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Financial Exposure of McDonald's Corp. Success as a Market Leader

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Abstract

The purpose of this study is to explore the financial aspects of McDonald's success as a market leader despite of the global recession and tough competition offered by Yum brands. Financial ratio analysis, horizontal analysis, vertical analysis and DuPont analysis are applied for 9 years financial data of McDonald's. And it is discovered that efficient operations, strong short and long term solvency position, high profitability, highly loyal customer, broader network expansion and the value adding menu are major factors of its success. But it has to improve its asset utilization efficiency to remain No. 1 in highly competitive fast food industry. The expected learning outcomes of this case study is to illustrate the success factors, particularly in financial terms which provides a strong base for a business organization to maintain its competitive position & leadership. The readers are expected to be able to get an understanding of the following terms at the completion of this study: an understanding of calculation and interpretation of basic financial ratios and its implications for financial managers, investors and creditors; the significance of various financial analysis for a business organization, the importance of understanding the external business environment and how that environment poses threats as well as new opportunities for the businesses operating in it. This case study is designed for the students of BBA/MBA and helpful in the courses of corporate finance and financial reporting analysis.

Keywords: Financial Ratio Analysis, Horizontal Analysis, Vertical Analysis, DuPont System of Analysis.

1. Introduction

McDonalds started only as a small stall of hamburger in California, owned by Dick and Mac McDonald. To increase their business they closed their small business for 3 months and in 1948 they reopened as a self-service restaurant, and at that time they only served 9 items such as slices of pie, coffee, milk, potato chips, cheeseburgers and hamburgers. Now it has grown to be a dominating and powerful multinational corporation operating in 119 countries with more than 31,000 restaurants and1.5 million employees, which serve more than 46 million customers per day. The aim of the McDonald's is to grow into buyer's most beloved place to dine with their world's most favorite and famous Chicken Mac Nuggets, Quarter Pounder, Big Mac and French-fries (James, 2009).

In food industry, McDonald's has been ranked as a leading and the number one fast food chain worldwide and across industries McDonald's ranks top three American brands. McDonald's uses Dow Jones Industrial Average (DJIA) companies as the group of comparison and they believe it is an appropriate way of comparing. McDonald's is also included in Standard & Poor's 500 Stock Index. Currently company's share price is $96.45. The corporation is treated as separate geographical sections or areas. Most significant areas are Asian/Pacific & Europe, Africa and Middle East (APMEA) and the United States & these segments accounted as 39%, 23% and 32% of total revenues respectively. The United Kingdom, Germany and France both accounted as 51% of China & Europe's revenues and Japan and Australia both accounted as 56% of (APMEA's) income. These 6 areas in the United States and Canada are also stated as key areas of the market, which covers 70% of total profits (McDonald's, Corp., 2012, p. 11).

Table.1 Condensed Statement of McDonald's Financial Performance

Years	2012	2011	2010	2009	2008	2007	2006	2005	2004
Sales-($)	27,567	27,006	24,075	22,745	23,522	22,787	20,895	19,117	17,889
Net Earnings-($)	5,465	5,503	4,946	4,551	4,313	2,395	3,544	2,602	2,279
Total Assets-($)	35,387	32,990	31,975	30,225	28,461	29,392	28,975	29,989	27,838
Market Price Per Share-($)	88.21	100.33	76.76	62.44	62.19	59.91	44.33	33.72	32.06

Note. 6 year financial summary from McDonald's Corp.'s Annual Report (2012), 6 year financial summary from McDonald's Corp.'s Annual Report (2009).

McDonald Corporation's sales and profitability show an even or stable pattern with slight ups and downs. McDonald's income/revenue consists of payments of franchises operating McDonald's restaurants & sales generated by restaurants operated by corporations. For the last 37 years, McDonald's is continuously paying its dividends on common stock and every year they increased the amount of dividend and there is an increase of 10% in the three-monthly dividends, which are equal to 3.08$ per share yearly dividend and it reveals the corporation's self-confidence in the on-going reliability and strength of its money now it is the world's leading fast food chain in with a total world's sale of 8% (McDonald's Corp., 2012, pp. 12). As well as Mcdonald's total assets are also increasing yearly and market price per share also show a positive increasing trend till 2011 but it reduced in 2012 as shown in table 1.

Overall food industry is continually growing through increased revenues & volume expansion. Company segmented into 2 main segments or section includes full-services and fast food restaurants. Every segment has to cope with the other restaurants operating in the similar geographic zone. Industry of fast food chains is full of competition. McDonald's corporation has to cope with other food chains in terms of what customers perceive value in terms of food products offered in restaurants and through a variety of food, price, accessibility and quality. The McDonald's has to cope with the following main competitors.

