

# Analysis of the Development Strategies of McDonald's

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**Abstract.** Fast-food chain industry in China has been thriving for the last thirty years, with an acceleration of urbanization and changes in consumers' willingness to eat outside. It is foreseeable that the future market of the fast-food chain industry is going to be more competitive and fiercer, and how companies develop in the such environment by developing reasonable market and management strategies is vital. In this case, McDonald's is a good example to be referred to. This passage analyses McDonald's performance with its competitors adopting different financial metrics, including revenue streams, profit margins, and P/E ratios. SWOT Analysis is as well adopted to analyze how McDonald's is able to fully take advantage of its strengths and seize the opportunities to solve weaknesses and decrease threats. In addition, after CITIC and CITIC Capital have taken up a total controlling stake of 52% in McDonald's (China), a new round of reform in development strategies has begun. This passage argues that McDonald's (China) updated its localization strategies and plans of expansion, including innovating its products and advertisements strategies, along with the development of digital order and payment methods to attract more young consumers. It is concluded that, with a high marginal rate of 82% for franchise stores, McDonald's (China) plans to expand in third and fourth-tier cities and sink markets of China to boost revenues when the first-tier cities have reached saturation, accompanied by *Green Development* to fulfill its ESG goals and maintain sustainable development.

**Keywords:** McDonald's; development strategies; fast-food chain.

## 1. Introduction

### 1.1 Background, Significance, and Prospect of Research

It has been more than 30 years since McDonald's entered the Chinese market. Although the modern fast-food chain in China started relatively later than in other countries, the fast-food chain industry has played an increasingly significant part in catering services of China. The total turnover of the fast-food chain industry had increased from 190.72 billion CNY to 531.29 billion CNY from 2007 to 2017, and in the coastal regions, market shares of the fast-food chain industry have taken up more than 50% of the catering services [1].

As the most competitive fast-food chain company in the world, McDonald's total revenues has reached 23.594 billion dollars in 2021 and it is the most valuable brand in the fast-food chain industry. Accompanied by a set of its own standardized management methods, McDonald's has a deep insight into the future market and consumer habits and utilized all of its strengths to develop strategies and increase revenues.

McDonald's has excellent business performance in more than 150 countries. However, in China, until recently it outperformed its main competitor Kentucky Fried Chicken because of its nearly-adjusted localization strategies. Through the analysis of the development strategies of McDonald's (China), this article analyzed how McDonald's (China) succeeded in recent years, and how CITIC adjusted the management strategies to make McDonald's (China) better suited for the development of China in the next 20 years. It is hoped that this article would have substantial help for the practitioners of fast-food chains in China, and could be used as a reference for Chinese fast-food chain practitioners to enhance their competitiveness.

## 1.2 Literature Review

In terms of the management environment of McDonald's (China), Jingrong Chen's dissertation: Developmental Strategic Research on McDonald's (China) from Tsinghua University analyzed the external environment of McDonald's (China) using PEST analysis and gave its own suggestions on the marketing strategies [2]. Gao Hui's dissertation: Marketing Strategies Research of McDonald's (China) from Xibei University introduced a simplified situation of McDonald's and analyzed the internal situation of McDonald's (China) from the aspects of resources and capabilities [3].

In terms of analysis of franchised business, A journal named Update and Sustainable Development of Business Model in the case of McDonald's by Zhijia Tan, Wei Wei, and Wuxiang Zhu from Tsinghua University and Peking University analyzed the franchised business model of McDonald's and how McDonald's renovate such business model in the 1960s [4].

In terms of localization, despite some suggestions given by the theses above, Yanchang Liu's journal Localisation Strategy of KFC and its Enlightenment illustrated some useful strategies that McDonald's is currently utilizing or can be utilized in the future [5]. Wenting Li's Analysis of McDonald's localization Strategy in China digs into the product, channel, and promotion strategy to analyze how McDonald's tries to attract more Chinese customers [6].

