McDonald's Corporation

"We will continue to pursue opportunities to extend our relevance with a particular emphasis on three key areas: service enhancements, restaurant reimaging and menu innovation. We will innovate at every tier of our menu to sustain our momentum and create excitement for our customers…one more step on our journey to modernize our brand and improve customer relevance."

— Jim Skinner, Vice Chairman and CEO, McDonald's Corporation

Oakbrook, Ill., February 2011. The U.S. supply chain management team of McDonald's Corporation was meeting to set parameters for sourcing ingredients of the company's new menu items initiative. These new items were a key part of the company's strategic initiative launched in 2003: *Plan to Win*. This initiative set out to refocus the company on improving the consumer experience at McDonald's restaurants. One key element of this strategy was keeping the products relevant.

The Real Fruit Smoothie line (Exhibit 1) and Fruit and Maple Oatmeal (Exhibit 2) had both been successfully test marketed during the past six months. These products were ready to become part of McDonald's permanent menu offerings, and they contained new ingredients. The Real Fruit Smoothies included fruit purees (strawberries, blueberries, blackberries, and banana); the oatmeal product contained fresh and dried fruits (red and green apples, dried cranberries, and golden and regular raisins). Some of these fruits were new to the supply chain or, in some cases, required significant increases in volume. Team members had spent months developing an understanding of each commodity, the production supply chain (fruit grower, first-stage processor, puree producer, distribution and restaurant), where and how it was grown, how it was processed, who processed and marketed it, how it was shipped and stored, and how it was priced and sold. Now, the team needed to transition its procurement activities from test marketing to rapid growth and steady replenishment to ensure a supply of quality product for the McDonald's restaurants and customers.

McDonald's supply chain is one of the largest and most sophisticated procurement systems in the fast food industry, enabling the company to reliably serve a consistent menu of safe, quality and affordable food to 64 million customers worldwide each day. As the team discussed their progress

Case Study: For Discussion Purposes Only — September 28–30, 2011. This case study was prepared by McDonald's Corporation and Kenneth McCorkle, executive vice president of agricultural industries at Wells Fargo Bank, as a basis for class discussion and represents the views of the authors, not the university. The author would like to thank Vicki Spiller and Sheila Musolino from McDonald's Corporation for their collaboration on this case.

toward adding these new items to McDonald's supply chain, a number of important questions surfaced:

1. What criteria should McDonald's use in selecting its long-term suppliers of each new commodity?
    a. For its berry puree products, at which levels of the supply chain should McDonald's work: the grower, the first-stage processor/freezer or the puree manufacturer? Why?
    b. For its fresh apple products, at which level of the supply chain should McDonald's work: the grower, the packer/shipper or the processor (slicer/packager)? Why?
    c. For its dried fruit products (raisins and cranberries), at what level of the supply chain should McDonald's work: the grower or the processor? Why?
2. How should McDonald's structure its relationships with these suppliers to ensure reliable short- and long-term supplies, consistent high quality, competitive prices, flexibility of supply and manageable price volatility?
3. How can the company develop relationships with these suppliers that encourage the generation of new product ideas, production and logistical innovations and efficiencies, and other creative ideas beneficial to both the supplier and McDonald's?
4. How can the company maintain flexibility and avoid creating relationships that become overly codependent — suppliers overly dependent on McDonald's, and McDonald's overly dependent on individual suppliers?
5. The McDonald's brand is built on consistency of experience, reliability of menu, quality and service. Can the company successfully, and cost effectively, offer seasonally available products without disrupting this brand identity? If so, what products are good candidates for seasonal offerings? What are the implications of offering these seasonal items for the supply chain?
6. Longer term, how will McDonald's uphold its corporate commitment to procure raw materials (food ingredients and packaging) only from sustainably managed lands for these new commodities?

Quick Service Restaurant (QSR) Industry

The QSR market is defined as the sale of food and drinks for immediate consumption either on premise or elsewhere. According to IBISWorld (December 2010), U.S. fast food is a $184 billion in sales, $5.5 billion in net profit industry and constitutes 56 percent of all dining revenue. McDonald's Corporation is the industry leader with a 12.7 percent market share[1], followed by Yum Brands (KFC, Taco Bell, Pizza Hut) at 9.7 percent, Wendy's/Arby's Group at 6.6 percent, Starbucks at 5.9 percent, Burger King at 5.1 percent and Doctor's Associates (Subway) at 5.0 percent. The domestic industry is characterized as mature: growth is slow; profit margins are

[1] Based on total domestic franchised and company-owned gross system-wide revenue.

tightening; competition is intense; and regional markets are saturated. (In July 2011, Wendy's Group sold 81.5 percent of Arby's to Atlanta-based, private-equity firm Roark Group.)

Despite the presence of these large, well-known and branded QSRs, the industry remains relatively fragmented: nearly 48 percent of the industry's 300,000 establishments are small-business operators with fewer than nine employees. An additional 52 percent have between 10 and 99 employees. Barriers to entry remain low. Industry concentration has increased only marginally.

From 2005 to 2010, growth was unusually slow (only 0.4 percent), largely attributable to a weakened economy, persistently high unemployment and slow growth in personal disposable income. Industry revenue declined by 3.3 percent to $178.6 billion in 2009, but recovered to $184 billion in 2010, a 3 percent growth rate.