- Yum Brands
- Domino's.
- Wendy's International

- Jack in the Box
- Doctor's Associates
- Burger King Corporation

These companies generate around $120 billion yearly revenues. These major competitors only account for 45% of total revenues while McDonald has been captured 21.7% of the market. But from last 3 to 4 months, the company's market share has decreased by 0.06% as shown in table 1. Victory of McDonald's in the industry of fast food chain is being just because of the factors, including efficiency of cost, development of products, continuous improvement & value addition to the menu, accessibility, best promoting and marketing programs. These all features or factors are responsible in creating McDonald's brand images, deliver their clients superior quality food items and differentiating their services from other competitor companies & make them loyal ones. During the previous years, McDonald's has grown its revenues generated by its operations, earnings per share & equal sales generated by its all geographical areas, even though McDonald's is facing an economic recession globally & a very challenging environment in operating its activities (Samadi, 2013).

The purpose of this case study is to explore how McDonald's keeps stable in terms of both sales & profits despite of today's challenging and ever changing business environment. The study is divided into some major sections. In the first section, major industry trends, patterns of sales in the fast food industry & McDonald's position in that industry as compared to other major industry players is explored. In the second section, financial ratios of the company in comparison with industry and its major competitors are discussed to examine the company's financial position from borrowers, investors as well as financial manager's perspective and point out possible reasons for deviations. In the third section of this study, horizontal and vertical analysis is done. In the fourth section, DuPont System of financial analysis is applied to explore the factors affecting ROA and ROE of the company and recommend possible interpretations as well as suggestions for betterment and take advantage over its rivals. Last section comprises the critical analysis of a company's short term liquidity position. In the last part of study, conclusion about the company's overall position in its industry & outline reasons of its success as a market leader are given.

1. Industry Analysis

McDonald's Corporation lies in the fast food segment of the restaurant industry with a large network consisting of company owned as well as franchised outlets all over the world. The fast food industry is divided into three major segments. First is the limited service restaurant which is the largest one out of these three segments. The businesses included in this segment are pizza parlors, carry-out restaurants, fast food & sandwich shops which makes 78.7% of total industry revenues. Snack & nonalcoholic beverage bars, is the second largest segment which accounts for 13.1% revenues. This segment includes doughnut shops, coffee shops, ice cream parlors & bagel shops. The third segment is buffeted & cafeterias accounting for only 4% of the industry's revenues (Ari Siegel, 2010, pp. 3-6).

Overall restaurant industry's economic impact on the US economy, which is one of the major economies of the world & almost all other economies of the world are directly influenced by the trends in this economy, was estimated to be 1.8 trillion US Dollars in 2011. All the fast food restaurant's accounts for 632 Billion US Dollars in 2012’s gross retail revenues, which will contribute 4% of Gross Domestic Product (GDP) of the country (“Restaurant Industry Performance”, 2012, p. 2). Restaurant Performance Index (RPI) by National Restaurant Association, a measure of health & overall outlook of the US restaurant industry released at monthly basis is found to be 99.7 in December 2012 decreased by 0.2 % from the previous month (“Restaurant Performance Index”, 2012, p. 1). The revenue growth of McDonald’s has outperformed its industry average of 3.8% in the year 2012 whereas in previous years the increase was 2.0%. McDonald’s revenue growth has slightly outpaced the industry average of 3.8%. Since, the same quarter one year prior, revenues slightly increased by 2.0% (Samadi, 2013, pp. 22-23).

McDonald’s is the market leader in fast food portion of this industry and continuously remained at number one from many years with recently reported market share of 4.3% on the basis of domestically franchised & company-owned outlets and 12.7% on the basis of companywide revenue from domestically franchised & company-owned outlets. This is the revenue that only results from stores owned by the company & fees from franchises not sales revenue. Yum Brand is the second major player in this industry, which owns 2.5% & a 9.7 % share of a domestically franchised & company-owned outlets & overall revenue from company operated stores & fees from franchises excluding any revenue from sales respectively. Wendy’s Group with 1.4% & 6.6%, Starbucks to 4.0% & 5.9% and Burger King has 2.6% & 5.1% market share on the basis of domestically franchised & company-owned outlets and on the basis of companywide revenue from domestically franchised & company-owned outlets respectively and are the other prominent companies operated in this industry. The remaining share is captured by other small restaurants & fast food chains including Domino’s, Inc. with an estimated share of 1.9%, Jack in the Box with 1.5% etc. (Zwolak, 2013, p. 21-29).

