McDonald's Corporation (MCD)

Updated April 28th, 2022, by Eli Inkrot

Key Metrics

Current Price:	$254	**5 Year CAGR Estimate:**	3.4%	**Market Cap:**	$189 B
Fair Value Price:	$200	**5 Year Growth Estimate:**	6.0%	**Ex-Dividend Date:**	06/01/22
% Fair Value:	127%	**5 Year Valuation Multiple Estimate:**	-4.7%	**Dividend Payment Date:**	06/15/22
Dividend Yield:	2.2%	**5 Year Price Target**	$268	**Years Of Dividend Growth:**	46
Dividend Risk Score:	A	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

McDonald's, founded in 1940 and headquartered in Chicago IL, is the world's leading global foodservice retailer with more than 40,000 locations in over 100 countries. Approximately 93% of the stores are independently owned and operated. The $189 billion market cap company has raised its dividend every year since paying its first dividend in 1976, qualifying the company as a Dividend Aristocrat.

On September 23rd, 2021, McDonald's declared a $1.38 quarterly dividend, marking a 7.0% year-over-year increase.

On April 28th, 2022, McDonald's reported Q1 2022 results for the period ending March 31st, 2022. For the quarter, total revenue came in at $5.67 billion, a 10.6% increase compared to Q1 2021. Revenue grew 6.5% at company-owned stores, while revenue increased 13.4% at franchised restaurants. Net income equaled $1.10 billion or $1.48 per share compared to $1.54 billion or $2.05 per share in Q1 2021.

Growth on a Per-Share Basis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
EPS	$5.36	$5.55	$4.82	$4.97	$5.71	$6.66	$7.90	$7.84	$6.05	$9.28	***$10.00***	***$13.38***
DPS	$2.87	$3.12	$3.28	$3.44	$3.61	$3.83	$4.19	$4.73	$5.04	$5.25	***$5.52***	***$7.39***
Shares[1]	1,003	990	963	907	819	794	767	746	750	752	***745***	***690***

McDonald's has a long and successful growth history when it comes to both earnings-per-share and dividends. In the 2008 through 2019 period earnings-per-share compounded at an average rate of 7.1% per annum. During that time the company did encounter some headwinds, though, as profits dropped in 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 healthier offerings. Another big strategic shift was McDonald's decision to refranchise many of its restaurants. The company generates lower revenue now (sales peaked at $28 billion in 2013) 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 successful, with earnings-per-share growing at a strong pace. 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 could 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 years.

Earnings snapped back materially in 2021 and we are forecasting 6% annual growth over the intermediate term.

Valuation Analysis

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	Now	2027
Avg. P/E	17.3	17.5	20.0	20.2	21.1	22.3	21.1	25.2	33.2	25.3	***25.4***	***20.0***
Avg. Yld.	3.1%	3.2%	3.4%	3.4%	3.0%	2.6%	2.5%	2.4%	2.5%	2.2%	***2.2%***	***2.8%***

[1] In millions.

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Over the past decade shares of McDonald's have traded hands with an average P/E ratio of 22 times earnings. We consider 20 times earnings as a reasonable starting place, taking into consideration the slightly reduced growth expectations and a very solid business model. This valuation could be too conservative if growth continues to accelerate, but this has been somewhat typical of the security's past. With shares trading near 25 times our expected earnings, this implies the potential for a notable valuation headwind in the years to come.

Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2027
Payout	52%	56%	68%	69%	63%	58%	53%	60%	83%	57%	***55%***	***55%***

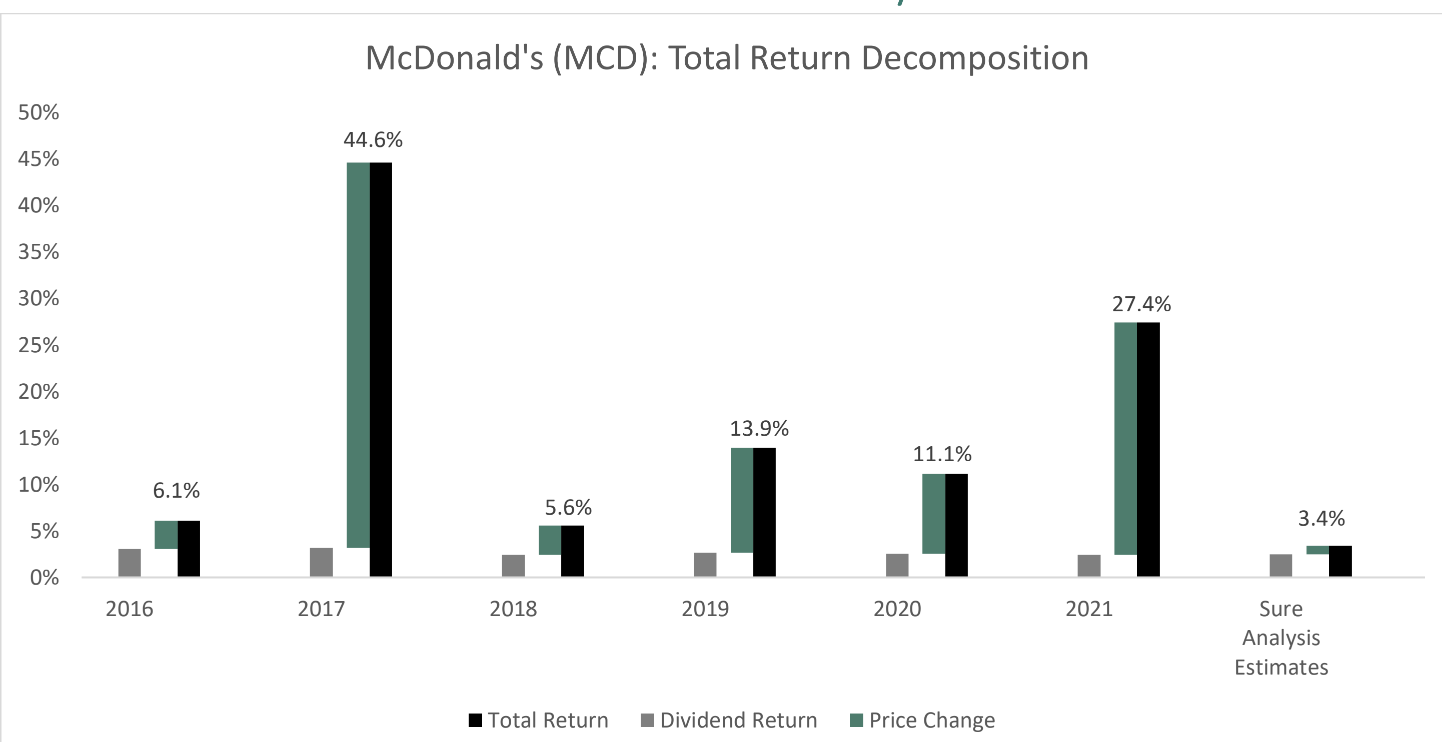
McDonald's dividend payout ratio has been oscillating in a range of ~50% to ~70% throughout the last decade. Due to the stability of McDonald's during past recessions, coupled with a payout ratio that is not overly high, we view McDonald's dividend as safe; the most recent 7.0% dividend increase being a good example of this.

