McDonald’s Corporation
Analysis of Financial Statements

By: Mohammad Assad Siddiqi.
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Table of Contents

1. Project objective and overall research approach ............................................................................. 3
   1.1 Introduction ................................................................................................................................. 3
   1.2 Reasons for Choosing the Topic and Organization ................................................................. 3
   1.3 Project Objectives ...................................................................................................................... 3
   1.4 Research Questions ................................................................................................................... 4
   1.5 Research Approach ..................................................................................................................... 4

2. Information Gathering .................................................................................................................... 6
   2.1 Sources of Information ............................................................................................................... 6
   2.2 Methods of Information Gathering ............................................................................................ 6
   2.3 Limitations of information gathering ......................................................................................... 7
   2.4 Ethical Issues faced during information gathering .................................................................... 7
   2.5 Accounting and Business Techniques used and their Limitations .......................................... 8

Ratio Analysis .................................................................................................................................... 8

Limitations of Ratio Analysis ........................................................................................................... 8

SWOT Analysis .................................................................................................................................... 9

Limitations of SWOT Analysis .......................................................................................................... 9

3. Business and Financial Analysis .................................................................................................. 10

Company Overview .......................................................................................................................... 10

3.1 McDonald’s SWOT Analysis ........................................................................................................ 10

Strengths ............................................................................................................................................. 11

Weaknesses ......................................................................................................................................... 11

Opportunities ..................................................................................................................................... 11

Threats ................................................................................................................................................ 12

3.2 Ratio Analysis ............................................................................................................................... 13

Revenue Growth ................................................................................................................................. 13

Profitability Ratios ............................................................................................................................. 14

Liquidity Ratios .................................................................................................................................... 19

Debt Management Ratios .................................................................................................................. 22

Asset Management Ratios ................................................................................................................ 23

McDonald’s Market Value Summary ................................................................................................. 26

Conclusion .......................................................................................................................................... 28

Skills and Learning Statement .......................................................................................................... Error! Bookmark not defined.
1. Project objective and overall research approach

1.1 Introduction

The topic which I have chosen for my research and analysis report is Topic No: 8

“The business and financial performance of an organization over a three year period”

The organization on which this RAP would be conducted is McDonald’s Corporation.

1.2 Reasons for Choosing the Topic and Organization

The most important aspect when choosing the topic is one’s personal interest. I was always interested in finding out the success factors of different businesses and to get an insight into its business and financial performance. The topic was also important for me as it is somewhat part of my work. Through completing this RAP I wanted to develop my analysis and reporting skills which are vital for my career progression. Gaining the complete understanding, knowledge and skills to execute the project is of utmost importance. The knowledge which I gained through my ACCA studies and work assignments gave me an extra comfort towards choosing this topic.

The chosen company for this purpose is McDonald’s Corporation. That has demonstrated significant growth and sustainability as the Market Leader in Fast Food Industry. The purpose of the analysis is to find out the trend that McDonald’s has demonstrated in the key areas where they have excelled.

1.3 Project Objectives

This report aims to analyze the financial results of McDonald’s over a five year period and to compare it with its competitor Burger King. They represent two big names in the Food Industry. They are very much related to each other. The types of food they serve are somewhat similar. This analysis will mainly be accomplished by conducting a detailed ratio analysis on the financial data available for the last five year period.

The financial analysis of McDonald’s should give us a peek into the future not just of the company but also as to what lies in store for us at the stock exchanges and on the economic front. Such is the broad and dimensional measure of McDonald’s.
Looking on the financial aspect alone will not provide a comprehensive analysis of its performance. Therefore, this report will also focus on the non-financial aspects using a strategic planning tool called SWOT analysis which will look into the strength, weaknesses, opportunities and threats inherent in the company or faced by it.

### 1.4 Research Questions

The aims and objectives of the report on which my research questions were based are as follows:

1. To gather, present and analyze the financial information of McDonald’s for the last 5 years in a form which can assist an investor to assess the overall financial performance and prospects of the organization.

2. To analyze the strengths, weaknesses, opportunities and threats which have resulted from the current strategy and their impact on the company as a whole?

3. What are the key financial drivers, business strengths and strategies that led to McDonald’s significant growth and sustainability as the Market Leader in Fast Food Industry?

4. To develop analytical skills and to apply gained financial knowledge to the business environment.

For the execution and completion of this project following questions were to be answered:

1. Identify the sources from where the information will be gathered about the topic i.e. which sources would be used to access the data and information?