According to IBISWorld, key external drivers impacting the industry's performance over the next five years include:

- Consumer spending: Personal consumption increases with stronger economic growth and higher per capita disposable income. When personal consumption expenditure is high, consumers spend money on eating away from home, including at fast food restaurants.
- Consumer sentiment: Changes in consumer sentiment affect household expenditures on discretionary items, including fast foods. During recessionary periods, consumers tend to trade down in their purchases opting for less expensive formats and products.
- Health consciousness: Consumers are increasingly aware of issues related to weight, obesity, fatty food, salt intake and food safety. Sectors selling meat, hamburger products and fried foods are being disproportionately affected by this consumer trend. Subway was among the first QSRs to capitalize on consumer health and weight concerns. The company successfully marketed the health benefits of its sandwiches. McDonald's also successfully introduced a healthy choices menu that includes salads, fruit and yogurt parfaits, apple dippers, etc.
- Competition from alternative formats: QSR operators compete among themselves, with full-service restaurants, caterers, convenience stores and supermarkets offering prepared foods. Some sectors of the fast food industry have benefited from consumers trading down from other more expensive formats. Nevertheless, competition among fast food chains has intensified as each has focused on taking market share.

IBISWorld is forecasting that industry revenue will increase to $208.2 billion by 2015 (2.5 percent annual growth), benefiting from an improving economy, a declining unemployment rate and increased consumer spending. Competition will remain intensely focused on pricing and new product introductions. Healthy food alternatives (non-red meat, Mexican foods, pasta, fresh salads) are projected to be key menu additions. International expansion, particularly in Asia and the Middle East where market penetration remains low, is expected to be the largest source of revenue and profit growth for the major QSRs. Industry profitability is projected to only marginally improve because of ongoing competition in the low-growth, saturated domestic market.

McDonald's Corporation

McDonald's Corporation is the iconic brand in the fast food business worldwide. The company franchises and operates approximately 33,000 restaurants in 118 countries. Of these, about 80 percent are operated by franchisees, while 20 percent are operated by the company. Eight key markets — the United States, Canada, France, Germany, the United Kingdom, Australia and Japan — contribute approximately 70 percent of the company's revenue. Forty-three percent of its restaurants are within North America; these restaurants generated 43 percent of the system sales, 35 percent of company revenues and 49 percent of McDonald's operating profit.

Under its franchising agreement, McDonald's owns (or secures the long-term lease for) the land and building. The franchisee provides a percentage of the initial capital required (via investment in equipment, signs, seating and décor) and by reinvesting in the business over time.

While McDonald's considers itself primarily a franchisor, the more capital-intensive, company-owned/operated stores play an important role in the company's success. These restaurants allow McDonald's to develop, test and refine operating standards, marketing ideas, new products and pricing strategies that could be introduced system wide.

The restaurants offer a variety of value-priced items, such as hamburgers, chicken sandwiches, French fries, salads, desserts, soft drinks, shakes, coffee and other beverages. In addition, McDonald's breakfast menu includes Egg McMuffin, Sausage McMuffin with egg, McGriddles, biscuit and bagel sandwiches, pancakes and muffins.

Company revenues consist of sales from company-operated stores, plus fees from franchised stores. These include an initial fee, rent for the land and building owned by McDonald's and royalties based on a percentage of sales. The company's stated financial growth objectives include:

- Long-term, system-wide sales growth of 3 to 5 percent
- Average operating income growth of 6 to 7 percent
- Average annual returns on incremental invested capital in the high teens every year

The Origin of McDonald's: Ray Kroc

Although Ray Kroc did not open the first McDonald's restaurant, it was his vision, his philosophy, and his passion for quality and efficiency that continues to guide the corporation. In 1954, while working as a paper cup and multi-mixer salesman, Ray Kroc was surprised by a large order for eight multi-mixers from a restaurant in San Bernardino, Calif. At the location, he found a small but successful restaurant, founded in 1940 and run by brothers Dick and Mac McDonald. He was particularly impressed by their operation's effectiveness. The McDonald brothers produced a limited menu, concentrated on a few items — burgers, fries and beverages — and focused on quality at every step.

Kroc envisioned a chain of McDonald's restaurants all over the United States and successfully proposed the idea to the brothers. In 1955, he founded the McDonald's Corporation, and within five years, acquired the exclusive rights to the McDonald's name. By 1958, McDonald's had sold its 100 millionth hamburger.

Part of Kroc's vision was to build a restaurant system known for consistently high-quality food and uniformity in its preparation methods. He wanted to serve burgers, buns, fries and beverages that tasted the same regardless of where they were purchased.

To achieve this consistency, he envisioned both franchisees and suppliers that were working not for McDonald's, but for themselves, together with McDonald's. He promoted the slogan, "In business for yourself, but not by yourself." His philosophy was based on the three-legged stool principal: one leg was McDonald's; the second, the franchisees; and the third, McDonald's suppliers. The stool was only as strong as the three legs.

Kroc believed in the entrepreneurial spirit and rewarded franchisees for individual creativity. Many of McDonald's most famous menu items, including the Big Mac, Filet-O-Fish and the Egg McMuffin, were created by franchisees. At the same time, the McDonald's operating system insisted franchisees follow the core McDonald's principles of quality, service, cleanliness and value.

McDonald's passion for quality meant that every ingredient was tested, tasted and perfected to fit the operating system. As restaurants boomed, the massive volume of orders caught the attention of suppliers, who began taking McDonald's standards as seriously as McDonald's did. As other QSRs began to follow, the high standards rippled through the meat, produce and dairy industries.

Kroc again sought partnerships — this time with McDonald's suppliers — to assist him in creating the most integrated, efficient and innovative supply system in the food service industry. These supplier relationships flourished over the decades, and many McDonald's suppliers operating today first started business with a handshake from Ray Kroc.

