Final report

ASSIGN BUSTER

B. For McDonald's Corporation (McDonald's) and Burger King Holdings, Inc. (Burger King), the three of the largest variable expenses for the years ended December 31, 2003 to 2005 and June 30, 2004 to 2006 are food and paper, payroll and employee benefits, and occupancy and other operating expenses (Burger King Holdings, Inc. a, 2006; McDonald's Corporation, 2005).

For McDonald's, food and paper for the three years ended December 31, 2003 to 2005 were $4314. 8 million, $4, 852. 7 million, and $5, 207. 2 million respectively, constituting 31. 16%, 31. 26%, and 31. 68% of the total operating costs and expenses respectively (McDonald's Corporation, 2005). For Burger King, food and paper for the three years ended June 30, 2004 to 2006 were $391 million, $437 million, and $470 million respectively, constituting 23. 26%, 24. 43%, and 25. 03% of the total operating costs and expenses respectively (Burger King Holdings, Inc. a, 2006). Food and paper are only incurred with each burger sold.

For McDonald's, payroll and employee benefits for the three years ended December 31, 2003 to 2005 were $3, 411. 4 million, $3, 726. 3 million, and $4, 039. 2 million respectively, constituting 23. 84%, 24. 00%, and 24. 57% of the total operating costs and expenses respectively (McDonald's Corporation, 2005). For Burger King, payroll and employee benefits for the three years ended June 30, 2004 to 2006 were $382 million, $415 million, and $446 million respectively, constituting 22. 72%, 23. 20%, and 23. 75% of the total operating costs and expenses respectively (Burger King Holdings, Inc. a, 2006). Although payroll and employee benefits for support staff such as finance and human resources are more or less fixed cost, we can reasonably assume that they are only a small proportion of total payroll and employee benefits. Since McDonald's has more than 8, 000 restaurants

worldwide (McDonald's Corporation, 2005) and Burger King has more than 1, 200 restaurants worldwide (Burger King Holdings, Inc. a, 2006), we can expect that most of the payroll and employee benefits are incurred for crew members. Payroll and employee benefits for crew members are semi-fixed costs. A crew member can handle a certain number of burgers within any period. Beyond this level, another crew member has to be hired.

For McDonald's, occupancy and other operating expenses for the three years ended December 31, 2003 to 2005 were $3279. 8 million, $3520. 8 million, and $3867. 7 million respectively, constituting 22. 92%, 22. 68%, and 23. 53% respectively (McDonald's Corporation, 2005). For Burger King, occupancy and other operating expenses for the three years ended June 30, 2004 to 2006 were $314 million, $343 million, and $380 million respectively, constituting 18. 68%, 19. 17%, and 20. 23% respectively (Burger King Holdings, Inc. a, 2006). Included inside occupancy and other operating expenses are occupancy expense that may not be a variable cost. Occupancy expenses are most likely lease fees and rent and therefore represent fixed costs (Burger King Holdings, Inc. a, 2006, McDonald's Corporation, 2005). However, other operating expense most likely comprises packaging cost and miscellaneous costs such as costs of paper cutlery. Such costs are variable costs. Packaging and paper cutlery are incurred for each burger sold.

The below calculations in Table 1 to 4 show the financial impact food and paper, payroll and employee benefits, and occupancy and other operating expenses have had on McDonald's and Burger King's margins and profitability for the years ended December 31, 2003 to 2005 and June 30, 2004 to 2006 respectively.

First, let's take a look at McDonald's. As can be seen from Table 1, food and paper reduces profit margin by 25% in all three years, payroll and employee benefits reduce profit margin by 20% in all three years, and occupancy and other operating expenses reduce profit margin by around 18% to 19% in all three years. As can be seen from Table 2, food and paper reduces return on assets by 17% to 18% in all three years, payroll and employee benefits reduce return on assets by 14% in all three years, and occupancy and other operating expenses reduce return on assets by 13% in all three years.