2. Which technical issues would arise and how to address them?

3. What mechanism should be followed in execution of the analysis?

4. What sort of IT and Communication skills would be required?

### 1.5 Research Approach

The first step before execution of any project is to plan. Planning is the core for gaining success in any task. My objective was to complete the RAP before the submission deadline for this I set a target date before which I should complete each task and set mile stones. This helped me in visualizing the issues which I might face during my work and possible solutions for each. If I don’t have a solution for a problem then from where I can seek help for resolving this issue. I selected the techniques that could be used to work on the RAP. I used different sources to gather information and summarize data. Most of the time I relied on the Internet, moreover I got knowledge from books, newspapers and business articles. The critical question which I had to answer all the time during gathering information was to
differentiate what information is most important, relevant and must be mentioned or not to be disclosed.

The approach was to analyze the last 5 years financial statements of both the companies and trend analysis that will show the growth in the business of two companies and will compare the results. For this purpose I have gathered the information from the annual reports and other data available in the public domain. I read wide variety of news articles, analysis, companies press briefs, various reports and commentaries from various different sources. For the purpose of this report I relied on secondary data, few attempts were made to gather primary data but to no avail. Various sources were used to find reliable, accurate and unbiased information. I then collected information on the methods and sources that I could use for effective secondary research.

The next phase was the most important one as I required me to carry out actual, target oriented research on the topic The methodology was to analyze the financial ratios which are classified into following categorize:

- Profitability Ratios.
- Liquidity & Debt Management Ratios.
- Asset Management Ratios.

Market Value analysis would be carried out in which following indicators will be analyzed:

- Market price (by New York stock exchange, closing price)
- Cash flow per share
- Price / Cash flow per share (P/CF)
- Book value per share (BVPS)

In the end a SWOT analysis of McDonald’s was carried out and a conclusion is drawn. I made a check list and ticked off each of my project objectives and research questions that I felt had been answered upon the completion of the project.
2. Information Gathering

2.1 Sources of Information

Following sources of information were used due to the mentioned reasons.

<table>
<thead>
<tr>
<th>Source</th>
<th>Reason</th>
</tr>
</thead>
</table>
| Internet                      | • Easily accessible  
                               | • Reliability (E-Journals)  
                               | • Citable and verifiable  
                               | • Access to multiple & differing opinions  
                               | • Easily searchable  
                               | • Up to date information  
                               | • Access to extensive analysis & comments. |
| Annual Report                 | • Audited accounts which are reliable  
                               | • Extensive information about company performance  
                               | • All financial reports available in single report. |
| Personal communication        | • Efficiency  
                               | • Effectiveness in getting desired information  
                               | • Cost effective primary source of information, when directed at appropriate sources |
| through meetings and telephone|                                                                 |
| Books                         | • Detailed guidance  
                               | • Citable and authentic theoretical concepts. |
| Investor reports, Newspapers &| • Analysis and comments  
                               | • Up to date information. |
| Magazines                     |                                                                 |

2.2 Methods of Information Gathering

Internet

One of the most popular software which helped me most in searching through the websites was the “Google Toolbar”, sitting under my internet explorer address bar providing me immediate searches, whenever I needed them.

Apart from gathering information from McDonald’s and Burger King Websites, I also extracted information and enhanced my understanding from website such as www.investopedia.com and www.ventureline.com as in their own words they say it is:
“for professionals and students alike to find MBA-level tools and current data with which to conduct near instantaneous fundamental financial ratios analysis on any business entity and the industries in which they compete.” (Ventureline, 2012)

I used these tools more often when I was reading around my topic. Later on, I essentially leached on to a few other websites as they provided me with most of the relevant information.

Additionally, I used to McDonald’s and Burger King Websites to get their Annual Report and commentaries.

**Personal Communication**

It was also possible for me to benefit from the valuable time of my highly qualified colleagues, manager and lecturers. They were not acting as my mentors but we had general conversations over various topics related to my project in which they specialized individually by arranging meetings with them. Whenever I faced any difficulty or required some information they were only a phone call away.

**Books**

I faced some problems in referring to books as the public libraries in Jeddah, Saudi Arabia do not hold relevant books. So I had to rely on my academic books of ACCA and CMA. I also borrowed some books from friends and colleagues at work, further more I downloaded e-books from the internet.

**Investor reports, Newspapers & Magazines**

These were a useful source of commentaries, analysis and reviews. I didn’t really have to dig into micro-fiches as I was working on rather recent reports. I had done my homework as to which articles I was looking for by looking up in the investor’s database and websites. All I had to do was locate the issue I needed and make notes.