Kroc operated with a strong sense of ethics and trust with the suppliers. He often asked suppliers for assistance even with financing in the early years to help grow the business. With their faith in Kroc and his vision, suppliers were rewarded with volume increases as McDonald's experienced growth. He worked with suppliers as partners, relying on them for their business acumen. These partners recognized that if McDonald's was successful, the suppliers would also be successful. Kroc truly felt they were partners and valued what they could bring to the business, and in turn, was willing to share the benefits that would be enjoyed by the entire "system" — the franchisees, the suppliers and the corporation. To this day, McDonald's suppliers continue to provide franchisees in-store training on how to properly handle their products and equipment to assure the best customer experience.

Two of Ray Kroc's notable quotations demonstrate his commitment to ethics and trust in his relationships with his business partners:

- It's easy to have principles when you're rich. The important thing is to have principles when you're poor.
- None of us is as good as all of us.

In 1961, Kroc launched a training program, later called Hamburger University, at a new restaurant in Elk Grove Village, Ill. There, franchisees and operators were trained in the scientific methods of running a successful McDonald's. Hamburger University also included a research and development laboratory to explore new cooking, freezing, storing and serving methods. By 2011, Hamburger University boasted more than 80,000 graduates.

Kroc was also a firm believer in giving "something back into the community where you do business." In 1974, McDonald's acted upon that philosophy in an original way by opening the first Ronald McDonald House in Philadelphia to provide a "home away from home" for the families of children in nearby hospitals. Twelve years after this first house opened, 100 similar Ronald McDonald Houses were in operation across the United States.

Although Kroc died on January 14, 1984, his passion for innovation and efficiency, his relentless pursuit of quality and his commitment to charitable causes continues to be an inspirational, integral part of McDonald's today.

Recent History

McDonald's original product line consisted exclusively of branded hamburgers, fries and fountain drinks. Through extraordinarily efficient procurement and logistics support, plus standardized, efficient in-store preparation, this menu could be consistently produced and profitably priced within a range attractive to its customers. Furthermore, through its combination of company-owned and franchised stores, the McDonald's concept was scalable across the country and internationally. Thus, new McDonald's restaurants sprang up worldwide and the company flourished. The stock price soared by 5,700 percent from 1980 to 1999.

But in the late 1990s and entering the new millennium, the company's success began to fade. The field of players within the QSR industry was getting crowded. McDonald's historical focus on the consumer and the basics of quality, cleanliness and service may have shifted to growing store locations and efficiencies. Competitors had significantly challenged McDonald's position as the value leader, and company sales and profits slowed. The stock price dropped precipitously over three years from more than $36/share to $11/share.

In 2003, management launched its *Plan to Win* strategic initiative. This plan was the blueprint to reinvent the company and achieve its objective of becoming "better, not just bigger." The *Plan to Win* program refocused the company on restaurant execution and value with the goal of improving the overall customer experience. *Plan to Win* identified the five core drivers of McDonald's business — people, products, plan, price and promotion — and aligned its owner-operators, suppliers and employees around initiatives that drive results. As *Plan to Win* evolved, so did the menu as consumers' tastes changed. The new products, Real Fruit Smoothies and Fruit and Maple Oatmeal, are part of that *Plan to Win* strategy; they are products designed to increase the relevance of McDonald's product line to its customers.

Results of the *Plan to Win* strategy were both immediate and ongoing. Since it was introduced in 2003, the company's earnings and stock have again soared from $11/share in 2003 to more than $75/share entering 2011. Even during the economic downturn beginning in 2008, McDonald's was ideally positioned to thrive. Where much of the traditional restaurant trade experienced significant declines in patrons and dollar sales, McDonald's sales continued to grow as consumers sought out lower cost and higher value in their food purchases. Strong consumer demand combined with deflationary food costs resulted in consistently strong margins, returns on assets and returns on equity. Exhibits 3 and 4 show company income statements and balance sheets for the past three years. Exhibit 5 shows a return on equity analysis for McDonald's and three of its public competitors. Exhibit 6 shows the company's stock price over the past 40 years.

The Supply Chain

David Bell, professor of agribusiness at the Harvard Business School, recently described the origins and evolution of the food supply chain as follows:

> A supply chain mentality has existed for decades. The idea was that food started with farmers who grew the crops, and then the processors thought about how they could use these raw foods to make products for customers. Consumers went to the store, saw the items available and decided what they would eat.
>
> Now, it's become much more driven from the consumer end. Industry players have to get closer to the customers and become more responsive to their needs. In order to do that, the vertical food chain must become more integrated. By this, I don't mean having one company grow the crops, process the food and build a store for selling it. Instead, retailers must become more integrated with their suppliers, and suppliers must become more integrated with the farmers. The real thrust is for the information loop to move much faster so that the time between identifying a product consumers want and being able to grow, process and put it on the shelf is much shorter. Everyone is going to have to work more as partners than competitors. Global success will be driven by the capacity to establish seamless partnerships that serve customers.

McDonald's recognized the value of an effective supply chain long before professors were discussing the concept. Its unique supply chain is at the heart of the company's success in supplying 64 million customers worldwide each day. Management views the McDonald's supply chain as a key competitive advantage: it mitigates cost; it ensures a supply of safe product; and it provides the quality and innovative products on which the company's success depends. These factors, in turn, drive better value to the customer, strengthen the brand and drive stronger business performance. The McDonald's supply chain is also very difficult to replicate.

In order to maintain the strong level of trust required of a franchising relationship between the company and the franchisees, McDonald's believes the supply base should be independent of the corporation. Suppliers are independently owned and operated to keep the relationship arm's length and to allow each company the ability to focus in their areas of expertise. For the strategic products, the company is interested in creating strong relationships with suppliers that are flexible, responsive and willing to invest for the long-term benefit of the relationship. Often, these relationships are with privately owned companies that do not have branded products to support; thus, they can focus closely on their relationship with McDonald's.

