McDonalds Just Quietly Raised Their Prices Without You Knowing

Description

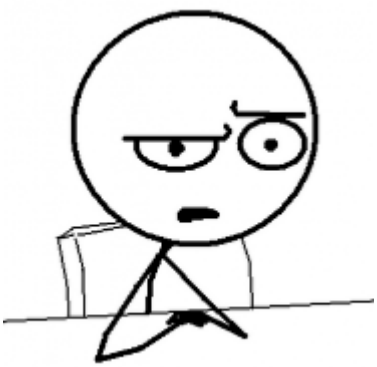


My weekends usually start at 9am for giving General Paper tuition, and a staple breakfast for me on every Saturday morning this year has been my all-time favourite McDonalds Sausage McMuffin meal.

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In the past 3 weeks, many of my students took a break due to their preliminary exams, so quite a few tuition sessions got postponed. As such, it was only today morning when I strode to McDonalds once more to order my usual breakfastâ?¦

Then I realized, **McDonalds just raised their prices AGAIN!**



My set meal just went from $4 to $4.20 after the short break. Many of their breakfast set meals have increased by 10 â?? 20 cents each. (I donâ??t know about the afternoon one since Iâ??ve not been a loyal customer of their regular menu.)

I asked some of my friends if they knew about the price changes, but those who have eaten at the fast food restaurant in the last week barely noticed anything.

While a few cents may not seem like much, consider this over 52 weeks, thatâ??s $10.40 more every year for just 1 regular consumer (or slightly more than 2 meals). Presuming 1 in 10 Singaporeans eat McDonalds every day (thatâ??s less than their local market share), thatâ??s close to 39 million extra in revenue for the company each year in Singapore alone!

I think Iâ??ll switch to Burger King instead for now. A taco pie and fish burger only sets me back by $2.95, and it fills me up pretty well enough for me to function in my tuition sessions.



But hereâ??s a closer look at the McDonalds business (and stock).



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Bad news for McDonalds in the past 5 years

Once the worldâ??s biggest fast-food darling, business at McDonalds has been slumping over the last 5 years. Faced with higher commodity costs, fiercer competition and minimum wage in certain countries, their earnings took a huge dip. To counter inflated beef prices and higher minimum wages (especially in California), the brand has been increasing its prices (by about 2% each year) as a result.

McDonalds net income also fell by 15% last year, and growth has been slow.



It was also troubled by various PR disasters last year, including accusations against one of their suppliers in China for selling expired meat. CEO Don Thompson retired earlier this March, after being blamed for almost all of the brandâ??s problems during his three-year leadership â?? confusing the

menu, lack of customization, not riding the healthy food trend, adding products that made waiting times longer, declines in same-store salesâ?¦and of course, the overall decline in McDonaldâ??s growth and profits.

All eyes are on its new CEO, Steve Easterbrook, to see if he can reverse the brandâ??s performance.

A great business story

Market cap: McDonald is still one of the worldâ??s largest fast-food chains, with over 35,000 locations and currently still the largely publicly traded restaurant in the world.



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Dividends: The company has a solid track record for delivering increasing dividends every year since 1976 (39 years).

Strong branding: The brandâ??s golden arches are recognizable throughout the world. Its slogan â??Iâ??m loving itâ?• was marketed so well that those words bring about a familiar jingle to everyone when they see it.

Strong business model: Its competitive advantage lies in McDonaldâ??s franchising model, which allows it to grow quickly and get higher returns on their assets compared to a store-owned one. With its strong branding and wide appeal to customers, many are also keen to franchise the business and ride on its success.

Recession-proof: Is the business recession proof? Although you might expect Singaporeans to start eating at home or at hawker centres more in the next few years with the expected economic slowdown, but this is not the case for many of the other countries McDonalds operates in. In the U.S. and Europe, Mcdonaldâ??s food can be much cheaper than cooking at home, depending on what you buy in your weekly groceries list. Its famous dollar menu (which we barely have here in Singapore) remains popular among the low-income and budget-conscious folks. Furthermore, during recessions, more people are likely to switch away from expensive restaurants to alternative choices like McDonalds instead.

