



Católica Porto Investment Club

EQUITY RESEARCH

MCDONALD'S CORPORATION

12 de abril de 2023



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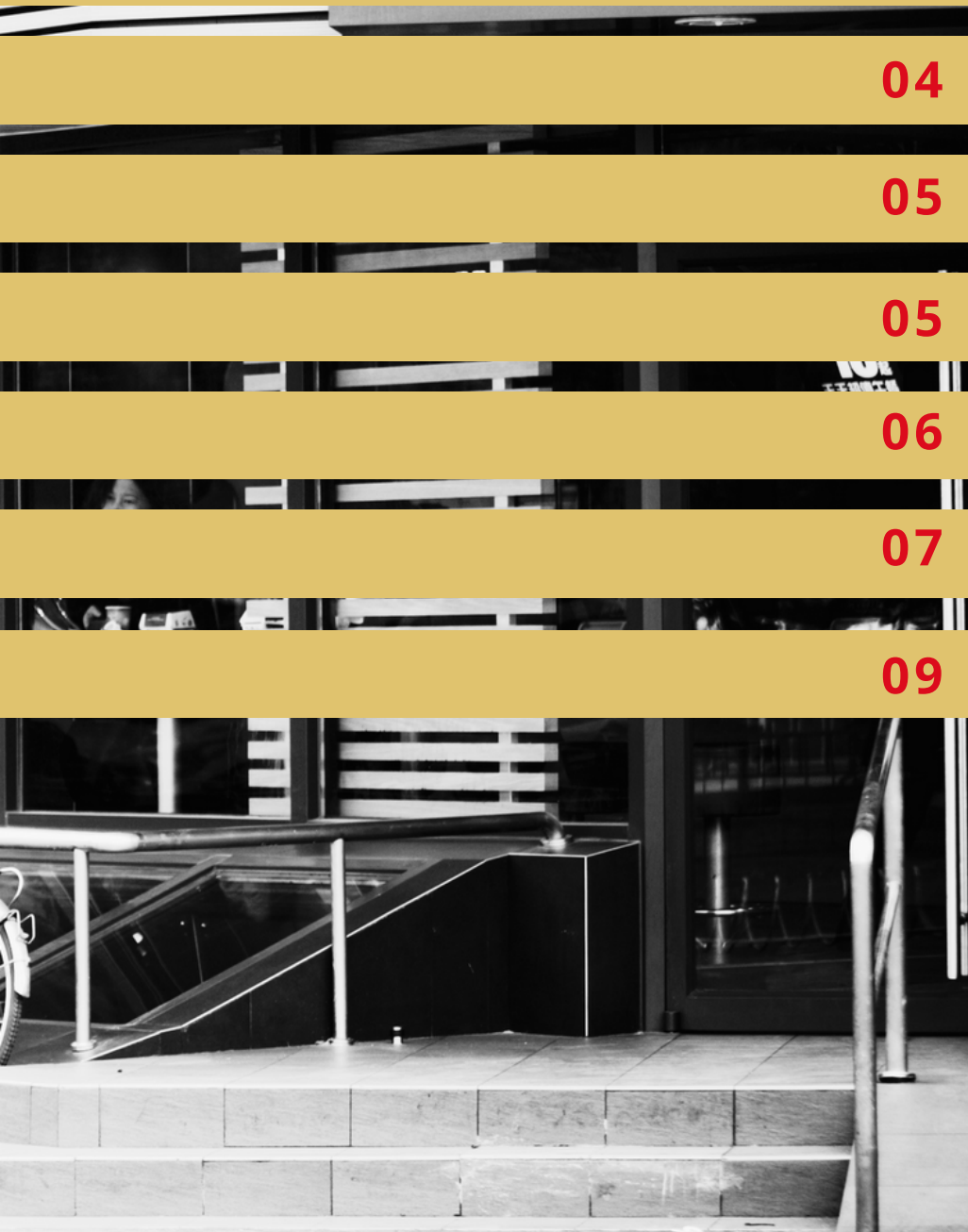
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INTRODUCTION

This report aims to perform a valuation of McDonald's Corporation using two valuation models, Relative Valuation and Discounted Cash Flow model.

Firstly, we do a brief presentation of the company, presenting its shareholders, management team and some key ratios of McDonald's Corporation comparing to its industry. Secondly, we present our valuation using Relative Valuation and then Discounted Cash Flow Model.

Finally, it is important to mention that all data used is from the first of March 2023 and this report should not be used as an investment recommendation.