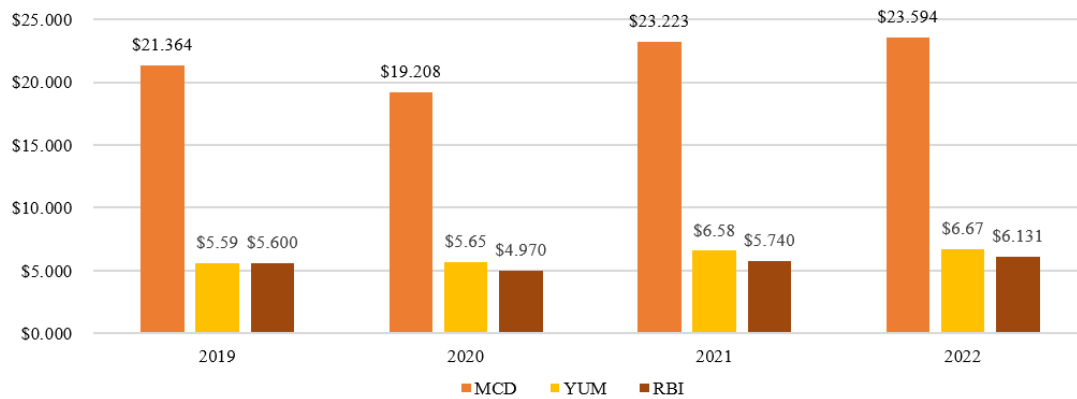
However, nearly all of the theses did not mention the impact of CITIC Limited's acquisition of the franchised right of McDonald's (China) in 2017. Among the few theses that have introduced CITIC's acquisition of franchised rights, the future expansion plan of CITIC Limited is a new round of competition against Yum! Brands are not yet been fully discussed. Meanwhile, the rapid digital development is also a must-review but has not yet been comprehensively consolidated and analyzed. Therefore, the localization strategy of McDonald's after 2017 needs to be updated and reviewed, and how CITIC Limited will manage McDonald's (China) as the master franchisee in China in the next 15 years is as well a lack of research for the existing theses.

## 2. Analysis of the Strategic Management of McDonald's

### 2.1 Revenue analysis of McDonald's

According to the 2021 Annual report of McDonald's, the company's revenues consist of sales by company-operated restaurants and fees from restaurants operated by franchisees. These fees, along with occupancy and operating rights, are stipulated in franchise/license agreements that generally have 20 years [7]. McDonald's adopt franchised restaurant model worldwide to maintain a fast speed of expansion. Moreover, apart from the positive impact of McDonald's renowned brand, McDonald's benefits from franchising by excluding rent fees and instrument maintenance fees from the cost structure, therefore generating a better net profit. It was McDonald's first introduced such a modernized franchised business model, and by 2021 93% of McDonald's restaurants worldwide are franchised.

When compared with Yum! Brands (YUM) and Restaurant Brands International (RBI), McDonald's main competitors, shows their leading position in the fast-food chain in the world. As can be seen in the following Fig. 1, McDonald's maintains the highest revenue stream. Suffering from a slightly greater impact of covid-19, which is partly due to the much larger scale worldwide, McDonald's shows its high recovery ability to thrive and continue to grow as the industry leader.



**Fig 1.** Revenue (in billions) (Photo credit: Original)

## 2.2 P/E ratio Analysis of McDonald’s

When estimating the value of McDonald’s utilizing the P/E ratio, as can be seen in Table 2, McDonald’s P/E ratios are the median of three companies annually in the past three years, which indicates that the stock price of McDonald’s is fairly-valued in the past three years. Although a slight reduction in the P/E ratio shows shrinking profitability, McDonald’s earnings profit is approximately triple that of the altogether of YUM and RBI, showing its leading economies of scale and world-class competitiveness during the recession.

