



# McDonald's (MCD)

Updated January 30<sup>th</sup>, 2019 by Jonathan Weber

## Key Metrics

<b>Current Price:</b>	\$180	<b>5 Year CAGR Estimate:</b>	7.5%	<b>Volatility Percentile:</b>	8.3%
<b>Fair Value Price:</b>	\$166	<b>5 Year Growth Estimate:</b>	6.5%	<b>Momentum Percentile:</b>	75.7%
<b>% Fair Value:</b>	109%	<b>5 Year Valuation Multiple Estimate:</b>	-1.6%	<b>Growth Percentile:</b>	60.7%
<b>Dividend Yield:</b>	2.6%	<b>5 Year Price Target</b>	\$226	<b>Valuation Percentile:</b>	30.2%
<b>Dividend Risk Score:</b>	B	<b>Retirement Suitability Score:</b>	B	<b>Total Return Percentile:</b>	31.5%

## Overview & Current Events

McDonald's is the largest publicly-traded restaurant company in the world. The Oak Brook (IL) – based company was founded in 1940 and has a market capitalization of \$140 billion. As a Dividend Aristocrat, McDonald's has a long dividend growth history, which has made it a favorite holding for many retail investors.

McDonald's reported its fourth quarter and full year earnings results on January 30. The company generated revenues of \$5.16 billion during the fourth quarter. This was 3.4% less than the company's revenues during the previous year's quarter. McDonald's underlying performance was still very solid, though. Revenue declines were based on the negative impact of a strengthening dollar as well as on the impact of McDonald's refranchising efforts throughout the last year, which result in a lower portion of sales at franchised restaurants revenues flowing towards the company.

Comparable restaurant sales rose at a highly attractive pace of 4.4% during the fourth quarter, which was more than the 4.0% comparable restaurant sales growth rate that analysts had forecasted. US comps sales were up 2.3%, but international comps sales grew faster than that. This includes a 4.8% comparable restaurant sales growth in the regions that McDonald's sums up under the high-growth market label. McDonald's generated earnings-per-share of \$1.97 during the fourth quarter, which was 15.2% more than McDonald's earnings-per-share during the fourth quarter of fiscal 2017. The growth rate was positively impacted by tax rate changes.

## Growth on a Per-Share Basis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
<b>EPS</b>	\$3.98	\$4.60	\$5.27	\$5.36	\$5.55	\$4.82	\$4.97	\$5.71	\$6.66	\$7.85	<b>\$8.23</b>	<b>\$11.28</b>
<b>DPS</b>	\$2.05	\$2.26	\$2.53	\$2.87	\$3.12	\$3.28	\$3.44	\$3.61	\$3.83	\$4.19	<b>\$4.68</b>	<b>\$6.50</b>
<b>Shares</b>	1080	1050	1020	1000	990	960	910	820	790	770	<b>760</b>	<b>700</b>

McDonald's has a long and successful growth history when it comes to its earnings-per-share as well as when it comes to the company's dividend payments. A couple of years ago the company encountered some headwinds, though, as profits dropped between 2013 and 2014. McDonald's has found ways to reignite growth during the following years, which included driving comparable sales by offering all day breakfast at its restaurants and expanding the menu through offerings like organic meat and healthier alternatives. Another big strategic shift was McDonald's decision to refranchise many of its restaurants. The company generates lower revenue now, but its costs have come down to more than offset this top-line change. McDonald's has turned itself into an asset-light, low-cost company that collects franchise fees from a larger number of total restaurants.

This strategy has been very successful, as earnings-per-share have grown at a strong pace over the last three years. It is highly likely that McDonald's will continue to perform well in the future. McDonald's continues to perform better than many of its peers when it comes to generating rising revenues from existing restaurants, and there is potential for McDonald's to open new restaurants in international markets throughout the next couple of years. Earnings-per-share growth will be driven by higher franchising fees, declining operating costs, and the impact of share repurchases, which have lowered the company's share count considerably over the last couple of years. Management states that the

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company aims for system wide sales growth of 3%-5% a year in the long run, while the company also targets earnings-per-share growth in the high single digits in the long run.

## Valuation Analysis

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	Now	2024
Avg. P/E	14.4	15.4	15.9	17.3	17.5	20.0	20.2	21.1	22.3	22.4	<b>21.7</b>	<b>20.0</b>
Avg. Yld.	3.6%	3.2%	3.0%	3.1%	3.2%	3.4%	3.4%	3.0%	2.6%	2.6%	<b>2.6%</b>	<b>3.0%</b>

McDonald's trades at close to 22 times 2019's net profits right now. This is close to the top end of the historic range for the company's price to earnings ratio, which shows that shares are relatively expensive right here. We see downside potential for McDonald's valuation over the coming years. The above-average valuation will likely be a headwind for the company's total returns going forward. The dividend yield is below the long-term average as well.

## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2024
Payout	51.5%	49.1%	48.0%	53.5%	56.2%	68.0%	69.2%	63.2%	57.5%	53.4%	<b>56.9%</b>	<b>57.6%</b>