COMPANY DESCRIPTION

McDonald's Corporation is a multinational fast-food restaurant chain that was founded in 1940 by Richard and Maurice McDonald in San Bernardino, California, USA. It is now headquartered in Chicago, Illinois, USA.



The company operates over 39,000 restaurants worldwide, serving approximately 69 million customers daily in over 100 countries. McDonald's primarily sells burgers, chicken products, fries, breakfast items, soft drinks, and desserts. The company also offers a variety of options for its customers, including vegetarian and vegan items,

salads, and coffee beverages. In addition to its restaurant operations, McDonald's has expanded into other areas such as real estate, franchising, and marketing. Most of its restaurants are owned by independent franchisees, with the company collecting rent and royalties from them.



MAIN SHAREHOLDERS

| Ownership | Name | # Shares | Current Value* | Change % (1) | Portfolio % (2) |
|-----------|--|------------|----------------|--------------|-----------------|
| 9,32% | The Vanguard Group, Inc. | 68 178 100 | 18 | 0,90% | 0,38% |
| 7,05% | BlackRock, Inc. | 51 569 204 | 13,6 | 3,34% | 0,3% |
| 4,65% | State Street Global Advisors, Inc. | 34 034 123 | 9 | -1,93% | 0,47% |
| 2,20% | Wellington Management Group LLP | 16 087 317 | 4,2 | -7,13% | 0,73% |
| 1,87% | Geode Capital Management, LLC | 13 702 475 | 3,6 | 1,33% | 0,42% |
| 1,43% | J.P. Morgan Asset Management, Inc. | 10 424 810 | 2,8 | -24,56% | 0,46% |
| 1,28% | Northern Trust Global Investments | 9 331 730 | 2,5 | 0,45% | 0,46% |
| 1,22% | Morgan Stanley, Investment Banking and Brokerage Investments | 8 948 263 | 2,4 | 4,91% | 0,43% |
| 1,21% | Norges Bank Investment Management | 8 884 607 | 2,3 | 15,60% | 0,26% |
| 1,18% | T. Rowe Price Group, Inc. | 8 651 215 | 2,3 | 9,94% | 0,25% |
| 1,18% | UBS Asset Management | 8 643 172 | 2,3 | 10,85% | 0,39% |
| 1,03% | BW Mellon Asset Management | 7 510 245 | 2 | 1,62% | 0,42% |
| 1,01% | Capital Research and Management Company | 7 363 399 | 1,9 | -20,12% | 0,12% |
| 0,95% | Wells Fargo & Company, Securities and | 6 982 629 | 1,8 | -1,00% | 0,75% |

Source: <https://simplywall.st>

(1) The amount of shares bought or sold by the shareholder between the last two reporting dates.

(2) What percentage this stock makes up of the shareholders total stock portfolio.



MANAGEMENT TEAM

| | Position | Tenure (years) | # Shares Owned |
|-------------------------|--|----------------|----------------|
| Christopher Kempczinski | President | 3.08 | 2 580 |
| Ian Borden | Executive VP & CFO | 0.25 | 7 131 |
| Desiree Ralls-Morrison | Executive VP | 1.67 | 0 |
| Kevin Ozan | Senior Executive Vice President of Strategic Initiatives | 0.25 | 21 581 |
| Joseph Erlinger | President of McDonald's USA | 7.75 | 8 187 |
| Brian Rice | Executive VP & Global Chief Information Officer | 0.33 | 0 |
| Mike Flores | Senior VP & Investor Relations Officer | NA | 0 |
| Amy Kovalan | VP & Chief Compliance Officer | 1.92 | 0 |
| Michael Gonda | Senior VP & Chief Communications Officer | 1.92 | 0 |
| Morgan Flatley | Global Chief Marketing Officer | 1.92 | 0 |
| Heidi Capozzi | Corporate Executive VP & Global Chief People Officer | 2.67 | 0 |
| Jill McDonald | Executive VP & President at International Operated Markets | 0.25 | 0 |

Source: <https://simplywall.st>

KEY RATIOS

| KEY RATIOS* | | |
|-------------------|------------|------------------|
| | McDonald's | Industry Average |
| Gross Margin | 56,97% | 47,43% |
| Operating Margin | 40,97% | -0,02% |
| Net profit margin | 26,65% | 11,28% |
| EPS | 8,33% | 6,18% |
| Return on Equity | - | 33,88% |
| Return on Assets | 11,85% | 6,83% |
| Quick Ratio | 1,24 | 0,99 |
| Current Ratio | 1,43 | 1,23 |
| Asset Turnover | 0,44 | 0,62 |
| Dividend Yield | 2,31% | 1,01% |
| Payout Ratio | 67,47% | 30,19% |