**2.3 Limitations of information gathering**

Information gathering was the lengthiest and most time consuming process of all as the information gathered was either difficult to classify as relevant to RAP or reliable and authentic. Most of the financial information was collected from McDonald’s and Burger King Websites which may be favorably biased towards the company. Some sources of information may contain research carried out with different objectives than this Report. It is difficult to judge whether such information should be sued for the purposes of this Report or not. The financial statements of the company may be a bit favorably biased towards the company as through these the company aims to present itself in the best possible manner. Searching the information from the internet was difficult to say as reliable and it took too long to have access to most appropriate and relevant information.

**2.4 Ethical Issues faced during information gathering**

The issue of plagiarism was the one which I faced. As nearly all my research is based on secondary data, there was a risk of plagiarism if any information that was used was not properly referenced. I
took special care by properly referencing the data, information and quotations which were not my own. I used the Harvard Referencing System to eliminate beyond any possible doubt any chance of plagiarism. I also followed the IFAC code of ethics adopted by ACCA, ensuring that I am following the guidelines and taking appropriate measures such as: competence and due care, professional behavior and confidentiality.

### 2.5 Accounting and Business Techniques used and their Limitations

#### Ratio Analysis

A tool used by individuals to conduct a quantitative analysis of information in a company's financial statements. Ratios are calculated from current year numbers and are then compared to previous years, other companies, the industry, or even the economy to judge the performance of the company. Ratio analysis is predominately used by proponents of fundamental analysis. (Investopedia, 2012)

Ratio analysis is more than comparing different numbers from the balance sheet, income statement, and cash flow statement. It includes comparing the numbers against previous years, other companies, the industry and the economy in general. Ratios look at the relationships between individual values and relate them to how a company has performed in the past, and might perform in the future.

Ratio analysis helps in the following ways:

- It helps in making investment decisions by looking at various ratios.
- It simplifies the comprehension of financial statements. It provides a fairly complete picture of the various changes in the financial condition of a business.
- It facilitates in making inter-company comparison and highlights the factors which are commonly associated with successful and unsuccessful firms.

The details of each of these ratios are mentioned in the Analysis segment of this Report and their calculation formulas are provided in the Appendix 3.

#### Limitations of Ratio Analysis

Ratio analysis has a number of limitations which are as follows:

- No single ratio, or measure, is capable of capturing all relevant or important information about a particular company.
- The calculation of various ratios is merely the starting point. Analysis requires thinking about these ratios, forming expectations and understanding the reasons of variances from those expectations. There is no overarching rule of what a ratio ought to be, and it depends on the particular industry as well as the business model.
The validity of ratios also depends on the validity of the numbers used in the calculations. If the business’s accounting system cannot be relied upon to produce reliable figures, ratios are also unreliable.

In addition to internal factors that affect ratios, it is essential to understand the status of external conditions, such as business conditions, and industry position.

Uses of different accounting methods (depreciation, inventory valuation method, etc.) make comparability difficult. Seasonal fluctuations should be considered.

The possibility that the firm has engaged in “window dressing” also can present a challenge. An internal accountant may be motivated to increase net income and to use decisions at their discretion (depreciation, etc.) to affect the results of the firm’s financial statements.


**SWOT Analysis**

SWOT is an acronym for Strengths, Weaknesses, Opportunities and Threats. By definition, Strengths (S) and Weaknesses (W) are considered to be internal factors over which you have some measure of control. Also, by definition, Opportunities (O) and Threats (T) are considered to be external factors over which you have essentially no control. (Management Study Guide, 2012)

A SWOT analysis is carried out in this Report as the main business technique used to analyze internal and external factors which have an impact on the company. It looks into the internal business strategies and business decisions made by management. The external factors are also analyzed such as the economic environment and the industry structure etc.

**Limitations of SWOT Analysis**

SWOT analysis is not free from its limitations. A truly successful SWOT analysis should extend beyond a simple list of strengths, weaknesses, opportunities and threats. A detailed SWOT analysis should also look at an opportunity or threat’s size in order to see how it is related with the company’s strength and weaknesses.

While useful for reducing a large quantity of situational factors into a more manageable profile, the SWOT framework has a tendency to oversimplify the situation by classifying the firm's environmental factors into categories in which they may not always fit. The classification of some factors as strengths or weaknesses, or as opportunities or threats is somewhat arbitrary. For example, a particular company culture can be either a strength or a weakness. A technological change can be a threat or an opportunity. Perhaps what is more important than the superficial classification of these factors is the firm’s awareness of them and its development of a strategic plan to use them to its advantage. (Net MBA, 2012)
Although SWOT analysis is considered to be a simple and straightforward, more research and analysis is usually needed in order to obtain a comprehensive picture.

