



McDonald's Corporation (MCD)

Updated May 5th, 2019 by Jonathan Weber

Key Metrics

Current Price:	\$198	5 Year CAGR Estimate:	5.3%	Volatility Percentile:	7.6%
Fair Value Price:	\$166	5 Year Growth Estimate:	6.5%	Momentum Percentile:	78.8%
% Fair Value:	119%	5 Year Valuation Multiple Estimate:	-3.6%	Growth Percentile:	63.7%
Dividend Yield:	2.4%	5 Year Price Target	\$226	Valuation Percentile:	27.4%
Dividend Risk Score:	A	Retirement Suitability Score:	B	Total Return Percentile:	28.2%

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 \$151 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 first quarter earnings results on May 1. The company generated revenues of \$4.96 billion during the first quarter. This was 3.5% less than the company's revenues during the previous year's quarter, but McDonald's nevertheless was able to beat the consensus analyst top line estimate. McDonald's underlying performance was quite strong: McDonald's comparable restaurant sales rose by 5.4% globally, which is a very strong pace compared to restaurant peers, and which easily beat the analyst estimate. Comparable sales in the US were up 4.5% year over year, which was also ahead of the analyst consensus of 3.0%. The fact that McDonald's revenues were down despite a strong pace of comparable restaurant sales can be explained by 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. McDonald's generated earnings-per-share of \$1.78 during the first quarter, which was unchanged compared to the earnings-per-share from Q1 of 2018. At constant currency rates, McDonald's earnings-per-share would have been up by 5%.

Growth on a Per-Share Basis

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

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 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 other types of healthier food. 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 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.

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.



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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	24.1	20.0
Avg. Yld.	3.6%	3.2%	3.0%	3.1%	3.2%	3.4%	3.4%	3.0%	2.6%	2.6%	2.4%	2.9%

McDonald's trades at more than 24 times this year's net profits right now. This is the highest valuation shares have traded at during the last couple of years, which is why we believe that the stock is overvalued right now. We see downside potential for McDonald's valuation over the coming years, the resulting multiple compression will be a headwind for the stock's total returns going forward. McDonald's dividend yield is below the long-term average right now.