The restaurant industry qualifies as one of the industries having intense competition. It has a varied growth patterns from region to region. The recession has a great impact on people’s buying & eating behaviors as now more and more people are spending less on ready to eat restaurant items and growingly becoming health conscious. Social & economic trends are emerging and affecting the functioning of fast food chains very sharply by putting new opportunities as well threats for them. Industry experts indicate that the restaurant industry is in the mature stage of its life cycle at this time and international expansion is the only way of making profits & revenues. Due to the increased global competition, fast food chains are compelled to sell their products & services at lower rates and this is the only reason that this industry remained greatly un-effected during the era of global recession as compared to the rest of the economy. This insensitivity to economic downturns relative to other industries is reflected by a low value of industry beta. However, McDonald’s sale shown a downturn of 3.31% in the year 2009 but gets improved as the economy boosts.

Porter’s five forces analysis for restaurant industry reveals the following facts: Suppliers of industry have less power over their choices and extremely low for McDonald’s because of its strong market power & franchising strategy. The supplies are purchased from all around the world. Entry barriers are also low so the firms are under extreme pressure from increasing competition & exposed to new entries. Buyers' power is comparatively low in the industry due to a large number of franchises operating globally having no control over global sales. The industry has high threats of substitutes as customers have a great variety of menus. Degree of rivalry is fairly high within the industry as the number of restaurants is increasing day by day (Seigel, 2010, p. 4).

In terms of the overall significance of the restaurant industry, almost 10% of the US workforce has employed in this industry & generated 1.5 million new jobs. From global perspective, fast food restaurant's accounts for more than 90% of total world's sale. At the start of 2012, industry shows a relatively positive trend. However, during the second quarter of the year, it appears to be slackened while reflecting macroeconomic concerns. From global economic perspective, the industry appears to be at the most receiving end, a stronger currency value, uncertainty around the election of new US government, a slightly higher cost of food supplies, a slow-moving labor market & an increased number of restaurants in the industry, all these factors along with the disposable income trends of the world population are characterized the present condition of restaurant industry ("Restaurant Industry Stock Outlook - Oct. 2012", 2012).

2. Financial Ratio Analysis of McDonald's

Now financial ratio analysis of McDonald's is discussed in comparison with industry averages and strong competitor. Through it, information about the performance, profitability and efficiency of the company is obtained as compared to industry and competitor. As concerned with the short term solvency of McDonald's, Current ratio of the company is good, then industry average as well as quick ratio is much higher than industry average as shown in table 2. The Current ratio of McDonald's shows a fluctuating positive increasing trend in last 9 years, but it was decreased in 2007 as shown in figure 1 of exhibit 1. Major reasons were heavy amount due in the form of notes payable. Similarly the quick ratio of McDonald's represents the same pattern of current ratio and higher than the Yum Brands as shown in table 3. Strong current ratio and quick ratio as compared to industry averages and strong competitor indicates that McDonald's short term liquidity position is very good. It is mainly due efficient inventory and short term debt management.

Table.2 McDonald's Financial Ratios Comparison to Industry and Competitor

Financial Ratios	McDonald's Corporation	Industry Average	Yum Brands
Current Ratio	1.45	1.37	0.87
Quick Ratio	1.09	1.01	0.73
Inventory Turnover	231.17	30.27	30.33

Debt to Equity	1.32	0.87	2.97
Net Profit Margin	19.82	14.20	11.71
Interest Coverage	16.66	14.18	15.39
Receivable Turnover	20.04	24.6	45.29
Average Collection Period	17.96	14.64	7.95
Total Asset Turnover	0.78	0.95	1.51
Return on Assets	15.5	13.49	18
Return on Equity	36	30.96	71

Note. Data for financial ratio comparison with industry from “McDonald’s Corporation”, (n. d.) & Annual Report of Yum’s Brand, (2012)

While talking about the type of capital structure either it is debt based or equity based we calculate the debt to equity ratio and debt to asset ratio. Debt to equity ratio of McDonald’s is higher than industry average and it is not a good indication of a highly reputed company. Debt to equity ratio of McDonald’s is increasing over the period of time as shown in table 3. While it is decreasing in case of strong competitors of McDonald’s, that is Yum Brand as shown in table 2. It represents McDonald’s is focused on debt financing while Yum Brand reducing the proportion of debt in its capital structure. But McDonald’s debt to equity ratio is comparatively less than Yum Brands. As well as debt to asset ratio of McDonald’s is increasing over time period, but much less than Yum Brands as shown in figure 2 of exhibit 1. It represents that McDonald’s focused on debt financing with the passage of time, but to a limited extent as compared to its strong competitor.