For product categories considered non-strategic (i.e., these products do not impact the consumer experience, owner-operator cash flow or company performance in a significant way) the supply chain strategy will likely be more transactional. In this case, the benefits of a transactional approach often outweigh the losses of influence, leverage and alignment.

In its strategic relationships, McDonald's has developed, among its suppliers, a unique culture of aligned values, internal governance, anticipatory (rather than reactive) management and flexibility. This culture is based on common ideals that work to the benefit of the entire system:

- Transparency, inclusion and trust among parties
- Long-term relationships (which outperform the sum of individual transactions)
- Focus on the system first, rather than the individual success of suppliers, McDonald's or franchisees
- Financial success for all through shared risk and shared reward: win, win, win
- Anticipatory issues management: predicting and proactively addressing issues before they become crises

Management identifies several factors contributing to the uniqueness of the McDonald's supply chain and making it difficult for others to replicate:

- Quality standards: McDonald's establishes the standards for and expectations associated with product quality and safety, as well as corporate social responsibility that includes sustainable supply. In addition to delivering against product-quality standards (e.g., how a given food should look and taste), McDonald's suppliers are expected to meet all food safety and quality systems requirements. As part of and in a manner consistent with these requirements, suppliers are responsible for managing their supply chains on behalf of the system or brand. For certain products, particularly those determined to be higher risk (e.g., fresh cut produce that is a "ready-to-eat" food without heating), McDonald's takes an active leadership role throughout the supply chain to assure delivery of safe, high-quality product.
- Strategic sourcing: McDonald's goals are imparted to its suppliers via its strategic relationships to efficiently provide quality products to its restaurants, to foster innovation and to increase the rate at which new solutions can be brought to market.
- Supplier investment: It is expected that suppliers take a long-term view, making production and distribution investments without guarantees; thereby, freeing McDonald's to invest in growth and effectiveness of the system.
- Risk management: McDonald's collaborates with and relies on its suppliers and industry experts to better understand the risks and opportunities in managing commodity price volatility.
- Distribution/logistics: McDonald's sets standards for the distribution network, as well. These distribution centers (DCs) are essential to ensuring quality, safety, timeliness, consistency and efficiency in product delivery. The DCs are independently owned and

operated, but linked by strategic plans that drive optimization in service, quality and cost for the entire system.

- Technology leveraging: McDonald's size and reach provides opportunities to view demand from an aggregate perspective — "One View of Demand." The company is in the process of providing visibility to suppliers at all levels of the supply chain. From this perspective, the company plans to minimize waste and optimize inventory volumes. Appropriate technology will be leveraged to streamline the restaurant ordering process and optimize product deliveries.
- Transparency in cost structure: McDonald's seeks relationships that disclose their cost structures and "unbundles" their package deals such that costs can be managed jointly by both the supplier and McDonald's. Only by understanding the true cost of the product and services being offered, can the supplier and the company seek opportunities to jointly improve the efficiency of the supply chain.

The McDonald's supply chain and its logistics and distribution capabilities are key competitive advantages from multiple perspectives. They enable the company to consistently offer its customers safe, high-quality food at an affordable price. They encourage supplier innovation. They measure, recognize and reward performance.

McDonald's believes in the power of a synergistic relationship with their suppliers. Creating aligned expectations for supplier performance is critical in meeting McDonald's and suppliers' business needs.

The Supplier Performance Index (SPI) is a global continuous improvement process that promotes supplier excellence, system alignment and enhanced business results. The SPI is the primary tool used to measure achievement on specific goals and provide feedback on meeting expectations. The index focuses on and measures six high-level business criteria:

1. Management vision and values
2. System first
3. Optimized supply
4. Quality systems
5. Innovation
6. Predictable competitive pricing

The sustainability portion of the SPI acknowledges McDonald's relatively recent recognition of sustainability as a driver of supply chain competitiveness — today, and especially in the long term, through efficiency, assured supply and brand trust. The McDonald's vision for sustainable supply includes "3 E's" — ethical, environmental and economic outcomes. The ethical focus addresses how people and animals are treated in its supply chain, the environmental about protecting natural resources, and the economic about the long-term financial health of the entire value chain, including farmers and equitable trade practices.

The company points to several key accomplishments during the past two years in developing and implementing sustainable practices in its supply chains (Exhibit 7):

- The company developed a comprehensive Sustainable Land Management Commitment with input from the World Wildlife Fund. It summarizes the company's commitment to work with suppliers toward ensuring that all agricultural raw materials for its products originate from legal and sustainably managed land sources.
- It successfully sourced more than 98 percent of its fish from fisheries with favorable sustainability ratings.
- All of McDonald's 500 approved abattoirs underwent and passed animal welfare audits.
- The supplier environmental scorecard, which requires suppliers of the top six categories (beef, poultry, packaging, toys, potatoes and buns) to provide data on waste, energy and water use for the top nine markets moved online.

New Product Introductions

McDonald's is continuously looking for new growth opportunities. From its original, limited-selection offering, the McDonald's menu has expanded to include dairy and other dessert products, chicken and fish products, breakfast sandwiches and entrees, fruit and salads to maintain competitive appeal and attract a broader customer base. Historically, some of these ideas originated with franchise owners, some from suppliers and some from internal development teams.