McDonald's competitive advantage lies in its global scale, immense network of restaurants, well-known brand, and real estate assets. Indeed, the company's superior track record against numerous competitors has illustrated why these aspects are important to the company's success. During the Great Recession McDonald's posted excellent results, with earnings-per-share of $2.91, $3.67, $3.98, and $4.60 over the 2007 through 2010 stretch, while the dividend kept on increasing to boot. Results bounced back in 2021 as well.

Final Thoughts & Recommendation

Shares are up 8% in the last year. McDonald's has a very successful history of generating earnings-per-share and dividend growth. That being said, today's valuation is not compelling in our view. Total return potential comes in at 3.4% per annum, as 6% growth, and a 2.2% dividend yield could be offset by a valuation headwind. While we believe the business is excellent, the valuation leaves a bit to be desired. Shares earn a hold rating.

Total Return Breakdown by Year



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Income Statement Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Revenue	27567	28106	27441	25413	24622	22820	21025	21077	19210	23220
Gross Profit	10816	10903	10456	9789	10205	10621	10786	11115	9752	12580
Gross Margin	39.2%	38.8%	38.1%	38.5%	41.4%	46.5%	51.3%	52.7%	50.8%	54.2%
SG&A Exp.	2455	2386	2488	2434	2385	2231	2200	2229	2245	2378
D&A Exp.	1489	1585	1645	1556	1517	1363	1482	1618	1751	1868
Operating Profit	8361	8517	7968	7355	7820	8390	8586	8886	7206	9873
Op. Margin	30.3%	30.3%	29.0%	28.9%	31.8%	36.8%	40.8%	42.2%	37.5%	42.5%
Net Profit	5465	5586	4758	4529	4687	5192	5924	6025	4730	7545
Net Margin	19.8%	19.9%	17.3%	17.8%	19.0%	22.8%	28.2%	28.6%	24.6%	32.5%
Free Cash Flow	3917	4296	4147	4725	4239	3698	4225	5728	4624	7102
Income Tax	2614	2619	2614	2026	2180	3381	1892	1993	1410	1583

Balance Sheet Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Total Assets	35387	36626	34227	37939	31024	33804	32811	47511	52630	53850
Cash & Equivalents	2336	2799	2078	7686	1223	2464	866	899	3449	4709
Inventories	122	124	110	100	59	59	51	50	51	56
Goodwill & Int.	2804	2873	2735	2516	2337	2380	2332	2677	2773	2782
Total Liabilities	20093	20617	21374	30851	33228	37072	39070	55721	60450	58460
Accounts Payable	1142	1086	860	875	756	925	1208	988	741	1007
Long-Term Debt	13633	14130	14936	24122	25956	29536	31075	34177	37440	35620
Total Equity	15294	16010	12853	7088	-2204	-3268	-6258	-8210	-7825	-4601
LTD/E Ratio	0.89	0.88	1.16	3.40	-11.78	-9.04	-4.97	-4.16	-4.79	-7.74

Profitability & Per Share Metrics

Year	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021
Return on Assets	16.0%	15.5%	13.4%	12.6%	13.6%	16.0%	17.8%	15.0%	9.5%	14.2%
Return on Equity	36.8%	35.7%	33.0%	45.4%	192%	-190%	-124%	---	---	---
ROIC	19.6%	18.9%	16.4%	15.4%	17.1%	20.8%	23.2%	23.7%	17.0%	24.9%
Shares Out.	1,003	990	963	907	819	794	767	746	750	752
Revenue/Share	27.02	27.94	27.82	26.90	28.59	27.98	26.76	27.55	25.61	30.89
FCF/Share	3.84	4.27	4.20	5.00	4.92	4.53	5.38	7.49	6.17	9.45

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