3. Business and Financial Analysis

Company Overview

The business began with two brothers. In 1940, Dick and Mc McDonald opened McDonald’s Barbeque restaurant in San Bernardino California selling hamburgers. It is a typical drive-in featuring a large menu and car hop service. By 1948 brothers had made a fortune they never expected. The brothers realized that hamburgers comprised 80 percent of their sales and closed their doors to re-evaluate their business model. The same year, in 1948 the model was about affordable dining for family who wanted to eat out. The “Speedy Service System” was also implemented that included an assembly line of sorts, a nine-item menu hamburger, cheeseburger, soft drinks, milk, coffee, potato chips and a slice of pie.

In 1954 Ray Kroc visited McDonald’s he was surprised by a huge order for 8 multi-mixers from a restaurant in San Bernardino, California. There he found a small but successful restaurant run by brothers Dick and Mac McDonald, and was stunned by the effectiveness of their operation. Kroc pitched his vision of creating McDonald’s restaurants all over the U.S. to the brothers. The brothers were reluctant at first to begin a national franchise system, but soon realized that too many copycats were creeping up and they needed an advantage and a head start. In 1955 he founded the McDonald’s Corporation, and 5 years later bought the exclusive rights to the McDonald’s name. By 1958, McDonald’s had sold its 100 millionth hamburger. (McDonald’s, 2012)

McDonald's is the leading global foodservice retailer with more than 32,000 local restaurants serving more than 64 million customers in 117 countries each day. More than 80% of McDonald's restaurants worldwide are owned and operated by independent local men and women. It has a work force of 1.7 million employees worldwide. (McDonald’s, 2012)

3.1 McDonald’s SWOT Analysis

ACCA/ Oxford Brookes Research and Analysis Project
Strengths

The business is ranked number one in Fortune Magazine’s 2011 list of most admired food service companies. (CNN Money, 2011)

One of the best brand recognition in the world, the golden arches and Ronald McDonald. McDonalds is a community oriented, socially responsible company. They run Ronald McDonald House Charities (RMHC) helping more than 4 million families a year (RMHC, 2012).

McDonald’s believe in empowering its staff with the best knowledge and skills. In 1961 McDonald’s established Hamburger University; today more than 5,000 students attend Hamburger University each year. Since 1961, more than 80,000 restaurant managers, mid-managers and owner/operators have graduated from this facility. (McDonald’s, 2012)

McDonald’s has an efficient, assembly line style of food preparation. In addition they have a systemization and duplication of all their food prep processes in every restaurant. McDonald's uses only 100% pure USDA inspected beef, no fillers or additives. Additionally the produce is farm fresh. McDonald’s serves 100% farm raised chicken no fillers or additives and only grade-A eggs. McDonald's foods are purchased from only certified and inspected suppliers. McDonalds works closely with ranchers, growers and suppliers to ensure food quality and freshness. (McDonald’s, 2012)

Weaknesses

Their test marketing for pizza failed to yield a substantial product. Leaving them much less able to compete with fast food pizza chains.

High employee turnover in their restaurants leads to more money being spent on training. (Novak, J. 2009)

Most of their employees working in their restaurants are either student or part-timers, they don’t see working in McDonald’s as there carrier.

McDonald’s might be reaching its saturation point where it won’t be possible to grow even further which could be a potential risk.

The company faces many risks, such as interest rates, inflation, foreign exchange rates and industry regulations. In addition, slowing economies, rising unemployment, current economic conditions, declining wages, constrained credit and volatile financial markets make it even harder to compete in the marketplace.

Opportunities
The introduction of a healthy hamburger is a great opportunity in today's health conscious societies. They would be the first QSR (Quick Service Restaurant) to have FDA approval on marketing a low fat low calorie hamburger with low calorie combo alternatives. They could also provide optional allergen free food items, such as gluten free and peanut free.

They have industrial, Formica restaurant settings; they could provide more upscale restaurant settings, like the one they have in New York City on Broadway, to appeal to a more upscale target market. (Novak, J. 2009)

There is a huge market for HALLAL Food (Lawful food for Muslims according to Islamic Laws) especially in UK and most of the European countries with large Muslim population. For example KFC has restaurants in UK serving HALLAL Food.

Changing trends in eating habits toward more healthy eating, seen as a threat to McDonald’s can also be seen as an opportunity. McDonald’s introduced new premium salads and Fruit n’ Yogurt Parfaits in the US which lead to growth in 2004 and the same products will probably bring some more growth in foreign markets. (Anne, O et al., 2005)

### Threats

McDonald's franchise remains at the forefront of child-directed marketing, a source of concern for both consumer groups and parents who believe that McDonald's purposely markets unhealthy food to children. They entice children as young as one year old into their restaurants with special meals, toys, playgrounds and popular movie character tie-ins. Children grow up eating and enjoying McDonalds and then continue into adulthood.