During the 1990s and into the new millennium, management identified two trends that it felt the company could leverage:

1. Demographics: The demographics of world population in general, and the U.S. population in particular, were changing. The average age was rising, and the number of young consumers (McDonald's target market) was not growing as fast as the number of customers "graduating" from their McDonald's years. The company had targeted and positioned itself to serve this younger market in its product line, advertising, promotional activities, restaurant layout and even its spokesperson, Ronald McDonald. As its customers aged, the company was constantly required to maintain their customers and make their product offerings more relevant to the young adult. As this population grew up, McDonald's had lost touch with what young-adult consumers wanted — a great meal, at a great price, every day.
2. QSR industry: Alternative QSR formats were rapidly rising in popularity. Coffee houses were appearing in nearly every community and, in big cities, on nearly every block. These coffee houses offered more than just premium-priced, specialty coffees; they were becoming a social hangout for like-minded high school and college-age youth, often with money to spend. To this young crowd, the experience was as important as the product. Concurrently, juice bars expanded from California, spreading the concept of healthy, nutritious juice-based beverages.

First, McDonald's focused on value. It built a strong base for a very important consumer segment who wanted value and convenience. With a focus on value and increasing accessibility through late-night and early morning hours, McDonald's gained permission to innovate with food and compete with the alternative QSRs with beverages. The success of these two concepts provided ideas and impetus to expand McDonald's target market and extend its product line to meet a broader range of customers. Internationally, McDonald's introduced the McCafé concept in 1992 — company-owned or franchised coffee houses focused on coffee drinks and complementary food items. Domestically, premium roast coffees were added to all McDonald's restaurants in 2006, followed shortly thereafter by specialty coffee drinks, including lattes, mochas and cappuccinos in a variety of options and flavors. Given the nation's daily 400-million-cup thirst for coffee, these products quickly became important contributors to same-store sales growth and profitability.

McDonald's latest new products initiative focused on expanding the menu choices well beyond the company's historical roots. The new product offerings were positioned to appeal to a broader demographic profile and new preferences by the consumer, thus attracting more patrons through McDonald's restaurants. These new products provided the company new nutritious items to advertise and promote, a key to keeping the restaurant chain fresh and relevant. The strong nutritional profile of these products also provided value by addressing current consumer concerns for a balanced diet and managing calorie intake.

In July 2010, after months of product development and test marketing, McDonald's rolled out its Real Fruit Smoothie products nationwide. These two products — a wild berry smoothie (yogurt plus strawberries, blueberries and blackberries) and a strawberry-banana smoothie — required the U.S. procurement team to create supply chains capable of reliably delivering these commodities to each of its U.S. restaurants for serving 365 days each year. Thus, the procurement team needed to familiarize itself with the principal growers and processors to understand the growing and processing seasons, along with the economics of these businesses, to assess the impact McDonald's volume would have on specific fruit supply segments, and to enter relationships with reliable suppliers both in the primary supply of puree and in the secondary procurement of the fruit. These activities were quite significant. If the smoothie products succeeded, McDonald's would virtually overnight become among the largest domestic purchaser of each of these products. Thus, the procurement team needed assurance that consistently high-quality products would be reliably available at a cost enabling McDonald's to provide a value to their customer and generate acceptable margins — that McDonald's presence in the market for these commodities would neither deplete the supply nor push their prices unacceptably high.

All the fruit procured by the puree processor was sourced as fresh fruit and shipped to the puree supplier based on McDonald's specification and expected demand. These berries would be the raw material from which the puree manufacturers would produce puree for delivery to each McDonald's restaurant. The bananas would be fresh, sourced from Central America.

In January 2011, the company was rolling out another new product — Fruit and Maple Oatmeal. One year earlier, two competitors launched oatmeal products, adding an alternative and line extension to their pastry/muffin and juice-oriented menus. McDonald's oatmeal product, introduced to all 14,000 domestic stores, is prepared in each store and contains fresh red and green apple slices, golden and regular raisins and dried cranberries. The product boasts a caloric count of only 290 calories in addition to all the other positive nutritional attributes of oatmeal (fiber, cholesterol fighter, etc.) and fruit. Once again, this item required procurement of new commodities from new suppliers.

Given the current consumer interest in food nutrition and the degree of political activism among city, state and federal governments, McDonald's management believes its current expansion of its nutritious menu items is appropriate.

Looking Ahead

Entering 2011, McDonald's is riding high. Its market share is growing faster than the overall category. Its profitability and return on assets and equity is substantially better than its competitors. Its stock price is near an all-time high. Furthermore, McDonald's top management sees tremendous opportunity for its brand, an opportunity to further differentiate and distance itself from the rest of the industry. "The company brings what no competitor can match — a scale advantage in voice, convenience and cost; a brand advantage in predictable value, family fun and familiar taste; and a strong balance sheet and cash flows to support continued investment in the business."

Discussion Questions

1. As an adviser to McDonald's senior management:
    a. How would you critique McDonald's strategy of expanding its array of product offerings?
    b. Are the recent additions — Real Fruit Smoothies and Fruit and Maple Oatmeal — the right products to be adding? Are there others you would recommend?
    c. What criteria would you use to determine what should be added and what should be avoided?
    d. How would you critique the McDonald's supply chain? Are there any changes you would suggest?
2. As an adviser to the supply chain management team:
    a. What criteria would you propose for selecting suppliers for each of the new product ingredients?
    b. What recommendations would you make regarding the structure of the relationships with these suppliers to ensure reliable short- and long-term supply, consistent high quality, competitive prices and manageable price volatility?
    c. How can these relationships be structured to encourage the generation of new product ideas, production and logistical innovations and other creative ideas beneficial to both McDonald's and the supplier?
    d. How should McDonald's deal with the supply issue of becoming overly codependent with its suppliers?
    e. How and when should the McDonald's long-term commitment to procuring its products only from sustainably managed lands be included in its new supplier relationships?
    f. With these new products now launched, the next phase may be seasonal flavors. Will different supply relationship be required to secure a reliable supply of these seasonal commodities given McDonald's need to change the commodities and production throughout a single year?

