AN OVERVIEW OF CORPORATE GOVERNANCE WITH RISK MANAGEMENT INSIGHT OF MCDONALD

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AN OVERVIEW OF CORPORATE GOVERNANCE WITH RISK MANAGEMENT: INSIGHT OF MCDONALD

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ABSTRACT

Corporate Governance management is a very important aspect in the any types of organization. This study is aimed to test the McDonald’s overall performance with specific risk to avoid or reduce any kind of risk that organization need to play important role to efficiently manage the corporate governance element. The data is integrated from McDonald’s annual report which from year 2014 until 2018. The analysis shows that company’s risk affected by corporate governance towards company’s performance. From this research suggest that McDonald’s should control their risk in the smart way to prove the McDonald’s more reputation and stable.

Keywords: corporate governance, risk, performance, Return on Assets (ROA)
1.0 INTRODUCTION

1.1 Company’s background

In year 1940, McDonald’s is established in the United States. It is considered as the world’s largest fast food restaurants. McDonald has more than 36,000 outlets in 119 countries worldwide. Every day, there are approximated 68 million of customers been served by McDonald. McDonald sells various types of food and beverage which include burgers, chicken, French fries, breakfast items, soft drinks, milkshakes, and desserts. Currently, consumers are much concern about the health therefore McDonald has expanded their menu by including salads, smoothies, fruit, and seasoned fries. The corporation form of McDonald is currently operated under franchise, an affiliate and its corporation.

1.2 The Existing Corporate Governance Mechanisms

McDonald’s company are having the board of directors where they can make decision fast. There is a board of directors below a unitary board structure, consisting of independent director and independent non-executive director, emphasizing the fact that they will act in the best interests of the broader shareholder population. In unitary board, the chairman (non-executives directors) will be classification as non-executive director, will contribute an external perspective on risk management and deal with people issues, such as the future shape of the board and resolution of conflicts.

1.3 Corporate Governance problems based on the features of Corporate Governance

1.3.1 Accountability

Accountability is defined as a person or individual that help making decision and implementation of action in the company for specific issues will be accountable for the decisions and action they make. Management is accountable to the Board and the Board is accountable to shareholders. This relates to the auditor of McDonald; Catherine A. Hoovel didn’t show the financial statements to its board of shareholders. She was not accountable to the work.
1.3.2 Responsibility
A key issue in corporate governance is to decide who should have responsibility, whether directors should be liable for their performance to the stakeholders. Executive managers are responsible for the operations of the business, and the ultimate responsibility rests with the CEO. Stephen J.Easterbrook wasn’t responsible for the accounts that has been shown throughout 2011-2018.

1.3.3 Transparency
As it is in scientific research, transparency refers to the ease with which an outsider can make a meaningful analysis of a company and its actions. Transparency means openness, accountability and honesty. In companies, organizations, administrations and communities, transparency is carried out. In McDonald’s case, the auditor not the CEO/chairman is not able to give a meaningful financial statement to the shareholders.

1.4 Aims of the study
This study is aimed to identify the relationship between corporate governance with the variables of credit risk, operation risk, liquidity risk and market risk against company’s performance.

1.5 Research Objectives
The purpose to conduct this research is to investigate the determinants that will be affected by corporate governance towards company’s performance. The objectives are as below:

1. To identified internal factors of McDonald’s affect dependent variable.
2. To identified external factors of McDonald’s affect dependent variable.
3. To investigate how internal and external factors are affecting the dependent variable.

1.6 Research Questions
1. Is there any internal factors of McDonald’s affect dependent variable?
2. Is there any external factors of McDonald’s affect dependent variable?
3. How internal and external factors are affecting the dependent variable?
2.0 LITERATURE REVIEW

2.1 Introduction
This chapter will further explain about the literature review that related to this study. The
literature review included corporate governance, credit risk, liquidity risk, market risk,
operation risk and performance of a company.