Health conscious consumers demanding better quality and healthier menu items. All fast-food chains expected to struggle to meet new consumer health expectations. This shows an overall weaker industry.

They have been sued multiple times for having "unhealthy" food, allegedly with addictive additives, contributing to the obesity epidemic in America. (Novak, J. 2009) Any new legislation or law which may ban any restaurant from serving unhealthy food could be a potential threat to McDonald’s.

Increased competition among rival sellers, including price wars, product innovation, and growth. Down turn in economy is affecting the ability to eat out as much. Especially in countries where there is a poor economy.
3.2 Ratio Analysis

Revenue Growth

<table>
<thead>
<tr>
<th>Years</th>
<th>McDonald's Revenue</th>
<th>Increase/(Decrease) in Revenue</th>
<th>Burger King Revenue</th>
<th>Increase/(Decrease) in Revenue</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>$22,787</td>
<td>9%</td>
<td>$2,234</td>
<td>9%</td>
</tr>
<tr>
<td>2008</td>
<td>$23,522</td>
<td>3%</td>
<td>$2,455</td>
<td>10%</td>
</tr>
<tr>
<td>2009</td>
<td>$22,745</td>
<td>-3%</td>
<td>$2,537</td>
<td>3%</td>
</tr>
<tr>
<td>2010</td>
<td>$24,075</td>
<td>6%</td>
<td>$2,502</td>
<td>-1%</td>
</tr>
<tr>
<td>2011</td>
<td>$27,006</td>
<td>12%</td>
<td>$2,336</td>
<td>-8%</td>
</tr>
</tbody>
</table>

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

McDonald’s is showing a strong growth trend. “This was achieved by introducing new menu items like Chicken McNuggets that featured new sauces, breakfast products including new Fruit & Maple Oatmeal and limited-time offering such as the McRib sandwich. In US the National launch of the McCafe’ Frozen Strawberry Lemonade and Mango Pineapple real-fruit smoothie provided an extra boost in revenues. Apart from that the extended opening hours and customer-focused Plan to Win. The execution of multiple initiatives surrounding the five elements of Plan to Win- People, Products, Place, Price and Promotion – have enhanced the restaurant experience for customers worldwide and grown comparable sales and customer visits in each of the last eight years. This Plan, combined with financial discipline, has delivered strong results”. (McDonald’s, 2011)
The Burger King revenues are showing a healthy growth during 2007, 2008 and 2009 of 9%, 10% and 3% respectively. In 2010 and 2011 it has decreased by 1% and 8% respectively.

“In 2011 Company restaurant revenues decreased primarily due to the reduction in refranchising of 38 Company restaurants and the effects of negative company comparable sales growth”. (Burger King, 2011).

**Profitability Ratios**

**Net Profit Margin**

“A ratio of profitability calculated as net income divided by revenues, or net profits divided by sales. It measures how much out of every dollar of sales a company actually keeps in earnings.” (Investopedia, 2012)

![Net Profit Margin McDonald's Vs Burger King](chart.png)

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

McDonald’s is demonstrating significant growth in profitability especially during the last 3 years the growth is above 20% on average. This performance is achieved because the franchised revenue has increased from $7842m in 2010 to $8713m in 2011 and as it is evident from the financial statement that McDonald’s Corporation directly does not bears any expenses of the franchised restaurants but enjoys the revenue and profits from it.

As we see that the net profit margin is 20% but the gross profit margin is 45% (difference 25%) which indicates that there are heavy non-operating expenses and in my view the reasons for these expenses include the following factors:

- Staff training expenses
Cost of moving towards green environment. (McDonald’s, Corporate social responsibility)

The net profit of Burger King is poor due to following reason:

- Due to the acquisition of Burger King the revenue has declined which might be because of restructuring of key managerial positions and change in the strategy.
- The assets of Burger King could also be another reason as evident from the financial statements of Burger King the assets have increased 121% from 2007 to 2011, whereas the net income has not increased in line with the increase in assets.

**Gross Profit Margin**

“Gross profit margin indicates the percentage of revenue available to cover operating expenditures”.