Exhibit 1

McDonald's Real Fruit Smoothie line launches

By Alicia Kelso
July 13, 2010

McDonald's Corp. is retiring its fruit and walnut salad later this year, but it won't abandon fruit on the menu all together. Today, the company saw the nationwide launch of its new McCafé Real Fruit Smoothie line, marking the final component in the brand's specialty beverage strategy.

The frozen drinks (which include real fruit blends, fruit juice, ice and low-fat yogurt) are available in strawberry-banana and wild berry flavors. The latter is a combination of strawberries, blueberries and blackberries.

The smoothies can also be customized with or without low-fat yogurt.

They are available in small (12 ounces), medium (16 ounces) and large (22 ounces), and the suggested retail price of a small smoothie is $2.29.

"The addition of the smoothies to the McCafé beverage line reinforces McDonald's as a convenient destination for a variety of quality, great-tasting beverages at a value only McDonald's can offer," said Ashlee Yingling, spokeswoman for McDonald's USA.

Thus far, the specialty beverage line – which includes espresso-based drinks and frappes and was initially introduced in the United States in 2009 – has helped the company exceed its initial goal of adding $125,000 in annual sales to the average U.S. store.

In addition to the nationwide launch, participating McDonald's stores will hold three national sampling days beginning July 22.

According to Darren Tristano, executive vice president of foodservice consultants Technomic, Inc., it makes sense for McDonald's to delve into the smoothie market.

"For McDonald's to compete with Jamba Juice or Smoothie King seems like a great idea because they'll have the product available at the drive-thru and at a 'better price,'' he said. "It will also allow their guests to upgrade into something different — a smoothie can be a snack or a meal, so McDonald's adds convenience and becomes more of a one-stop shop."

Consumers will also be excited about the "healthy perspective" of the smoothie, according to Tristano.

"Because there is fruit and there is yogurt, this product has a perception of fresh and that translates into a perception of healthy — regardless of its sugar content or calorie count," he said. "This is an indulgent and a crave-able product."

Exhibit 1, cont.

He also expects the McDonald's launch to be a boon for the smoothie market overall. Although it will increase competition for the Jamba Juice-type of specialty locations, anything McDonald's puts out will increase exposure.

"It will be competitive and may draw some traffic away from places like Smoothie King or Jamba Juice, but it will also create more awareness and a greater demand for this product," Tristano said. "I think ultimately it will translate into more sales for the other places."

Source: QSRWeb.com

Exhibit 2

McDonald's oatmeal now available

McDonald's has officially upped the ante on the quick-service breakfast wars with a national roll out of its new fruit and maple oatmeal.

The item is available at all 14,000 U.S. stores and is offered all day. It is the chain's first new breakfast offering since 2008.

The oatmeal is made of 100-percent natural whole grain oats, light cream and brown sugar, and is topped with diced red and green apples, dried cranberries and two types of raisins. Each bowl, sold at a suggested retail price of $1.99, is made upon request.

"With McDonald's Fruit & Maple Oatmeal, we're offering a portable, affordable and balanced breakfast solution to help customers start their day right," said Cindy Goody, Ph.D., MBA, R.D., senior director of nutrition at McDonald's. "McDonald's wants to help make it easier and more inviting for our guests to eat more whole grains and fruits, and fruit and maple oatmeal is an effective way to help our customers integrate these important food groups into their daily diets." The item has 290 calories (260 calories without brown sugar), 32 grams of whole grain oats and provides about 25 percent of the daily recommendations for fruit.

McDonald's began testing oatmeal earlier this year in the Washington, D.C., and Baltimore markets. The new offering further positions the QSR giant against Starbucks and Jamba Juice, which already sell oatmeal. Starbucks' oatmeal comes with packets of dried fruit and nuts and is priced at $2.45, while the Jamba Juice product is $2.95 and comes in different varieties such as berry cherry pecan.

Prior to the new oatmeal rollout, McDonald's threw down the gauntlet with these two chains with its successful McCafe line featuring a variety of coffee options and, most recently, smoothies.

Source: QSR Magazine 1/3/11

Exhibit 3

McDonald's Corporation Income Statements, 2008-2010

View: **Annual Data** | Quarterly Data — All numbers in thousands

Period Ending	Dec 31, 2010	Dec 31, 2009	Dec 31, 2008
Total Revenue	**24,074,600**	**22,744,700**	**23,522,400**
Cost of Revenue	14,437,300	13,952,900	14,883,200
Gross Profit	**9,637,300**	**8,791,800**	**8,639,200**
Operating Expenses			
Research Development	-	-	-
Selling General and Administrative	2,135,100	2,011,900	2,355,500
Non Recurring	29,100	(61,100)	(48,500)
Others	-	-	-
Total Operating Expenses	-	-	-
Operating Income or Loss	**7,473,100**	**6,841,000**	**6,332,200**
Income Tax Expense	2,054,000	1,936,000	1,844,800
Minority Interest	-	-	-
Net Income From Continuing Ops	4,946,300	4,551,000	4,313,200
Non-recurring Events			
Discontinued Operations	-	-	-
Extraordinary Items	-	-	-
Effect Of Accounting Changes	-	-	-
Other Items	-	-	-
Net Income	**4,946,300**	**4,551,000**	**4,313,200**
Preferred Stock And Other Adjustments	-	-	-
Net Income Applicable To Common Shares	**4,946,300**	**4,551,000**	**4,313,200**

Currency in USD.