Management: Many say that Don Thompson deserves blame for the companyâ??s weak performance during his term at the top. With a new CEO, it remains to be seen whether the new guy is up to the job.

Diversified business: Many think that McDonalds is just a food industry player, but few know about McDonaldâ??s ownership of real estate assets â?? $39 billion as of last year (or almost 40% of its market capitalization). These collect rents and fees from franchises, adding further to McDonaldâ??s

revenue. Its lease is only slightly over 1 billion, but yet it collected over 6 billion in rental fees!

Future outlook



Potential for growth: McDonalds can grow internal store-sales by reducing clutter in its menu, increase efficiency in wait times, and respond faster in order to adapt to the changing tastes of consumers. These changes have also been announced recently by its newest CEO, so there is hope that the brand might be able to grow further. Earlier today, it also revealed plans to serve a 100% organic burger in Germany as an attempt to revamp the brandâ??s image into a â??modern, progressive burger companyâ?•.

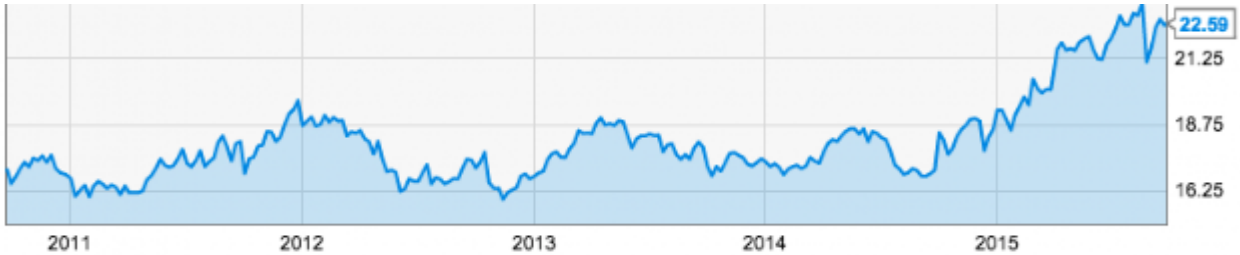
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Economic recession: May not have much of a negative impact on the brand compared to other food players.

Advertising: The company has been undergoing changes in its advertising strategies, which you may have noticed from the recent ads of customized McDonald burgers in Singapore.

Financial Ratios

P/E: At todayâ??s prices, McDonalds is trading at a P/E ratio of about 22, whereas its biggest competitor Yum! Brands trade at over 28 times valuations. Chipotle is trading at 44. While it is significantly lower than its peers, one must note that todayâ??s valuations are still at a 5-year high. Its lowest PE ratio during this timeframe was almost 14, and it was lower even in 2014 when the brand was plagued with various scandals.



ROE: The company also has a pretty attractive return on equity of 32.4%.

P/B: Its current price-to-book ratio is at 7.2 times, compared to the industry average of 8.1.

D/E: With a high debt of over USD 175,000,000,000 (yes, you read that right), McDonalds has a relatively high gearing of 1.7 to finance its business and assets.

Conclusion:

While there seems to be reason to believe that the new CEO may be able to turn around the businessâ?? lacklustre performance, I feel that the stock is overvalued today. Too many investors and stock analysts seem to believe rather strongly that the stock will definitely rise. Prices are still near its all-time historical high.

To me, this is a case of early optimism when there is little evidence to prove that the changes will indeed yield positive results for the company.

If you too, believe that the company will definitely turn around and only do better from here onwards, then it might be worth jumping in.

However, Iâ??m not as convinced. While I do not doubt growth, I personally feel that growth will be slow. After all, you canâ??t fix things overnight. Considering rising food prices and wages, on top of the weakening global economy, I will rather wait for another better time to buy in.

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Till then,
Budget Babe
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