**Table 1.** P/E ratio

Year	MCD	YUM	RBI
2019	24.7	23.8	29.7
2020	33.8	36.2	33.2
2021	26.55	26.2	25.5

## 2.3 SWOT analysis

SWOT Analysis method makes it practical to comprehensively analyze the advantage and disadvantages of a company, in order to find the core value of a company and to stipulate a sustainable development strategy.

### 2.3.1 Strengths

One of the most competitive strengths of McDonald’s is its renowned brand reputation built over decades, because of which its suppliers would like to build a long-term relationship, and McDonald’s can sign rent contracts with lower rent fees as well because of its high ability to attract visitors. Another strength of McDonald’s is its experienced marketing team. Accompanied by the fast speed of innovation testing, McDonald’s localization strategy successfully helps it to expand international markets at an incomparable speed. Different flavor preference varies among countries and need specialized teams to develop new products that fit with local customers.

### 2.3.2 Weakness

The main weakness of McDonald’s is its fast foods do not conform to a nowadays healthy diet. Although McDonald’s has been dedicated to improving its menu, the main dishes including hamburgers and French Fries are inevitably contrary to the modernized concept of diet.

### 2.3.3 Opportunity

The weakness stated above can be also seen as an opportunity for McDonald’s to diversify its current menu to meet the market’s demand. With 500 cal sets, McCafé meal, and Nutrition Calculator already been designed, McDonald’s ambition to develop low-caloric food is plain and Ciabatta set in China last year was its first trial to introduce light meal worldwide.

Apart from that, there are still available markets in tier-3 and tier-4 cities of China waiting for McDonald's to enter, which is also what McDonald's (China) is currently managing.

#### **2.3.4 Threat**

The fundamental threat to McDonald's is the fierce competition in the fast-food chain industry. Apart from well-known competitors such as KFC, pizza-hut, Taco Bell, and Burger King operated by Yum! Brands and Restaurant Brands International, Chinese fast-food chains, Mexican fast-food chains, and even convenience stores can be deemed as strong competitors since they all provide fast food at a relatively low price.

In conclusion, McDonald's has its unique advantage, including one-of-the-best brand reputation and supply chain, and its weaknesses and threats are the same as all fast-food companies would face. Moreover, with its first-tier product testing team, McDonald's is seizing the opportunity to diversify its menu to develop its products in different regions while maintaining its core competitiveness.

### **3. Basic Introduction of McDonald's (China)**

#### **3.1 Introduction of McDonald's (China)**

China is the second largest market for McDonald's after the United States, and McDonald's is the second largest restaurant brand in China in terms of market share of Western-style fast food after KFC of Yum! The first restaurant was opened in Shenzhen in 1990. By the end of 2021, McDonald's had opened 4,395 stores in China and employed about 200,000 people. McDonald's has five types of restaurants in China: Dessert Station (1994), McCafé (2001), 24-hour restaurant (2005), Deli Speed Drive-In (2005), and McNuggets delivery service (2007). McDonald's annual turnover is more than 10 billion RMB in China and serves more than 1 billion customers annually.

The main consumers of McDonald's are concentrated in 15 to 59 years old. In China, the population of this age group has reached about 894 million, nearly 64% of the population in China. McDonald's is committed to long-term growth in China and has increased its investment in China to accelerate its growth momentum.

#### **3.2 The difference of business model between China and other countries**

The revenue of McDonald's is from three main sources: income from real estate operations, service fees from franchised restaurants, and surplus from company-operated restaurants. McDonald's is good at real estate operations. In order to implement the real estate strategy, McDonald's has set up real estate companies to buy real estate with the money from the franchisee and then lease them to franchisees. This strategy gives the rights of the first creditor to McDonald's real estate company so that it is qualified to obtain bank loans. However, in China, McDonald's cannot follow the traditional model of "buying land then opening a store". On the one hand, there are many restrictions for foreign companies to purchase real estate, and on the other hand, facing an unfamiliar and huge market, McDonald's chose to open company-operated restaurants first to ensure the speed of expansion and brand quality.