*1st March 2023



RELATIVE VALUATION

| Multiple | MCD | CMG | DPZ | YUM | QSR | WEN | Average |
|--------------------------|--------|-------|-------|-------|-------|-------|--------------|
| P/E Non-GAAP (TTM) | 26,13 | 45,46 | 23,45 | 28,26 | 20,54 | 27,11 | 28,49 |
| EV/EBITDA (TTM) | 19,59 | 29,98 | 18,84 | 21,95 | 15,77 | 17,98 | 20,69 |
| EV/SALES ratio (TTM) | 10,32 | 5,1 | 3,44 | 7 | 5,36 | 5,05 | 6,05 |
| Dividend yield (TTM) | 2,20% | - | 1,50% | 1,82% | 3,35% | 2,85% | 2,34% |
| Price/ Sales (TTM) | 8,38 | 4,81 | 2,31 | 5,32 | 3,04 | 2,89 | 4,46 |
| Market Cap (Billions \$) | 193,05 | 41,19 | 10,41 | 35,62 | 29,08 | 4,68 | 52,34 |

| | |
|-----|--------------------------------------|
| MCD | McDonald's Corporation |
| CMG | Chipotle Mexican Grill, Inc. |
| DPZ | Domino's Pizza |
| YUM | Yum! Brands, Inc. |
| QSR | Restaurant Brands International Inc. |
| WEN | Wendy's |



RELATIVE VALUATION (CONT.)



| Item | PER | EV/EBITDA | DIV.YIELD |
|---|----------------|----------------|----------------|
| Average of benchmark assets | 28,5 | 20,7 | 2,34% |
| Values for McDonald's TTM | | | |
| Net income | 5912,8 | | |
| EBITDA | | 12 056 | |
| Equity (Book value) | | | |
| Revenues | | | |
| Dividends | | | 3 919 |
| Value of operations | 212 736 | 249 378 | 211 463 |
| Value of non-operating assets and liabilities | 3 110 | 3 110 | 3 110 |
| Enterprise value | 215 845 | 252 488 | 214 573 |
| Debt value | 47 380 | 47 380 | 47 380 |
| Equity value | 168 466 | 205 108 | 167 193 |
| Number of shares (millions) | 732 | 732 | 732 |
| Share Price | 264 | 264 | 264 |
| Market capitalization (€ in millions) | 193 288 | 193 288 | 193 288 |
| Deviation vis-a-vis multiple model (€ in millions) | 24 822 | -11 820 | 26 095 |
| Equity value per share | 230,0 | 280,0 | 228,3 |
| Current value per share (March 1st, 2023) | 263,9 | | |
| Upside/downside | -12,8% | 6,1% | -13,5% |

March 1st, 2023



DCF VALUATION

COST OF CAPITAL (WACC)

In order to determine the cost of capital of McDonald's, it is necessary to estimate the value of the expected return that the company should generate to compensate the investors for the risk that is being taken by investing in the company.

First, it is necessary to obtain the company's capital structure, which refers to how the company finances its operation, including the debt and equity in its capital structure.

The next step is to determine the cost of debt and equity. To obtain the cost of equity, it's used the CAPM formula, and for this, the risk-free rate is at 10-year US treasury yields.

$$R_i = R_f + \beta_i * (R_m - R_f)$$

Lastly, calculate the weighted average cost of capital (WACC), which represents the minimum return the company must generate on its investments to meet its obligations to the investors, which for McDonald's is 6,6%.

| WACC | |
|---------------------|--------------|
| Debt | 35 904 |
| % Debt | 15,0% |
| Cost of Debt | 3,4% |
| Tax Rate | 25,0% |
| Equity Value | 198 406 |
| % Equity | 85% |
| Cost of Equity | 6,8% |
| Risk Free Rate | 3,5% |
| Beta | 0,64 |
| Market Risk Premium | 5,1% |
| Debt + Equity | 234 310 |
| WACC | 6,13% |



DCF VALUATION (CONT.)

DCF

The next step in the valuation process is to compute the enterprise value using one of the DCF models, the Free Cash Flow model.