<table>
<thead>
<tr>
<th>Year</th>
<th>McDonald’s</th>
<th>Burger King</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>39.69%</td>
<td>36.93%</td>
</tr>
<tr>
<td>2008</td>
<td>41.96%</td>
<td>37.35%</td>
</tr>
<tr>
<td>2009</td>
<td>44.38%</td>
<td>35.21%</td>
</tr>
<tr>
<td>2010</td>
<td>45.76%</td>
<td>35.46%</td>
</tr>
<tr>
<td>2011</td>
<td>45.06%</td>
<td>38.05%</td>
</tr>
</tbody>
</table>

(Gross profit margin indicates the relationship between Gross profit and sales. A higher Gross profit ratio of both McDonald and Burger King indicates that both the companies are using a mix of higher product pricing and lower product costs. The possible reason for this could be the competitive advantage both the company is enjoying over others in areas of brand, quality and food technology. Also due to economies of scale they have bargaining power and good credit terms against their vendors.)
**Basic Earning Power (BEP)**

“This ratio is often used as a measure of the effectiveness of operations. Basic Earning Power measures the basic profitability of Assets because it excludes consideration of interest and tax.” (Ventureline, 2012)

![Basic Earning Power McDonald's Vs Burger King](chart.png)

(Data Extracted from McDonald's Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

The reason for this increase in BEP of McDonald’s is the affective use of premises and assets rather than purchasing of too many assets and do not use them affectively. The increase in revenue of McDonald’s and the decrease in the revenue of Burger King creates a gap in the market which is affectively used by McDonald’s from its unique products that is why the earning increased rapidly without investing in too many assets. We can also say that McDonald’s is investing in human asset instead rather than fixed assets. On the other hand Burger King do not focuses in maintaining its revenue rather than it is heavily investing in assets which has increased there depreciation expense, interest expense (if asset is purchased on loan) that’s why they are not focusing on training and developing their staff which have to serve their customers.
**Return on Assets (ROA)**

“Return on investment (ROI) and Return on Assets (ROA) are measures of a business’s efficiency in using its assets to create profits”. (CMA Learning System Part2: Financial Decision Making, 2010, p. 36)

![Return on Asset McDonald's Vs Burger King](image)

(Data Extracted from McDonald's Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

The above graph shows that McDonald’s is earning 17% profit from its assets. This indicates that the McDonald’s is using its assets affectively to earn profits but further investigation should be done in this matter that are the assets of McDonald’s is so old that they need replacement within a few years so weather McDonald’s has made a plan to replace the old assets or not. As we know that as the assets get older the net book value decreases and the profits earned on those assets increases.

If we analyze Burger King Performance from the above ratio we can see the declining phase of Burger King life cycle. We can conclude that during 2007 to 2010 it showed a modest growth, however in 2011 it is showing a sudden drop. When it comes to ROA or BEP ratios the year 2010 is not comparable because Burger King was taken over by 3G Capital and the total assets size has increased abnormally because of the increase in intangible assets specially goodwill.
Return on Equity (ROE)

“Return on equity measures a corporation's profitability by revealing how much profit a company generates with the money shareholders have invested.” (Investopedia, 2012)

<table>
<thead>
<tr>
<th>Percentage</th>
<th>Return on Equity McDonald's Vs Burger King</th>
</tr>
</thead>
<tbody>
<tr>
<td>2007</td>
<td>15.67%</td>
</tr>
<tr>
<td>2008</td>
<td>32.23%</td>
</tr>
<tr>
<td>2009</td>
<td>32.43%</td>
</tr>
<tr>
<td>2010</td>
<td>33.80%</td>
</tr>
<tr>
<td>2011</td>
<td>38.24%</td>
</tr>
</tbody>
</table>

(Data Extracted from McDonald's Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

McDonald’s again is showing a very impressive performance in terms of ROE. The average of last 4 years is above 32% especially in 2011 it reached to 38%. The major drivers behind this performance are as follows:

- Excellent increase in revenues
- Good control over costs and
- A balanced capital structure

This has resulted in achieving a consistent ROE by McDonald’s over the last 4 years.

If we analyze the performance of Burger King in terms of ROE we find that the performance was good during 2007 to 2009 and after that it is showing a declining trend. ROE average during 2007 to 2009 was above 20% however when we compare it to McDonald’s it is still on the lower side. The main cause of decline in ROE is the increase in Shareholder’s equity of $474m in 2011. As in 2009 it was $975m and in 2011 it increased to $1449m. The increase in shareholder’s equity is mainly because of the takeover of Burger King by 3G Capital. Compared to $474m increase in equity the net income has declined by $93m in 2011 compared to 2009. Due to decrease in sales from company
operated restaurant as evident from its financial statements as well as increase in Shareholder’s equity of $474m in 2011 from 2009 due to takeover of Burger King by 3G Capital in 2010.

**Liquidity Ratios**

**Current Ratio**

“The current ratio measures the adequacy of current assets to meet the company’s short term liabilities. It reflects whether the company is in a position to meet its liabilities as they fall due.”