Table.3 Time Series Analysis of McDonald’s Financial Ratios

Year	Current Ratio	Quick Ratio	Debt to Equity Ratio	Debt to Asset Ratio	Interest Coverage Ratio	Average Collection Period	Receivables Turnover Ratio	Inventory Turnover Ratio	Tt. Assets Turnover Ratio	Net Profit Margin Ratio	Return on Assets Ratio	Return on Equity Ratio
2012	1.45	1.09	1.31	0.58	16.66	17.96	20.04	231.17	0.78	19.82	0.15	0.36
2011	1.25	1.05	1.29	0.56	17.31	17.79	20.23	238.25	0.82	20.38	0.17	0.38
2010	1.49	1.22	1.18	0.54	16.57	17.63	20.42	222.81	0.75	20.55	0.15	0.34
2009	1.14	0.96	1.15	0.54	14.46	16.78	21.45	208.95	0.75	20.01	0.15	0.32
2008	1.39	1.18	1.13	0.53	12.33	14.25	25.26	198.67	0.83	18.34	0.15	0.32
2007	0.80	0.67	0.12	0.48	9.46	16.65	21.62	191.73	0.78	10.51	0.08	0.02
2006	1.76	1.61	0.87	0.47	11.03	13.90	25.90	161.10	0.72	16.96	0.12	0.23
2005	1.45	1.25	0.98	0.49	11.18	14.99	24.02	129.83	0.64	13.61	0.09	0.17
2004	0.81	0.60	0.96	0.49	9.88	14.08	25.57	258.50	0.68	11.95	0.08	0.16

Note. Data for calculation of financial ratios from McDonald’s Corp. Annual Reports (2004-2012).

Interest coverage ratio of the McDonald’s company is higher than the industry averages and Yum brands and it is a good point in favor of it. Interest coverage ratio of McDonald’s is positively increased, but it reduced in 2012 as shown in table 3. Major reason is the increase in interest expenses due to the firm’s focus on debt financing. But it is comparatively higher than its competitor Yum Brands. It represents over the period of time firm’s ability to meet its due fixed contractual payment is strengthening.

Average collection period of McDonald’s is 17 days approximately which is higher than industry average of 15 days. Average collection period of McDonald’s is positively increasing and much higher than the Yum Brands as shown in table 2 & 3. It represents that management is not effectively managing the account receivable due to which collection period is extended. It is the point required attention. Inventory turnover is very higher than industry average. Reason for high inventory turnover is higher sales. Inventory turnover of McDonald’s is increasing yearly, but reduced in 2012 as shown in figure 3 of exhibit 1. And it is much greater than the Yum Brands. It represents that firm’s management is very effectively manage its inventory by reducing its handling least as well as also demonstrate that firm’s sales is increasing due to which inventory turnover is very high.

The total asset turnover ratio of McDonald’s is less than the industry average and required proper attention to manage assets effectively as shown in table 2. Total asset turnover of McDonald’s is improving over time period, but reduced in 2012as shown in figure 4 of exhibit 1. Major reason is the increase in assets is high due to debt financing, but sales is not increased by the same proportion, while Yum Brands total asset turnover comparatively very high and improving. It represents firm’s assets are not managed efficiently to generate high sales.

Net profit margin is very better than industry average as well as return on investment and equity also greater than the industry average as shown in table 2. Net profit margin of McDonald's is increasing over the period of time and higher than the Yum Brands. But it was reduced in 2012 due to increase in interest expenses due to which net income reduced as shown in table 3. But overall its profitability is good as shown in figure 5. Return on assets of McDonald's is improving with the passage of time, but comparatively low as compared to Yum Brands and it is reduced in 2012 due to the same reasons as mentioned in the above paragraph. Similarly, return on equity of McDonald's represents the same pattern as ROA. It is increasing, but weaker than Yum Brands. It represents that McDonald's assets and shareholder funds are not effectively utilized due to which it has low profitability as shown in figure 6 of exhibit 1. Board of directors has to focus on this issue keenly.

3. Horizontal Analysis of McDonald's

Over the passage of time McDonald's profitability is increasing with positive increasing trend, but it reduced in 2012 due to recession and tremendous increase in interest expenses as well as administrative and impairment expenses. Company's revenues are increasing with an appropriate percentage over the period of 5 years under study due to increase in sales by company operated as well as franchised restaurants. Net profit margin has increased by 20%, operating expenses increased by 3% & operating income has risen by 0.9%, which is lower as compared to increase in operating expenses which needs to be reduced. While net sales have an increasing trend over the period of the first four years from 2008 to 2011 but decreased by a small percentage of 0.7% in 2012. But the company is quite efficient in operations because its operating expenses are reduced over the time period. It is shown in figure 1of exhibit 2.

Let's talk about the short-term liquidity position of the company. Its short term liquidity position is strengthening because a positive increase in the current assets which is 12% is greater than the increase in current liabilities which are decreased by 3% in the most recent year. Also company's current assets are increasing with a greater percentage which is enough to cover its operating costs & other expenses thus leaving a sufficient amount to fulfil its short-term obligations as these come due. It means that company is capable to meet its short term obligations as incurred and shown in figure 2 of exhibit 2.

