,689	1,731	1,706	1,736	1,809	1,848
Plus: Net PPE	34,443	36,626	37,194	39,071	41,037	43,061	45,159	47,273	49,460
Plus: Net Other Operating Assets	2,092	828	695	1,007	1,054	1,086	1,125	1,134	1,173
PV of Operating Leases	9,573	9,170	9,715	9,249	8,806	8,392	8,002	7,644	7,306
Invested Capital	48,783	48,293	49,419	51,016	52,628	54,245	56,022	57,859	59,787
FCF									
NOPLAT	36,311	30,629	6,701	6,539	6,279	6,536	6,793	6,882	7,237
Less: Change in Invested Capital	(31)	(490)	1,127	1,597	1,611	1,617	1,777	1,838	1,928
Free Cash Flow (FCF)	36,341	31,119	5,574	4,942	4,668	4,919	5,016	5,044	5,309
ROIC									
NOPLAT	36,311	30,629	6,701	6,539	6,279	6,536	6,793	6,882	7,237
Beginning Invested Capital	48,813	48,783	48,293	49,419	51,016	52,628	54,245	56,022	57,859
Return on Invested Capital (ROIC)	74%	63%	13.88%	13.23%	12.31%	12.42%	12.52%	12.28%	12.51%
EP									
Beginning Invested Capital	48813.45065	48782.62514	48,293	49,419	51,016	52,628	54,245	56,022	57,859
ROIC	74%	63%	13.88%	13.23%	12.31%	12.42%	12.52%	12.28%	12.51%
WACC	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%	8.00%
Economic Profit (EP)	\$32,405.48	\$26,725.97	2,837	2,586	2,198	2,326	2,454	2,400	2,608

Effects of ESOP Exercise and Share Repurchases on Common Stock Balance Sheet Account and Number of Shares Outstanding

Number of Options Outstanding (shares):	17
Average Time to Maturity (years):	6.20
Expected Annual Number of Options Exercised:	3

Current Average Strike Price:	\$ 113.06
Cost of Equity:	4.69%
Current Stock Price:	\$194.28

	2019E	2020E	2021E	2022E	2023E	2024E
Increase in Shares Outstanding:	3	3	3	3	3	3
Average Strike Price:	\$ 113.06	\$ 113.06	\$ 113.06	\$ 113.06	\$ 113.06	\$ 113.06
Increase in Common Stock Account:	303	303	303	303	303	303
Change in Treasury Stock	-4,801	-1,000	-1,000	-1,000	-1,000	-1,000
Expected Price of Repurchased Shares:	\$ 194.28	\$ 203.39	\$ 212.93	\$ 222.92	\$ 233.38	\$ 244.32
Number of Shares Repurchased:	(25)	(5)	(5)	(4)	(4)	(4)
Shares Outstanding (beginning of the year)	767	794	802	809	817	824
Plus: Shares Issued Through ESOP	3	3	3	3	3	3
Less: Shares Repurchased in Treasury	(25)	(5)	(5)	(4)	(4)	(4)
Shares Outstanding (end of the year)	794	802	809	817	824	830

VALUATION OF OPTIONS GRANTED IN ESOP

Ticker Symbol	MCD
Current Stock Price	\$194.28
Risk Free Rate	1.84%
Current Dividend Yield	1.00%
Annualized St. Dev. of Stock Returns	19.06%

Range of Outstanding Options	Number of Shares	Average Exercise Price	Average Remaining Life (yrs)	B-S Option Price	Value of Options Granted
Range 1	16.6	113.06	6.2	\$ 84.93	\$ 1,410
Range 2					
Range 3					
Range 4					
Range 5					
Range 6					
Range 7					
Range 8					
Range 9					
Range 10					
Range 11					
Range 12					
Range 13					
Range 14					
Total	17	\$ 113.06	6.20	\$ 95.81	\$ 1,410