(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

In the last 5 years the average is above 1 and since McDonald’s is in cash retail business therefore a ratio above 1 is healthy in this industry. This reflects a good working capital management by McDonald’s. The performance of Burger King in terms of current ratio is inconsistent and does not correspond with McDonald and even the benchmark of 1:1.
Quick Ratio

“The quick ratio, or acid-test ratio, examines liquidity from a more immediate aspect then does the current ratio by eliminating inventory from current assets.” (CMA Learning System Part2: Financial Decision Making, 2010, p.17)

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

McDonald’s is showing a better performance in terms of quick ratio during the years 2008 to 2010 and since last 4 years the ratio is above 1 which is a good indicator of having liquidity. The performance of Burger King in terms of quick ratio reflects that except for 2011 in all the years it was below 1 and it was almost in the same range. McDonald’s has more liquidity compared to Burger King. The interesting point is that the inventory levels are not significant in total composition of current assets for both the companies because the difference between current ratio and quick ratio is not significant.
**Defensive Interval Ratio**

“This ratio measures how long the company can continue to pay its expenses from its existing liquid assets without receiving any additional cash inflow”. (CFA Program Curriculum. Volume 3. Financial Reporting and Analysis. Pearson Custom Publishing, 2009, p. 508)

An average defensive interval ratio of 80 and 70 would indicate that McDonald and Burger King respectively, can continue to pay its operating expenses for 80 and 70 days respectively before running out of quick assets, with the assumption that there would be no additional cash inflows. This indicates that both the companies are enjoying similar liquidity position also reflected from other liquidity ratios.
Debt Management Ratios

Debt Ratio

“A ratio that indicates what proportion of debt a company has relative to its assets. The measure gives an idea to the leverage of the company along with the potential risks the company faces in terms of its debt-load.” (Investopedia, 2012)

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

If we look at the ratios of McDonald and Burger King we can say that both have identical average debt ratio of 0.34 and is enjoying the same leverage level and borrowing capacity. However if we look at the trend of both entity we see that during the last 5 years McDonald’s debt ratio has remained in almost the same rang during the last 5 years that shows a balanced capital structure of McDonald whereas Burger King is opposite to that of McDonald having great volatility in terms of debt.
**Asset Management Ratios**

**Inventory Turnover**

“In accounting, the **Inventory turnover** is a measure of the number of times inventory is sold or used in a time period such as a year.” (en.wikipedia, 2012)

The above graph in isolation shows that Burger King is more efficient in terms of inventory management compared to McDonald’s. However if we correlate this ratio with growth trend it is evident that growth trend of Burger King is decreasing YOY basis which is a clear sign of inadequate inventory level. As we can see from the financial statements of Burger King for the last 5 years inventory has been decreasing from $15m in 2007, $16m in 2008, $15.80m in 2009, $15.60m in 2010 and $13.70m in 2011.

(For Ratio Calculation and Formulas Please see Appendix 2)
**Fixed Asset Turnover**


![Fixed Asset Turnover Ratio McDonald's Vs Burger King](image)

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

McDonald’s has invested in its fixed asset to support the expansion that is why the fixed asset turnover is less than Burger King but it is improving its fixed asset turnover on the other hand Burger King has maintained its fixed asset turnover but after the acquisition its fixed asset turnover has declined from 2.47 to 2.27. In the future the McDonalds would improve its fixed asset turnover by attracting more customers in those countries where it established its premises recently for example China and Russia.
**Total Asset Turnover**

“Asset turnover is a financial ratio that measures the efficiency of a company's use of its assets in generating sales revenue.” (en.wikipedia, 2012)

![Graph of Total Asset Turnover McDonald's Vs Burger King](chart.jpg)

(Data Extracted from McDonald’s Corporation Annual Report 07, 08, 09, 10 & 11. Burger King Annual Report 07, 08, 09, 10 & 11. For Ratio Calculation and Formulas Please see Appendix-2)

One of the reasons for not having a high total asset turnover of McDonald’s is its expansion plans because in the growth path new restaurants generates lesser revenue but have the same value of the assets and as they become mature the revenue starts coming in. So the strong expansion plans of McDonald’s are one of the reasons for having a comparatively low total asset turnover ratio. (McDonald’s, 2011).
When we look at the numbers of Burger King in terms of total asset turnover it is showing a better performance than McDonald’s till 2010, however because of acquisition made in 2010 the total assets increased therefore the total asset turnover figure has dropped to more than half in 2011. Total Fixed Asset Turnover ratio of Burger King is not comparable with McDonald’s because of expansion plan of McDonald’s as evident from Fixed Asset Turnover Ratio and Total Asset Turnover Ratio.

In my view the new management of Burger King is not competing with McDonalds in an effective way it could be because lack of experience in this industry or they have not studied the market factors that lead to a successful company because every decision made after the acquisition has declined the financial and non-financial position of Burger King which is also evident from the drastic decline of Total asset turnover.