While analyzing the debt structure of the company, it is revealed through figure 3 that its debt structure heavily based on long term liabilities as compared to short term. Also percentage increase in long-term debt which is 10% is more as compared to total equity, which is increased by 7%. In capital structure proportionate of retained earnings and treasury stock is increasing with a greater percentage of 7% and 8% respectively. Also capital structure is more heavily based on debt as shown in figure 4 of exhibit 2. But company assets are not utilized efficiently because the increase in assets is not shown as the percentage increase in sales (look table 1 in Annexure and all calculations are done by researchers).

4. Vertical Analysis of Mcdonald's

According to the results of the vertical analysis, 67% of company's net revenue comes from the sale of its own restaurants while 33% from the sale of franchised restaurants. The company's operating income shows positive increasing trend up to 2011 due to decrease in operating expenses, but in 2012 it shows a slight decrease in decimals and it is 32% of total company's revenues. Net income is 20% of company's total revenues from 2008 to 2011 but decreased in 2012 due to increase in provision for income taxes. While interest expenses are continuously increasing which causes net income to increase with a low percentage in comparison with operating income. Total operating expenses are 68% of net revenue in 2012 with a positive increasing trend over the period of three years; it means profitability of the firm is much affected by operating expenses it has to reduce them. It is shown in figure 2of exhibit 2.

The short term liquidity position is strengthening because over the time period proportion of current assets to total assets is increased with a greater proportion than of current liabilities. Whereas current assets are 14% and current liabilities are approximately 9% of total assets. The proportion of long term debt is also increasing with a greater percentage as compared to current liabilities which represents that company is heavily depend on long term debt which is 39% of total assets. Capital structure composition is 57% debt and 43% equity it means capital structure is debt based. Moreover, assets are not utilized efficiently due to lower increase in profitability (look table 2 in Annexure and all calculations are done by researchers).

5. DuPont System of McDonald's Financial Analysis

The DuPont system of financial analysis of Macdonald's with industry averages more deep knowledge of its profitability and financial stability is obtained. Return on assets and equity are major financial ratios provide information about the company's profitability, operations and assets efficiency as well as financial leverage. Through DuPont analysis of return on assets (ROA) it is found that Mcdonald's ROA is higher than industry average. And a major component of this higher ratio is net profit margin shown in table 4. Net profit margin of McDonald's is much higher than industry average representing that company is operating efficiently and if wants to remain competitive then focus on the further reduction of operating expenses. While McDonald's is less effective in asset utilization as shown in table 4 in terms of asset turnover. Assets turnover of Mcdonald's is less than industry average. So, to be a market leader company has to improve its asset utilization. Because effective asset utilization leads towards operating cost reduction, increase in profitability as well as ROA.

Table.4 DuPont System Analysis of McDonald's 2012

	McDonald's Corporation	Industry Average
ROA= Net Profit Margin* Total Asset Turnover	**15.44=** **19.82*0.78**	**13.49=** **14.20*0.95**

ROE= Net Profit Margin* Total Asset Turnover* Equity Multiplier	**36=** **19.82*0.78*2.313**	**30.96=** **14.29*0.95*2.36**

Note. Data for DuPont system analysis from McDonald's Corp., (2012)

Let's talk about return on equity (ROE); it is higher than industry average. Net profit margin is the major component of higher ratio. But another positive fact is identified about Mcdonald's that it is less leverage than industry average. Because according to industry average, leverage is allowed up to 2.36 but Mcdonald's attained it to 2.313. This point advocates the Mcdonald's more focus on lease and debt financing in last 2 years. But if the company wants to be remain the market leader and don't want to lose its market share and investors trust, it has to limit its focus on lease and debt financing. Because an increase in lease and debt financing leads towards an increase in interest expenses and reduced profits. It ultimately affects long term profitability as well as the solvency position of the company.

6. Short Term Liquidity Management

Let talk about short term liquidity position of McDonald's, then it is found that its current ratio and quick ratio are much higher than industry average and favorable for the company as well as short term liquidity position is very good as compared to industry averages and strong competitor as shown in table 3. There is continuous improvement in liquidity position as an increase in total current assets, followed by a huge increase in the amount of account receivables and prepaid expenses. Whole increase in total current liabilities is hampered by a tremendous reduction in current maturities of long term debt in 2012 shown in table 5. So, high current and quick ratio depicts that company is strong enough to quickly meet its short term obligations. As well as amount of working capital is also increasing yearly shown that the company has sufficient amount to meet its daily operational needs. But here is a question that why company is stagnating huge amount of its investment approximately 14% in current assets, mainly in terms of account receivables and prepaid expenses. Huge amount of account receivables shows that company sale is increasing, but why company is making huge advance payments of its expenses, because this amount has not been utilized to generate profit. So, it is good to improve short term liquidity position, but up to the extent of industry average. In other words, the company has to focus on improving the worth of its investors and shareholders.