On January 9, 2017, CITIC, CITIC Capital, Carlyle Capital, and McDonald's jointly announced a strategic partnership and the new company will become the main franchisee of McDonald's in Mainland China and Hong Kong for the next 20 years. CITIC and CITIC Capital will hold a total controlling stake of 52% in the new company, while Carlyle and McDonald's (Worldwide) will hold 28% and 20% respectively [8]. Upon completion of the transaction, McDonald's China is transformed into a Sino-foreign joint venture.

According to the official statement, McDonald's China will need to pay two fees to the headquarters: royalty fees and initial fees for new store openings. This is an indication that McDonald's China does not adopt a property-dependent business model.

## 4. The Localisation of McDonald's (China)

### 4.1 McDonald's localization strategy

Since entering the Chinese market, McDonald's has been working on localization for more than 30 years. In 2017, CITIC Limited has acquired the franchised rights of McDonald's (China) for 20 years, and CITIC Limited plans to further proceed with the transition and expansion of McDonald's (China) by localization strategy. McDonald's (China) does not adopt a relatively radical strategy compared with KFC or Pizza-hut. However, currently, its localization strategy can be deemed as a more successful case.

#### 4.1.1 Product and Advertisement innovation

Product Innovation is one of the most significant parts of localization. McDonald's (China) two star-dishes: McCrispy Chicken Burger and Grilled Chicken Burger were both specially designed to satisfy Chinese customers, and they are still the most popular products sold nowadays. It was true that McDonald's persists in international standardization, but McDonald's also tries to make every country have its own specialized standardized star dishes that can last for decades, instead of changing fast without impression [9].

In the past five years, increasingly more attempts can be seen in McDonald's menu and some of which have already been proved successful. When mainstream culture advocated for more healthy diets, McDonald's (China) did not simply use its north American low-caloric diets for references but developed a completely new set for Chinese customers called the 500-cal set. 500-cal set is mixed with star dishes and some low-calorie snacks such as apple or corn, combined with coke zero, with the intent to maintain the classic flavor of burgers and simultaneously lower the caloric intake. Such sets vary differently from the product sold in the United States, which more resemble American-style breakfast. Moreover, McDonald's is developing low-caloric food set in China as well, and Ciabatta set introduced in China last year was its first trial to introduce light meal burgers.

Apart from 500 cal sets, in other product lines, with McCafé meal and Angus Burger introduced to the Chinese market, McDonald's plan to compete against Starbucks and Burger Kings at a higher price shall not be ignored. Both McCafé and Angus Burger are targeted at office workers with better consumption ability. McCafé has expanded various sets of breakfast and afternoon tea, while Angus Burger has developed the quality of dinner. Both sets show that McDonald's (China) is trying to make a transition, especially in metropolitan cities, with the purpose to attract more office workers by updating fancier products.

In terms of advertisement innovation, McDonald's (China) adapts a steadier strategy as well. It was in 2017 that McDonald's followed the example of KFC to firstly hired a celebrity endorser [10]. However, McDonald's (China) still holds a conservative attitude on celebrity endorsement.

Focusing more on the younger generation, what distinguishes McDonald's (China) from its competitors is how it attract youngster by running different social media platforms. Lower price and more selectable coupons are McDonald's core competitiveness when attracting young people, and McDonald's try its best to let every youngster get to know the discount. No matter on Weibo, Red, or Douban, it is agreed by the users that McDonald's normally gives a better discount compared with other fast-food companies. Once customers accept the idea that McDonald's stays closer to them, they would more likely to consume and even introduce social media as a return.

McDonald's (China) also teaches every franchisee to run its own WeChat community to attract active customers. It is simple to get a few coupons every day if participating in free Q&A, which improves the stickiness of customers even if they do not participate but just in the WeChat groups watching such interactions. In this case, with less advertisement cost, McDonald's (China) also achieved an ideal effect of advertising.