**McDonald’s Market Value Summary**

(Graph extracted from Yahoo finance, 2012)

**Market Share Price** As per the NYSE the closing price for the year 2011 of McDonald’s share was $94.87/share. For the year 2010 it was $80.94/share and price of 2011 reflects higher investor confidence in the company. Last 6 years average share price of McDonald’s was $68.70/share which means year 2010 and 2011 has shown excellent growth. (NYSE, 2012)
As per the NYSE the closing price for the year 2011 of Burger King Share was $24/share. For the year 2010 it was $24.00/share which is not a very good indicator if we compare the share price with 2007 and 2008 it was $28.71 and $24.12 respectively which shows that the shares of Burger King are performing badly in the market. If we compare the share price of McDonald’s then we can see that there is a difference of $71.00 which shows that McDonald’s shares are trading way higher than that of Burger King. (Advfn, 2012)

**Earnings Per Share (EPS)** of McDonald’s is showing high value i.e. $5.39/share (165m shares) in 2011. Compared to last year 2010 it was $4.69/share. If we see the historical EPS of McDonald’s it is showing a $3.86 as an average in last 6 years which indicates that EPS is improving for McDonald’s strong earnings growth of 20% plus is the main driver for this growth.

EPS of Burger King has declined to $0.79/share in 2011 compared to 2010 which was $1.37/share. The historical EPS of Burger King for last 6 years is showing $1.07 as an average which indicates that Burger King is also paying back to its shareholder but compared to McDonald’s it’s quite less.

**Price Earning Per Share (P/E)** of McDonald’s in year 2011 was $17.60/share and $17.25/share in year 2010 respectively which is an increase of $0.35/share. If we see the historical data of McDonald’s PE the average comes around $18.79/share in the last 6 years. This means a declining trend in 2011.

Burger King’s Price Earning is showing an upward trend in 2010 and 2011 this is mainly because of the acquisition that happened. The average P/E of Burger King is around $20.79 for the last 5 years compared to McDonald’s that has an average of $19.51.

**Cash Flow per share** of McDonald’s for the year 2011, 2010 & 2009 per share was $6.78, $5.90, and $5.35 respectively. It reflects the strength of McDonald’s and sustainability of its business model. The average Cash flow per share for the last 5 years is $5.22 which shows the strength of McDonald’s in its cash flow per share.

Cash flow per share of Burger King for the year 2011, 2010 & 2009 per share was $1.79, $2.20 and $2.21 respectively. The average for the last 5 years is $2.02/share. The decline in 2011 is a cause of concern for the investors and would negatively affect the company’s ability to raise capital for its future expansion plans.

**Price/ Cash flow per share** of McDonald’s for the year 2009, 2010 & 2011 per share was $11.96, $13.71 and $14.00 respectively. It shows the investment attractiveness to the investors as this metric compares the stock's market price to the amount of cash flow the company generates on a per-share basis. The average of last 5 years is also standing at an impressive $14.63.

Price/ Cash flow per share of Burger King for the year 2009, 2010 & 2011 per share was $8.65, $10.93 and $13.38 respectively an improvement of $2.45 per share in 2011. Last 5 years average is $12.12/per share. Although it has showing an increasing trend in the last 3 years but it is still lower than McDonald’s which is $14.00/per share.
Book Value per share of McDonald’s for the year 2009, 2010 & 2011 per share was $13.03, $13.88 and $14.09 respectively. It shows that the market price of McDonald’s is growing the reasons behind this are maintaining good cash flows, market strategies and shareholders’ equity. The average of last 5 years is $13.23.

Book value per share of Burger King in 2011 is $10.67/share which has increased compared to 2010 which was $8.30/per share. For the 5 years the average is $7.56/share. Although the BVPS is constantly increasing each year but still it is less than McDonald’s which is enjoying a BVPS of $14.09 per share.

Conclusion
Based on the respective performance of the two companies it can be concluded that McDonald’s is performing much better than Burger King in Fast Food Retail Industry and that is why it has been ranked number one fast food chain in the world. It has shown strong sales growth impressive profitability trend and a strong balance sheet. The market value of the shares and other equity ratios are also very good for McDonald’s, overall it is a very professional company having a solid performance during the last 5 years. Revenue growth in various parts of the world and its revitalization initiative the “Plan to Win” is yielding great results.

Burger King has shown mixed results in some years it has shown significant improved performance on the other hand it has shown decline in some important ratios during some years. In year 2010 it has been taken over by 3G Capital so the year 2010 is not right benchmark to compare with previous years and when it compares to McDonald’s then McDonald’s appears to be much stronger company in terms of financial ratios and overall business performance.