The free cash model consists of the principle that the company's worth is equal to the present value of its future cash flows, discounted by an appropriate rate of return. This model also takes into consideration the company's cash inflows and outflows.



DCF VALUATION (CONT.)

MCDonalds's DCF

| | | | | | |
|--------|------------|---------------------|----------|-------------------|--------|
| Ticker | MCD | Implied Share Price | \$255,87 | | |
| Date | 01/02/2023 | Today's Share Price | \$267,00 | Upside (Downside) | (4,2%) |

Assumptions

Valuation Assumptions

| | |
|------|------|
| WACC | 6,1% |
| TGR | 2,0% |

| | | | | | | | 1 | 2 | 3 | 4 | 5 |
|---------------------------------|--------|--------|--------|--------|--------|--------|--------------|--------------|--------------|--------------|----------------|
| DCF | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 | 2027 |
| Revenue | 22 820 | 21 025 | 21 364 | 19 208 | 23 223 | 23 183 | 23 647 | 24 120 | 24 602 | 25 094 | 25 596 |
| % growth | | -7,9% | 1,6% | -10,1% | 20,9% | -0,2% | 2,0% | 2,0% | 2,0% | 2,0% | 2,0% |
| EBIT | 8 390 | 8 586 | 8 878 | 7 162 | 9 773 | 9 371 | 9 459 | 9 648 | 9 841 | 10 038 | 10 238 |
| % margin | 36,8% | 40,8% | 41,6% | 37,3% | 42,1% | 40,4% | 40,0% | 40,0% | 40,0% | 40,0% | 40,0% |
| Effective Tax Rate | 39,44% | 24,20% | 24,85% | 22,96% | 17,34% | 21,10% | 25,00% | 25,00% | 25,00% | 25,00% | 25,00% |
| EBIAT | | | | | | | 7 094 | 7 236 | 7 381 | 7 528 | 7 679 |
| D&A | 1 363 | 1 482 | 1 618 | 1 751 | 1 868 | 1 889 | 1 892 | 1 930 | 1 968 | 2 008 | 2 048 |
| % of sales | 6,0% | 7,0% | 7,6% | 9,1% | 8,0% | 8,1% | 8,0% | 8,0% | 8,0% | 8,0% | 8,0% |
| CapEx | 1 854 | 2 742 | 2 394 | 1 641 | 2 040 | 1 899 | 2 010 | 2 050 | 2 091 | 2 133 | 2 176 |
| % of sales | 8,1% | 13,0% | 11,2% | 8,5% | 8,8% | 8,2% | 8,5% | 8,5% | 8,5% | 8,5% | 8,5% |
| Change in NWC | -981 | -473 | 299 | -212 | 454 | -645 | -284 | -289 | -295 | -301 | -307 |
| % of sales | (4,3%) | (2,2%) | 1,4% | (1,1%) | 2,0% | (2,8%) | (1,2%) | (1,2%) | (1,2%) | (1,2%) | (1,2%) |
| Unlevered FCF | | | | | | | 7 260 | 7 405 | 7 553 | 7 704 | 7 858 |
| Present Value of FCF | | | | | | | 6 840 | 6 574 | 6 318 | 6 071 | 5 835 |
| Terminal Value | | | | | | | | | | | 193884,1 |
| Present Value of Terminal Value | | | | | | | | | | | 143969,4 |
| Enterprise Value | | | | | | | | | | | 175 607 |
| + Cash | | | | | | | | | | | 47 595 |
| - Debt | | | | | | | | | | | 35 904 |
| Equity Value | | | | | | | | | | | 187 298 |
| Shares | | | | | | | | | | | 732 |
| Share Price | | | | | | | | | | | 255,87 |



CONCLUSION

In conclusion, there is no doubt that McDonald's is one of the best businesses in the fast food industry, and has seen immense success since its founding in 1940. McDonald's brand is known everywhere and their customers can expect similar meals wherever there are around the globe.

Regarding the company's financials we concluded that McDonald's tends to perform better than its competitors in a series of key aspects like cost efficiency, return on assets, the overall liquidity and the returns it provides to the shareholders. By running a relative valuation we also saw that the company is slightly overvalued (12% to 14%) when considering the PE ratio and dividend yield multiples. On the other hand, the EV/ EBITDA multiple suggests that the company has a slight upside.

Finally, considering the DCF model valuation, according with the underlying assumptions we took to value the company, we believe that there can be a downside by investing in the company, given that the equity value we calculated is lower than the value at what the stock is trading in the present moment.

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