#### 4.1.2 Digital Development

The digital development of McDonald's (China) has been going through generations. 2022 is the fifth year that McDonald's (China) has been known as Golden Arch. Localization of e-commerce is

what CITIC Limited has stressed and persisted [11]. Nowadays, how McDonald's (China) develops an online ordering platform working with delivery producers and portable payment methods is critical for the future development of the Chinese market.

In 2017, the first year CITIC Limited acquired the franchised right of McDonald's (China), McDonald's (China) announced that it has successfully accomplished a transition called future 2.0. It has developed self-help ordering machines in more than 1000 restaurants and will introduce them to all restaurants. Apart from that, online order was developed very soon. McDonald's (China) was one of the few early companies that worked with WeChat pay and Alipay. In addition, shortly after WeChat and Alipay introduced the mini-program, McDonald's (China) followed up to develop its mini-programs in both applications to allow customers to order online ahead of picking up food or direct delivery. Furthermore, they also invented their own apps which occasionally include more coupons. All programs have clean but clear interfaces and are user-friendly.

## **4.2 Analysis of franchised restaurants in China**

### **4.2.1 High Margins of franchised restaurants**

There are two kinds of business models in McDonald's-- franchise restaurants and company-operated restaurants. There's no huge difference between the revenue of these two restaurant models. But there's a huge difference between the cost and margin rate. There's a high marginal rate of 82% for franchise stores in 2021. while the company-operated restaurant's margin rate is only 17%. Because these two restaurants are completely different ways of operating.

For the franchise restaurant, McDonald's provides franchisees with a long-term lease for the location. The franchisees are responsible for all equipment, seating, décor, and signage. Franchisees are also responsible for reinvesting capital back into their businesses to make improvements. The franchised revenues include rents, royalties based on a percent of sales & Initial fees. The franchised costs include lease expenses & depreciation [12].

For the company-operated restaurants, McDonald's operates stores and produces its own products. These are two completely different types of business models.

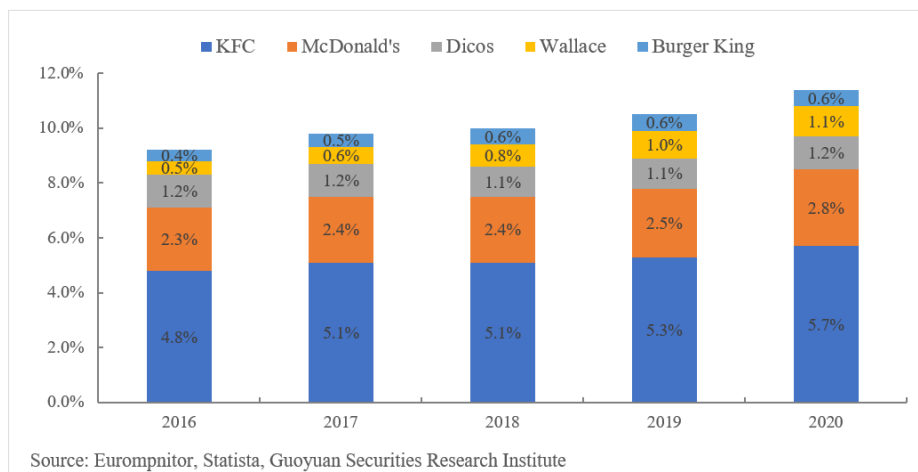
There're 40,031 McDonald's restaurants at the end of 2021 and 93% of restaurants were franchised. In the future, McDonald's long-term goal is to make the franchising proportion approach 95%. In August 2003, the first franchised restaurant was opened in Tianjin China.