Exhibit 4

McDonald's Corporation Balance Sheets, 2008-2010

View: **Annual Data** | Quarterly Data

All numbers in thousands

Period Ending	Dec 31, 2010	Dec 31, 2009	Dec 31, 2008
Assets			
Current Assets			
Cash And Cash Equivalents	2,387,000	1,796,000	2,063,400
Short Term Investments	-	-	-
Net Receivables	1,179,100	1,060,400	931,200
Inventory	109,900	106,200	111,500
Other Current Assets	692,500	453,700	411,500
Total Current Assets	**4,368,500**	**3,416,300**	**3,517,600**
Long Term Investments	1,335,300	1,212,700	1,222,300
Property Plant and Equipment	22,060,600	21,531,500	20,254,500
Goodwill	2,586,100	2,425,200	2,237,400
Intangible Assets	-	-	-
Accumulated Amortization	-	-	-
Other Assets	1,624,700	1,639,200	1,229,700
Deferred Long Term Asset Charges	-	-	-
Total Assets	**31,975,200**	**30,224,900**	**28,461,500**
Liabilities			
Current Liabilities			
Accounts Payable	2,916,400	2,970,600	2,506,100
Short/Current Long Term Debt	8,300	18,100	31,800
Other Current Liabilities	-	-	-
Total Current Liabilities	**2,924,700**	**2,988,700**	**2,537,900**
Long Term Debt	11,497,000	10,560,300	10,186,000
Other Liabilities	1,586,900	1,363,100	1,410,100
Deferred Long Term Liability Charges	1,332,400	1,278,900	944,900
Minority Interest	-	-	-
Negative Goodwill	-	-	-
Total Liabilities	**17,341,000**	**16,191,000**	**15,078,900**

Exhibit 4, cont.

McDonald's Corporation Balance Sheets, 2008-2010

Stockholders' Equity			
Misc Stocks Options Warrants	-	-	-
Redeemable Preferred Stock	-	-	-
Preferred Stock	-	-	-
Common Stock	16,600	16,600	16,600
Retained Earnings	33,811,700	31,270,800	28,953,900
Treasury Stock	(25,143,400)	(22,854,800)	(20,289,400)
Capital Surplus	5,196,400	4,853,900	4,600,200
Other Stockholder Equity	752,900	747,400	101,300
Total Stockholder Equity	**14,634,200**	**14,033,900**	**13,382,600**
Net Tangible Assets	**12,048,100**	**11,608,700**	**11,145,200**

Currency in USD.

Exhibit 5

Historical Performance Measures for Major Public Fast Food Operators

McDonald's Performance Measures

	ROE =	Profitability X	Asset Turnover X	Leverage
	Profit / Equity	Profit / Sales	Sales / Assets	Assets / Equity
2004	2279	2279	17889	27838
	14201	17889	27838	14201
	16.0%	**13%**	**0.64**	**1.96**
2005	2602	2602	19117	29989
	15146	19117	29989	15146
	17.2%	**14%**	**0.64**	**1.98**
2006	3544	3544	20895	28974
	15458	20895	28974	15458
	22.9%	**17%**	**0.72**	**1.87**
2007	2395	2395	22787	29392
	15280	22787	29392	15280
	15.7%	**11%**	**0.78**	**1.92**
2008	4313	4313	23522	28462
	13383	23522	28462	13383
	32.2%	**18%**	**0.83**	**2.13**
2009	4551	4551	22745	30225
	14034	22745	30225	14034
	32.4%	**20%**	**0.75**	**2.15**
2010	4946	4946	24074	31975
	14634	24074	31975	14634
	33.8%	**21%**	**0.75**	**2.18**

Source: Company Records

Yum Brands Performance Measures

	ROE =	Profitability X	Asset Turnover X	Leverage
	Profit / Equity	Profit / Sales	Sales / Assets	Assets / Equity
2008	964	964	11279	6527
	-108	11279	6527	-108
	-8.9%	**8.5%**	**1.73**	**-60.4**
2009	1071	1071	10836	7148
	1025	10836	7148	1025
	104.5%	**9.9%**	**1.52**	**6.97**
2010	1158	1158	11343	8316
	1576	11343	8316	1576
	73.5%	**10.2%**	**1.36**	**5.28**

Source: Yahoo Finance

Exhibit 5, cont.

Historical Performance Measures for Major Public Fast Food Operators

Wendy's/Arby's Performance Measures

	ROE =	**Profitability X**	**Asset Turnover X**	**Leverage**
	Profit	Profit	Sales	Assets
	Equity	Sales	Assets	Equity
2008	-480	-480	1822	4646
	2383	1822	4646	2383
	-20.1%	**-26.3%**	**.39**	**1.95**
2009	5	5	3580	4975
	2336	3580	4975	2336
	0.2%	**0.1%**	**0.72**	**2.13**
2010	-4	-4	3416	4733
	2163	3416	4733	2163
	0.0%	**-0.1%**	**.72**	**2.19**

Source: Yahoo Finance

Starbuck's Performance Measures

	ROE =	**Profitability X**	**Asset Turnover X**	**Leverage**
	Profit	Profit	Sales	Assets
	Equity	Sales	Assets	Equity
2008	315	315	10707	6386
	2491	10707	6386	2491
	12.6%	**2.9%**	**1.68**	**2.56**
2009	391	391	9775	5577
	3046	9775	5577	3046
	12.8%	**4.0%**	**1.75**	**1.83**
2010	946	946	10383	5673
	3675	10383	5673	3675
	25.8%	**9.1%**	**1.83**	**1.54**

Source: Yahoo Finance

Exhibit 6

McDonald's Stock Price (last 40 years)