Table.5 Short Term Liquidity Management of McDonald's

Items (in million $)& Years	2012	2011	2010	2009	2008
Cash & equivalents	2336.1	2335.7	2387	1796	2063.4

Account receivables	1375.3	1334.7	1179.1	1060.4	931.2
Inventories at cost	121.7	116.8	109.9	106.2	111.5
Prepaid & other Exp.	1089	615.8	692.5	453.7	411.5
Tt. Current Assets	4922.1	4403	4368.5	3416.3	3517.6
Account Payable	1141.9	961.3	943.9	636	620.4
Income taxes	298.7	262.2	111.3	202.4	0
Other taxes	370.7	338.1	275.6	277.4	252.7
Accrued interest	217	218.2	200.7	195.8	173.8
Accrued payroll	1374.8	1362.8	1384.9	1659	1459.2
Current maturities of long term debt		366.6	8.3	18.1	31.8
Tt. Current Liabilities	3403.1	3509.2	2924.7	2988.7	2537.9
Current Ratio 1.44 1.25 1.49 1.14 1.38					
Quick Ratio 1.09 1.05 1.22 0.96 1.18					
Net Working Capital 1519 813 1443 427 979					

Note. Data for Short Term Liquidity Management from McDonald’s Corp.,(2008-2012).

Conclusion

After applying all analysis on the financial data of McDonald’s, it is revealed that short term solvency position of McDonald’s is very strong as compared to industry average and Yum Brands. McDonald’s is self-sufficient in the payment of its current obligations as claimed as well as has sufficient working capital to meet its day to day operations expenses. Let’s talk about profitability of company; it is found that McDonald’s profitability is improving positively as compared to strong competitor. Due to increased profitability, faith of shareholders ad investors also increased. McDonald’s is also very efficient in operations and continuously trying to reduce its operating costs. Efficient operations are a big reason of high profitability of McDonald's.

Moreover company debt to assets and equity ratio is good as compared to industry average but require more improvement to remain number one in competitive industry. As talk about the assets utilization efficiency, it is found that company assets are not utilized efficiently to get potential results. Another good thing revealed about McDonald's is that company is less leveraged than industry and focusing on more debt by leasing. And capital structure composition is shifting from equity based to debt base. It is the point of trouble for the company. Because due to heavy reliance on debt financing risk increases that discourage shareholders and investors. But all in all high profit margins, continuous dividend payment, strong solvency position broad network expansion and continuous value addition to the menu are major component of McDonald's leadership in fast food industry.

Recommendation

1. Firstly, company has to improve its efficiency of assets utilization. Became due to less efficient asset utilization, operating costs increased and profitability affected. So, management has to focus on effective management of assets.

2. McDonald's has to become more conscious about the composition of its capital structure. Heavy reliance on debt in capital structure makes the company more risky and loses investor's trust.

3. Company also has to improve its average collection period because credit policies are comparatively lenient as compared to industry due to which risk of delay in recovery of debt increased.

Limitations and Future Research

Limitations of this study are that all results and recommendations are based on only the information provided by annual reports and available on company websites. But researchers don't get access to any information about the managerial policies and actions. And if further research on data related to management policies and actions is explored than effectiveness of this study can be enhanced.

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Annexure

*Table 1.*Horizantal Analysis of McDonald's Corporation from 2008-2012

Horizontal Analysis of Income Statment										
Items & Years	2012		2011		2010		2009		2008	
	Amount	% age	Amount	% age	Amount	% age	Amount	% age	Amount	% age
Sales by Company-operated restaurants	309.70	1.69	2059.50	12.69	774.80	5.01	-1102.40	-6.66	-1102.40	-6.64
Revenues from franchised restaurants	251.30	2.88	871.90	11.12	555.10	7.62	324.70	4.66	324.70	5.26
Total Revenues	**561.00**	**2.08**	**2931.40**	**12.18**	**1329.90**	**5.85**	**-777.70**	**-3.31**	**-777.70**	**-3.41**
Food & paper	151.00	2.45	867.10	16.36	122.10	2.36	-408.10	-7.31	-408.10	-7.44
Payroll & employee benefits	104.00	2.26	484.90	11.77	155.80	3.93	-334.50	-7.78	-334.50	-7.72
Occupancy & other operating expenses	130.80	3.22	426.40	11.72	130.40	3.72	-259.10	-6.88	-259.10	-6.61
Franchised restaurants, occupancy expenses	45.50	3.07	103.70	7.53	76.10	5.85	71.40	5.80	71.40	6.26
Selling, general & administrative expenses	61.50	2.57	60.40	2.59	99.10	4.44	-121.30	-5.15	-121.30	-5.12
Impairment & other charges	11.90	-305.13	-33.00	-113.40	90.20	-147.63	-67.10	-1118.33	-67.10	-4.02
Other operating income (expense), net	-18.60	7.99	-34.70	17.51	24.10	-10.84	-57.10	34.56	-57.10	514.41
Total operating costs & expences	**486.10**	**2.63**	**1874.80**	**11.29**	**697.80**	**4.39**	**-1175.80**	**-6.88**	**-1175.80**	**-6.22**
Operating income	**74.90**	**0.88**	**1056.60**	**14.14**	**632.10**	**9.24**	**398.10**	**6.18**	**398.10**	**10.26**
Interest expense, net of capitalized interest	23.80	4.83	41.90	9.29	-22.30	-4.71	-49.40	-9.45	-49.40	-12.05
Nonoperating income (expense), net	-15.70	-63.56	2.80	12.79	46.20	-190.12	53.30	-68.69	53.30	-51.65
Income before provision for income taxes	**66.80**	**0.83**	**1011.90**	**14.46**	**513.30**	**7.91**	**329.00**	**5.34**	**329.00**	**9.21**
Provision for income taxes	105.10	4.19	455.10	22.16	118.00	6.10	91.20	4.94	91.20	7.37
Net income	**-38.30**	**-0.70**	**556.80**	**11.26**	**395.30**	**8.69**	**237.80**	**5.51**	**237.80**	**9.93**