### **4.2.2 Future expansion in the next 5 years**

#### **4.2.2.1 Accelerate store expansion and expand the sink market**

McDonald's sold its 80% stake in China in 2017, in order to bring in capital, and plans to increase the proportion of franchise restaurants with the funds. McDonald's said CITIC and Carlyle have rich resources in real estate, finance, supply chain, consumer retail, and technology, which are conducive to the further development of McDonald's business, including opening new restaurants, boosting sales of existing restaurants, and enhancing menu innovation, convenience services, digital retail, and takeaway. McDonald's (China) is expected to open a number of new restaurants in Mainland China and Hong Kong in the next five years. While accelerating business development in Mainland China and Hong Kong, McDonald's (China) will continue to uphold McDonald's business philosophy of Quality, Service, Cleanliness, and Value (QSC&V), as well as the strict requirements for food safety.

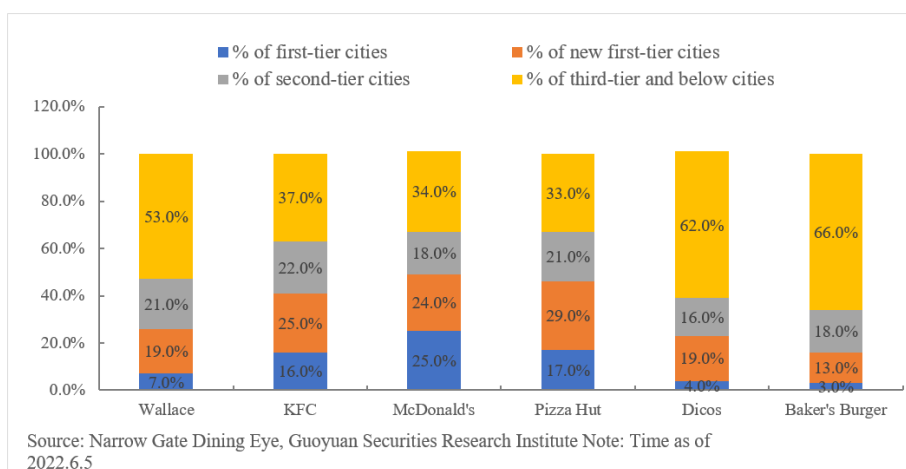
The first step is to increase the proportion of franchised restaurants. The proportion of McDonald's franchised restaurants worldwide has increased to 95% as of June 30, 2022. During the same period, McDonald's had 39,696 restaurants worldwide, including 4,727 restaurants in China, an increase of 644 restaurants from 2021 [13].



**Fig 2.** Market share of Western fast-food brands in the Chinese fast food market, 2016-2020 (Photo credit: Original)

The market size of Western fast food in China has reached 238.1 billion RMB in 2020, with a CAGR of 4.6% from 2016 to 2020, higher than the Chinese fast-food (3.9%) and the average level of the fast-food industry (4.1%). The market size is expected to reach 476.2 billion RMB in 2025, maintaining rapid growth in the future. From the competitive landscape, KFC and McDonald's occupied the top two positions in the market, benefiting from the growth of the fast-food industry. According to Fig. 3: Euromonitor data, in 2020, the share of KFC China in the fast food market is about 5.7%, followed by McDonald's, accounting for about 2.8%, McDonald's maintained rapid growth in 2020.

McDonald's (China) media spokeswoman Xu Yingting said another major purpose of equity transfer is to vigorously develop the fast-food chain market in third and fourth-tier cities. As of December 31, 2021, there are more than 13,000 McDonald's restaurants in the United States, while China has a population of 1.3 billion, the current number of McDonald's restaurants is only about 4,500. The market has huge market growth space, McDonald's (China) is still very optimistic about the opportunity to expand into the blank cities of the third and fourth tier markets. Zhang Jiayin said at the media conference that it is expected that by the end of 2022, about 45% of McDonald's restaurants will be located in third and fourth-tier cities.