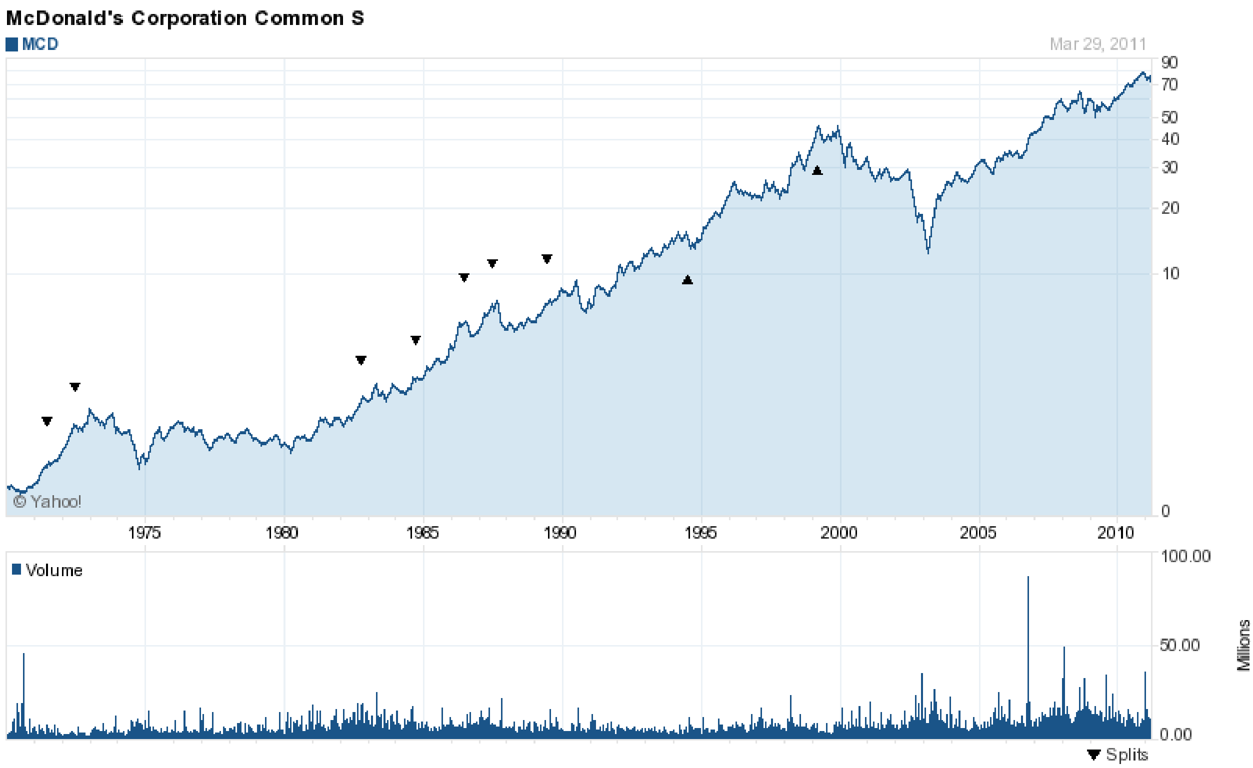

Exhibit 7

McDonald's Sets Long-Term Sustainable Beef, Coffee Plans

By Jonathan Bardelline
March 11, 2011

OAK BROOK, IL — McDonald's has laid out a plan to move to more sustainable meat, coffee and packaging.

The company's Sustainable Land Management Commitment will require suppliers to gradually source food and materials from sustainably-managed land, though there are no specific timelines for now, and it is initially focusing just on beef, poultry, coffee, palm oil and packaging.

Those five were chosen, with the help of analysis from the World Wildlife Fund, since they have the most potential to be changed to have lower impacts. Beef, especially, has some of the biggest impacts among McDonald's foods.

Exhibit 7, cont.

The United Nations Food and Agriculture Organization reported in 2006 that beef accounts for 18 percent of greenhouse gas emissions globally, pumping out not only carbon dioxide, but nitrous oxide and methane, which are more potent than CO2 in contributing to global warming.

Beef production also degrades and pollutes land and water due to animal wastes, antibiotics and hormones, as well as fertilizers and pesticides used on crops for feeding livestock.

McDonald's is initially sponsoring a three-year study, by the E-CO2 Project, of carbon emissions from 350 beef farms in the United Kingdom and Ireland, and it is working with the Global Conference on Sustainable Beef.

Growing demand for beef has also led to deforestation, such as in the Amazon and its related ecosystems. Since 1989, McDonald's has had a policy to not buy beef from deforested areas of Brazil. The company now plans to create a program for tracing and certifying beef raised sustainably in the Amazon.

As for poultry, McDonald's has worked to avoid sourcing feed, mainly soya, from deforested areas by working with major soya purchasers and creating a voluntary agreement to not buy soya from deforested lands. The company will also gather best practices for managing poultry waste, which, like beef waste, can harm water systems.

The company's European and other non-U.S. operations have already made headway in buying more sustainable coffee, with all stores in Australia, New Zealand and 39 European countries buying coffee that's certified by the Rainforest Alliance or Utz. In the U.S., McDonald's says it will create a plan for giving farmers training on sustainable operations and work on reporting purchases of certified coffee.

For palm oil, the company plans to join the Roundtable on Sustainable Palm Oil and aims to only buy palm oil certified by the roundtable by 2015, a goal shared by companies like Walmart and General Mills.

Since the bulk of McDonald's packaging is paper, its packaging work has revolved mainly around getting fiber from "legal and acceptable" sources and giving preference to certified sources. Among the various wood certification programs, McDonald's gives preference to Forest Stewardship Council certification, but also recognized the Sustainable Forestry Initiative, Programme for the Endorsement of Forestry Certification, CSA International and Cerflor.

Along with announcing the Sustainable Land Management Commitment, McDonald's released its latest corporate responsibility report, in which it says it will put out a report later this year on pesticide and fertilizer use on potato crops. The report is based on a survey of suppliers that was created in response to a shareholder resolution.

Source: McDonald's