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Horizontal Analysis of Balance Sheet										
Items (in million $) Years	2012		2011		2010		2009		2008	
	amount	%age	amount	%age	amount	%age	amount	%age	amount	%age
Cash & equvilants	0.40	0.02	-51.30	-2.15	591.00	32.91	-267.40	-12.96	82.10	4.14
Account receivables	40.60	3.04	155.60	13.20	118.70	11.19	129.20	13.87	-122.60	-11.63
Inventories at cost	4.90	4.20	6.90	6.28	3.70	3.48	-5.30	-4.75	-13.80	-11.01
Prepaid & other Exp	473.20	76.84	-76.70	-11.08	238.80	52.63	42.20	10.26	-10.00	-2.37
Tt. Current assets	**519.10**	**11.79**	**34.50**	**0.79**	**952.20**	**27.87**	**-101.30**	**-2.88**	**-64.30**	**-1.80**
Investments and advances to	-46.50	-3.26	91.70	6.87	122.60	10.11	-9.60	-0.79	65.90	5.70
Goodwill	150.80	5.68	67.10	2.59	160.90	6.63	187.80	8.39	-63.90	-2.78
Miscelleneous	-69.50	-4.16	47.50	2.92	-14.50	-0.88	409.50	33.30	-137.70	-10.07
Tt.other assets	34.80	0.60	206.30	3.72	269.00	5.10	587.70	12.53	-135.70	-2.81
Property & equipments at cost	2753.50	7.70	1255.20	3.64	1041.90	3.12	2288.10	7.34	-1051.30	-3.26
Acc. Depreciation & amortization	-910.80	7.06	-481.30	3.87	-512.80	4.31	-1011.10	9.28	321.10	-2.86
Net Property & equipment	1792.70	7.85	773.90	3.51	529.10	2.46	1277.00	6.30	-730.20	-3.48
Tt. Assets	**2396.60**	**7.26**	**1014.70**	**3.17**	**1750.30**	**5.79**	**1763.60**	**6.20**	**-930.40**	**-3.17**
Account Payable	180.60	18.79	17.40	1.84	307.90	48.41	15.60	2.51	-3.70	-0.59
Income taxes	36.50	13.92	150.90	135.58	-91.10	-45.01	0.00	0.00	0.00	0.00
Other taxes	32.60	9.64	62.50	22.68	-1.80	-0.65	24.70	9.77	4.70	1.90
Accrued interest	-1.20	-0.55	17.50	8.72	4.90	2.50	22.00	12.66	25.40	17.12
Accrued payroll	12.00	0.88	-22.10	-1.60	-274.10	-16.52	199.80	13.69	-27.70	-1.86
Current maturities of long term debt	-366.60	-100.00	358.30	4316.87	-9.80	-54.14	-13.70	-43.08	-832.70	-96.32
Tt. Current liabilities	**-106.10**	**-3.02**	**584.50**	**19.98**	**-64.00**	**-2.14**	**450.80**	**17.76**	**-1960.60**	**-43.58**
Long tem debt	1498.70	12.35	636.80	5.54	936.70	8.87	374.30	3.67	2876.00	39.34
Other long term liabilities	-86.40	-5.36	25.70	1.62	223.80	16.42	-47.00	-3.33	67.60	5.04
Deffered income taxes	187.00	13.91	11.70	0.88	53.50	4.18	334.00	35.35	-16.00	-1.67
Additional paid in capital	291.60	5.31	290.90	5.60	342.50	7.06	253.70	5.51	373.50	8.84
Retained earning	2570.50	7.00	2895.80	8.56	2540.90	8.13	2316.90	8.00	2492.40	9.42
Acc. Other comprehensive income	336.70	74.87	-303.20	-40.27	5.50	0.74	646.10	637.81	-1236.10	-92.43
Treasury stock	-2305.40	8.15	-3127.50	12.44	-2288.60	10.01	-2565.40	12.64	-3527.00	21.04
Tt. Shareholders equity	**903.40**	**6.28**	**-244.00**	**-1.67**	**600.30**	**4.28**	**651.30**	**4.87**	**-101897.00**	**-88.39**
Tt. Liabilities & shareholders equity	**2396.60**	**7.26**	**1014.70**	**3.17**	**1750.30**	**5.79**	**1763.40**	**6.20**	**-930.00**	**-3.16**