**Fig 3.** Distribution of major fast-food brands by city level (Photo credit: Original)

According to Fig. 4 data from Narrow Gate Dining Eye, as of June 5, 2022, McDonald's share of third and fourth-tier cities was 34%, which is still far from the target of 45%. In the long run, McDonald's still has a lot of space for development in China, but the current epidemic impact coupled with the decline of profits in the short term still puts it at some risk. Whether McDonald's can break

through the development bottleneck, the key point may not lie in the localization operation. The key to McDonald's downward expansion to third and fourth-tier cities in the next five years lies in its ability to maintain high standards of supply chain management. Secondly, McDonald's will be in close combat with a wide variety of local restaurant brands.

#### 4.2.2.2 Promote the concept of Green Development

Currently, McDonald's is promoting Future 2.0 restaurants, including integrating cashless payment, a self-ordering system, delivery to the table, etc. In the plan of Vision 2022, more than 75% of restaurants will offer delivery services. The coverage of Future 2.0 restaurants will be increased to over 90%, providing more customers with a digital and user-friendly dining experience. By the end of 2022, the number of McDonald's green restaurants is expected to exceed 1,800.

LEED-certified green restaurants are those certified by the U.S. Green Building Council (USGBC) and required to meet the standard of 'Leadership in Energy and Environmental Design (LEED)'.

Restaurants need to follow environmental standards from site selection to design, building materials, construction and energy management, etc. In addition to green restaurants, McDonald's will also build its green growth engine through three major aspects: green packaging, green supply chain, and green recycling [14].

McDonald's (China) now uses paper certified by the Forest Stewardship Council (FSC) for all of its paper packaging. At the same time, it has stopped using plastic straws. Compared with the previous packaging, McDonald's has reduced the amount of paper used by nearly 80%.

In terms of the supply chain, according to media reports, 100% of the cod purchased by McDonald's (China) comes from fisheries certified by the Marine Stewardship Council (MSC) to ensure that the suppliers are committed to sustainable sourcing concepts in farming and catching to minimize environmental impact.

In addition, McDonald's (China) is committed to achieving a circular economy by rebuilding waste plastics into restaurant items through its "Reinventing Good Stuff" program.

As can be seen, McDonald's current strategy in China is still focused on accelerating store expansion and expanding the third and fourth-tier cities markets. This process, also takes into account the Green Development concept that is currently being promoted.

## 5. Conclusion

McDonald's has a globally renowned brand reputation and supply chain. Its development of franchised stores through real estate as well as its ability to rapidly localize its strategy has kept it a globally recognized FMCG brand. McDonald's outperformed its competitors based on both revenue data and P/E ratio comparisons. After 2021, McDonald's revenue quick recovery, and its P/E ratio shows its leading economies of scale and world-class competitiveness during the recession.

But McDonald's also faces many challenges, such as the impact of the epidemic on store operations, the demands of carbon neutrality on McDonald's strategy, people's reduced desire to consume high-calorie, high-sugar foods, and the emergence of more and more localized brands.

McDonald's is also actively taking the challenges of the external environment and internal operations, by increasing the number of franchised stores, developing markets in third and fourth-tier cities in China, and advocating the implementation of the *green development* concept. In terms of strategy, McDonald's is actively promoting innovation in products and marketing strategies, as well as the transformation of digital marketing.

The study of McDonald's localization development is useful for us to see how a global brand strategically pushes its standardization to the world, how it insists on brand reputation, how its franchise model is localized, and how it responds to the needs of local users to adjust its product supply and quickly localizes by leveraging local resources. This is meaningful for China's brands to go abroad, both for FMCG brands and for chain brands in other industries.

To quote Chris Kempczinski, President and CEO of McDonald's, the McDonald's system remain strong and resilient, but 'the operating environment across the competitive landscape remains

challenging. There are some shortcomings in this study, as we had difficulties in obtaining financial data of McDonald's (China), so we were not able to analyze its financial changes and profitability after its localization in China. McDonald's (China) has no plans to go public for the time being, but we believe McDonald's can maintain its strengths and continue to grow while persisting with its expansion.

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