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%	56.9%	57.6%

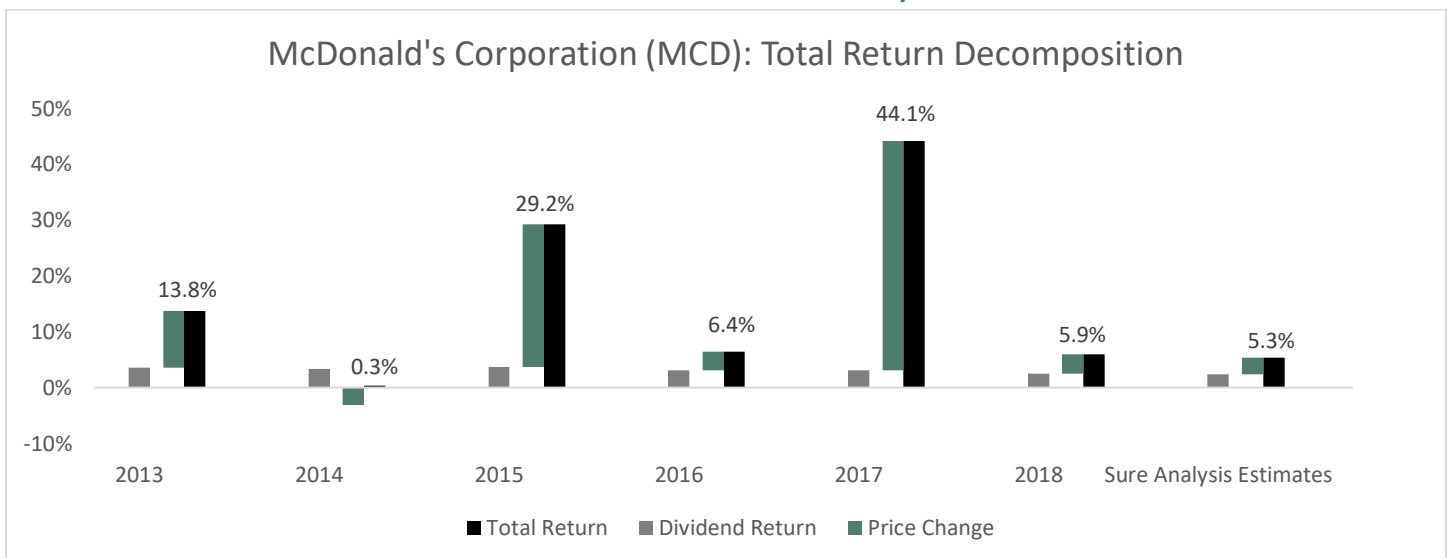
McDonald's dividend payout ratio has been moving in a range of slightly below 50% to slightly below 70% throughout the last decade. During the last couple of years McDonald's has increased its dividend at a pace that was lower than its earnings-per-share growth rate, which has made the dividend payout 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 very 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 the top restaurant company in terms of size and scale thanks to its global reach, and the company has a very successful history regarding generating earnings-per-share as well as dividend growth. McDonald's will likely be able to grow at a solid pace going forward, but the very high valuation will be a headwind for share price gains in the future. 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	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Revenue	22745	24075	27006	27567	28106	27441	25413	24622	22820	21025
Gross Profit	8792	9637	10687	10816	10903	10456	9789	10205	10621	10786
Gross Margin	38.7%	40.0%	39.6%	39.2%	38.8%	38.1%	38.5%	41.4%	46.5%	51.3%
SG&A Exp.	2234	2333	2394	2455	2386	2488	2434	2385	2231	2200
D&A Exp.	1216	1276	1415	1489	1585	1645	1556	1517	1363	1482
Operating Profit	6780	7304	8293	8361	8517	7968	7355	7820	8390	8586
Op. Margin	29.8%	30.3%	30.7%	30.3%	30.3%	29.0%	28.9%	31.8%	36.8%	40.8%
Net Profit	4551	4946	5503	5465	5586	4758	4529	4687	5192	5924
Net Margin	20.0%	20.5%	20.4%	19.8%	19.9%	17.3%	17.8%	19.0%	22.8%	28.2%
Free Cash Flow	3799	4206	4420	3917	4296	4147	4725	4239	3698	4225
Income Tax	1936	2054	2509	2614	2619	2614	2026	2180	3381	1892

Balance Sheet Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Total Assets	30225	31975	32990	35387	36626	34227	37939	31024	33804	32811
Cash & Equivalents	1796	2387	2336	2336	2799	2078	7686	1223	2464	866
Inventories	106	110	117	122	124	110	100	59	59	51
Goodwill & Int.	2425	2586	2653	2804	2873	2735	2516	2337	2380	2332
Total Liabilities	16191	17341	18600	20093	20617	21374	30851	33228	37072	39070
Accounts Payable	636	944	961	1142	1086	860	875	756	925	1208
Long-Term Debt	10578	11505	12500	13633	14130	14936	24122	25956	29536	31075
Total Equity	14034	14634	14390	15294	16010	12853	7088	-2204	-3268	-6258
D/E Ratio	0.75	0.79	0.87	0.89	0.88	1.16	3.40	-11.78	-9.04	-4.97

Profitability & Per Share Metrics

Year	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018
Return on Assets	15.5%	15.9%	16.9%	16.0%	15.5%	13.4%	12.6%	13.6%	16.0%	17.8%
Return on Equity	33.2%	34.5%	37.9%	36.8%	35.7%	33.0%	45.4%	192%	-190%	-124%
ROIC	18.9%	19.5%	20.8%	19.6%	18.9%	16.4%	15.4%	17.1%	20.8%	23.2%
Shares Out.	1080	1050	1020	1000	990	960	910	820	790	770
Revenue/Share	20.54	22.29	25.85	27.02	27.94	27.82	26.90	28.59	27.98	26.76
FCF/Share	3.43	3.89	4.23	3.84	4.27	4.20	5.00	4.92	4.53	5.38

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

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