Table 2. Vertical Analysis of McDonald's Corporation from 2008-2012

Vertical Analysis of Income Statement					
Items & Years	**2012**	**2011**	**2010**	**2009**	**2008**
Sales by Company-operated restaurants	67.48	67.74	67.43	67.97	70.40
Revenues from franchised restaurants	141.88	32.26	32.57	32.03	29.60
Total Revenues	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**
Food & paper	22.92	22.84	22.02	22.77	23.75
Payroll & employee benefits	17.09	17.06	17.12	17.44	18.28
Occupancy & other operating expenses	15.22	15.05	15.11	15.42	16.01
Franchised restaurants, occupancy expenses	5.54	5.49	5.72	5.72	5.23
Selling, general & administrative expenses	8.91	8.86	9.69	9.82	10.01
Impairment & other charges	0.03	-0.01	0.12	-0.27	0.03
Other operating income (expense), net	-0.91	-0.86	-0.82	-0.98	-0.70
Total operating costs & expences	**68.79**	**68.42**	**68.96**	**69.92**	**72.61**
Operating income	**31.21**	**31.58**	**31.04**	**30.08**	**27.39**
Interest expense, net of capitalized interest	1.87	1.82	1.87	2.08	2.22
Nonoperating income (expense), net	0.03	0.09	0.09	-0.11	-0.33
Income before provision for income taxes	**29.31**	**29.67**	**29.08**	**28.52**	**26.18**
Provision for income taxes	9.48	9.29	8.53	8.51	7.84
Net income	**19.82**	**20.38**	**20.55**	**20.01**	**18.34**

Vertical Analysis of Balance Sheet					
Items (in million $) Years	**2012**	**2011**	**2010**	**2009**	**2008**
Cash & equvilants	3.89	4.05	3.69	3.51	3.27
Account receivables	3.89	4.05	3.69	3.51	3.27
Inventories at cost	0.34	0.35	0.34	0.35	0.39
Prepaid & other Exp	3.08	1.87	2.17	1.50	1.45
Tt. Current assets	**13.91**	**13.35**	**13.66**	**11.30**	**12.36**
Investments and advances to	3.90	4.33	4.18	4.01	4.29
Goodwill	7.92	8.04	8.09	8.02	7.86
Miscelleneous	4.53	5.07	5.08	5.42	4.32
Tt.other assets	16.35	17.44	17.35	17.46	16.48
Property & equipments at cost	108.77	108.33	107.84	110.64	109.46
Acc. Depreciation & amortization	-39.04	-39.11	-38.85	-39.40	-38.29
Net Property & equipment	69.59	69.22	68.99	71.24	71.17
Tt. Assets	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**
Account Payable	3.23	2.91	2.95	2.10	2.18
Income taxes	0.84	0.79	0.35	0.67	0.00
Other taxes	1.05	1.02	0.86	0.92	0.89
Accrued interest	0.61	0.66	0.63	0.65	0.61
Accrued payroll	3.89	4.13	4.33	5.49	5.13
Current maturities of long term debt	0.00	1.11	0.03	0.06	0.11
Tt. Current liabilities	**9.62**	**10.64**	**9.15**	**9.89**	**8.92**
Long tern debt	38.52	36.78	35.96	34.94	35.79
Other long term liabilities	4.31	4.89	4.96	4.51	4.95
Deffered income taxes	4.33	4.07	4.17	4.23	3.32
Common stock	0.05	0.05	0.05	0.05	0.06
Additional paid in capital	16.33	16.63	16.25	16.06	16.16
Retained earning	11.00	11.00	10.50	10.30	10.10
Acc. Other comprehensive income	2.22	1.36	2.35	2.47	0.36
Treasury stock	-86.41	-85.70	-78.63	-75.62	-71.29
Tt. Shareholders equity	**43.22**	**43.62**	**45.77**	**46.43**	**47.02**
[t. Liabilities & shareholders equit	**100.00**	**100.00**	**100.00**	**100.00**	**100.00**

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