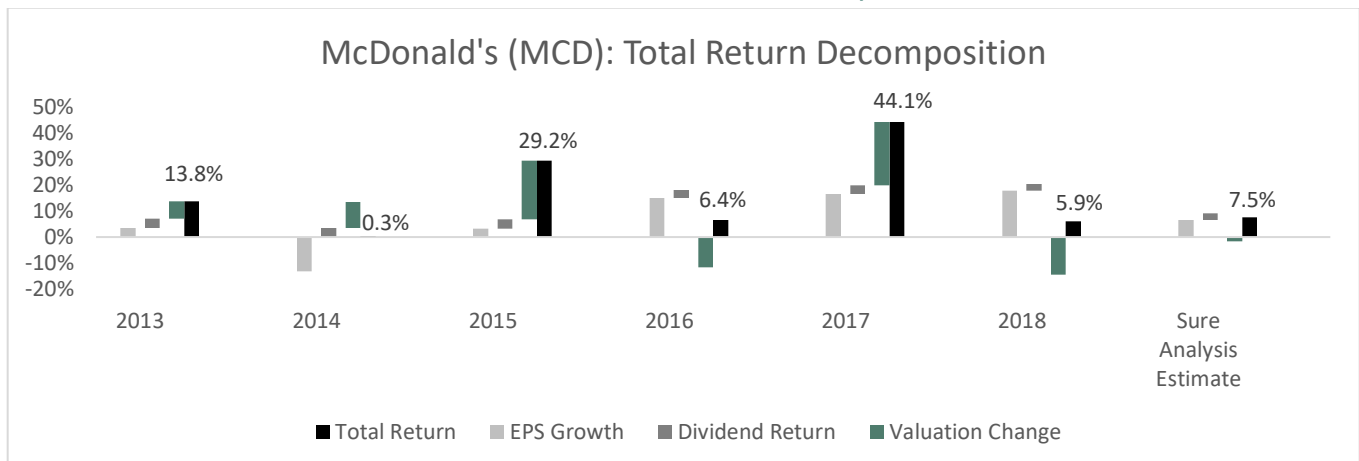
McDonald's dividend payout ratio has been moving in a range of slightly below 50% to slightly below 70% throughout the last decade. During the last couple of years McDonald's has increased its dividend at a pace that was lower than its earnings-per-share growth rate, which has made the dividend payout ratio decline. Due to the stability of McDonald's during past recessions, coupled with a dividend ratio that is not overly high, we rate McDonald's dividend as quite safe.

McDonald's global scale makes the company less vulnerable to headwinds in one geographic region, and the company has performed well compared to other restaurant companies over the last couple of years when it comes to maintaining comparable restaurant sales growth. With its inexpensive offerings McDonald's is also relatively recession-proof, which is showcased by the fact that McDonald's kept growing during the 2008-2009 financial crisis.

## Final Thoughts & Recommendation

McDonald's is among the top restaurant companies in terms of size and scale, and the company has a very successful history regarding generating earnings-per-share growth and rising dividend payouts. McDonald's will likely be able to grow at a solid pace going forward, but we believe that the above-average valuation will be a headwind for share price gains. We rate McDonald's a hold right now, with valuation concerns being the primary reason.

## Total Return Breakdown by Year



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## Income Statement Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>Revenue</b>	23522	22745	24075	27006	27567	28106	27441	25413	24622	22820
<b>Gross Profit</b>	8639	8792	9637	10687	10816	10903	10456	9789	10205	10621
<b>Gross Margin</b>	36.7%	38.7%	40.0%	39.6%	39.2%	38.8%	38.1%	38.5%	41.4%	46.5%
<b>SG&amp;A Exp.</b>	2356	2234	2333	2394	2455	2386	2488	2434	2385	2231
<b>D&amp;A Exp.</b>	1208	1216	1276	1415	1489	1585	1645	1556	1517	1363
<b>Operating Profit</b>	6449	6780	7304	8293	8361	8517	7968	7355	7820	8390
<b>Op. Margin</b>	27.4%	29.8%	30.3%	30.7%	30.3%	30.3%	29.0%	28.9%	31.8%	36.8%
<b>Net Profit</b>	4313	4551	4946	5503	5465	5586	4758	4529	4687	5192
<b>Net Margin</b>	18.3%	20.0%	20.5%	20.4%	19.8%	19.9%	17.3%	17.8%	19.0%	22.8%
<b>Free Cash Flow</b>	3782	3799	4206	4420	3917	4296	4147	4725	4239	3698
<b>Income Tax</b>	1845	1936	2054	2509	2614	2619	2614	2026	2180	3381

## Balance Sheet Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>Total Assets</b>	28462	30225	31975	32990	35387	36626	34227	37939	31024	33804
<b>Cash &amp; Equivalents</b>	2063	1796	2387	2336	2336	2799	2078	7686	1223	2464
<b>Inventories</b>	112	106	110	117	122	124	110	100	59	59
<b>Goodwill &amp; Int.</b>	2237	2425	2586	2653	2804	2873	2735	2516	2337	2380
<b>Total Liabilities</b>	15079	16191	17341	18600	20093	20617	21374	30851	33228	37072
<b>Accounts Payable</b>	620	636	944	961	1142	1086	860	875	756	925
<b>Long-Term Debt</b>	10218	10578	11505	12500	13633	14130	14936	24122	25956	29536
<b>Total Equity</b>	13383	14034	14634	14390	15294	16010	12853	7088	-2204	-3268
<b>D/E Ratio</b>	0.76	0.75	0.79	0.87	0.89	0.88	1.16	3.40	-11.78	-9.04

## Profitability & Per Share Metrics

Year	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017
<b>Return on Assets</b>	14.9%	15.5%	15.9%	16.9%	16.0%	15.5%	13.4%	12.6%	13.6%	16.0%
<b>Return on Equity</b>	30.1%	33.2%	34.5%	37.9%	36.8%	35.7%	33.0%	45.4%	192%	-190%
<b>ROIC</b>	17.9%	18.9%	19.5%	20.8%	19.6%	18.9%	16.4%	15.4%	17.1%	20.8%
<b>Shares Out.</b>	1110	1080	1050	1020	1000	990	960	910	820	790
<b>Revenue/Share</b>	20.53	20.54	22.29	25.85	27.02	27.94	27.82	26.90	28.59	27.98
<b>FCF/Share</b>	3.30	3.43	3.89	4.23	3.84	4.27	4.20	5.00	4.92	4.53

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.

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