Table 1

McDonald's Corporation

Financial Impact of the Three Largest Variable Expenses on Profit Margin for the Years Ended December 31, 2003 to 2005

2005

2004

2003

Food and Paper

5207. 2/20460. 2= 25. 4%

4852. 7/19064. 7= 25. 45%

4314. 8/17140. 5= 25. 17%

Payroll and Employee Benefits

4039. 2/20460. 2= 19. 74%

3726. 3/19064. 7= 19. 55%

3411. 4/17140. 5= 19. 90%

Occupancy and Other Expenses

3867. 7/20460. 2= 18. 90%

3520. 8/19064. 7= 18. 47%

3279. 8/17140. 5= 19. 13%

(McDonald's Corporation, 2005)

Table 2

McDonald's Corporation

Financial Impact of the Three Largest Variable Expenses on Return on Assets

for the Years Ended December 31, 2003 to 2005

2005

2004

2003

Food and Paper

5207. 2/[(29988. 8 + 27837. 5)/2]= 18. 01%

4852. 7/[(27837. 5+25838. 0)/2]= 18. 08%

4314. 8/[(25838+24194)/2]= 17. 25%

Payroll and Employee Benefits

4039. 2/[(29988. 8 + 27837. 5)/2]= 13. 97%

3726. 3/[(27837. 5+25838. 0)/2]= 13. 88%

3411. 4/[(25838+24194)/2]= 13. 64%

Occupancy and Other Expenses

3867. 7/[(29988. 8 + 27837. 5)/2]= 13. 38%

3520. 8/[(27837. 5+25838. 0)/2]= 13. 12%

3279. 8/[(25838+24194)/2]= 13. 11%

(McDonald's Corporation, 2005)

Next, let's turn our attention to Burger King. As can be seen from Table 3, food, paper, and product costs reduce profit margin by 22% to 23% in all three years, payroll and employee benefits reduce profit margin by 21% to 22% in all three years, and occupancy and other operating costs reduce

profit margin by around 18% to 19% in all three years. As can be seen from Table 4, food, paper, and product costs reduce return on assets by 17. 82%, 16. 22%, and 14. 67% in 2006, 2005, and 2004 respectively, payroll and employee benefits reduce return on assets by 16. 91%, 15. 40%, and 14. 33% in 2006, 2005, and 2004 respectively, and occupancy and other operating costs reduce return on assets by 14. 41%, 12. 73%, and 11. 78% in 2006, 2005, and 2004 respectively.

Table 3

Burger King Holdings, Inc.

Financial Impact of the Three Largest Variable Expenses on Profit Margin for the Years Ended June 30, 2004 to 2006

	2006	2005	2004
Food, Paper and Product Costs	470/2048= 22. 95%	437/1940= 22. 53%	391/1754= 22. 29%
Payroll and Employee Benefits	446/2048= 21. 78%	415/1940= 21. 39%	382/1754= 21. 78%
Occupancy and Other Operating Costs	380/2048= 18. 55%	343/1940= 17. 68%	314/1754= 17. 90%

(Burger King Holdings, Inc. a, 2006)

Table 4

Burger King Holdings, Inc.

Financial Impact of the Three Largest Variable Expenses on Return on Assets

for the Years Ended June 30, 2004 to 2006

2006

2005

20041

Food, Paper and Product Costs

470/[(2552+2723)/2]= 17. 82%

437/[(2723+2665)/2]= 16. 22%

391/2665= 14. 67%

Payroll and Employee Benefits

446/[(2552+2723)/2]= 16. 91%

415/[(2723+2665)/2]= 15. 40%

382/2665= 14. 33%

Occupancy and Other Operating Costs

380/[(2552+2723)/2]= 14. 41%

343/[(2723+2665)/2]= 12. 73%

314/2665= 11. 78%

(Burger King Holdings, Inc. a, 2006; Burger King Holdings, Inc.: financial statement, n. d.)

DQs

1. Marketable securities are securities that can be easily converted into cash. Such securities will generally have highly liquid markets allowing the security to be sold at a reasonable price very quickly (Marketable Securities, n. d.).

They are thus appropriate investments in the management of cash because their rate of return is higher than cash, but they can be converted more readily into cash than securities that are not easily marketable such as closely-held stock.

2. If a firm has too much cash on hand, it means that the firm is not optimizing its investment opportunities since cash earns a low rate of interest.

3. Inventory level should be just right. Too high an inventory level would incur a high level of holding cost. Besides, the inventory might turn obsolete. On the other hand, too low an inventory level would result in lost sales when demand cannot be met.

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