2.2 Corporate Governance
According to Bury & Leblanc (2007), corporate governance refers to the system by which
company are directed and unpaid. Besides, a set of relationship in between company’s
performance, board, stakeholders and other stakeholders with providing the structure through
the objectives of the company are set and means of attending those objectives and monitoring
performance. Good corporate governance purpose is to provide support to the board and
management in pursuing goals in the interests of the corporation and its shareholders.

Furthermore, according to Rahim (nd), corporate governance also has the important roles for
the company. From here, they need to make sure all the responsibilities are always maintaining
as usual. For example, need to make sure for the financial reporting take their duty for the
various stakeholders to increase the governance mechanisms. Corporate governance describes
a set of relationships between a company’s management, shareholders and other stakeholders.

Corporate governance is defined as a system where companies are direct and control by
monitoring who save and invest their capital to earn a return the relationship between corporate
managers, directors and the providers of equity, people and institutions who save and invest
their capital to earn a return. It ensures that the board of directors is accountable for the pursuit
of corporate objectives and that the corporation itself conforms to the law and regulations.

It is the process by which managers and auditors manage their responsibilities towards the
company’s shareholders and larger stakeholders. It can give shareholders greater confidence in
a fair return on their investment. It can also provide company stakeholders with an assurance
that the company is responsible for managing its environmental and community impact.

When they refer to a company’s stakeholders and shareholder, shareholders are the
management team of the company and the shareholders are who hold some of the company’s
share. So, it will provide the bad news when all the agents fail to follow the principle of corporate governance.

2.3 Corporate governance and credit risk

Nowadays, it is very outstanding that company will facing for the credit risk. According to Astrom, (2013) we can know that credit risk means that the loss of default swap or on the other third parties. Through this credit risk, we also can know different types of risk such as operational risk, rate of return risk and others.

The shareholders should encourage the fast food company to enhance the risk management so that it can increase the value of company by implication its value to shareholders. From these three sources that we search can increase the value. For example, minimize the costs of financial, minimize the value of taxes and minimize the possibility that the company may be forced to give up on the projects because lack of funds (Fatemi & Fooladi, 2006).

In opposite for the shareholder, the hypothesis of the managerial risk which based on the agency argument that managers will maximize their own personal as well. Means that the managers may deal with the risk management for practices the shareholders expenses. Especially, when the interests are not very perfectly with the managers, managers may seek for the risk management strategies that designed to insulate their own personal wealth for affects the interest rates, prices and foreign currency values. This decision may be taken and not to think for the shareholders wealth.

Therefore, whether shareholder will maximize the managerial risk or encourage the risk management to be defend. One of the important forms of the management of credit risk especially for the company of the financial services industry.

Credit risk appears from uncertainty for the counterparty ability to achieve the obligations. The more the counterparties and overspend for the obligations. From here means that credit risk management already being carry out by the company in financial services to manage risk management. Most companies try hard to have a high level of corporate governance so that not easily affects for the company credit risk.

Credit risk is the possibility of a loss from borrower’s failure to repay a loan or meet contractual obligations. Therefore, it is also used loosely to mean the probability of default, regardless of the value that stands to be lost.
2.4 Corporate governance and liquidity risk
According to Giannotti, Gibilaro, & Mattarocci, (2011) liquidity is the capability that bank might be improve the assets without any loss to fulfill the liability so that it could overcome all the problems. Banks cannot increase the liquidity because of the funding liquidity risk may affects the unforeseen liquidity that need to increase from fortuity conditions. The ripeness transformation of short-term deposits turns into long-terms loans, the banks will be easily assault into the liquidity risk. Moreover, at the limited time period, bank will unable to solve the deal in the limited time. The weakness of banks for liquidity risk is decided by the funding risk and market risk.

Many researchers have examined the relationship between liquidity ratios and indicators of financial performance under fast food industry. According to (Deventer, Imai, & Mesler, 2013) for our knowledge, there are no incorporated liquidity risk in financial management, but the risk is real and should be measured. The main intention is to manufacture a model for comprise the risk and liquidity risk into exchange pricing. In our research, exchange is pretended to be transferable, it is means that liquidity risk.

For example, if the value of exchange is negative and occurs in the default, the value is invalidated. Then, if the value of exchange is positive in the default, the default can sell the value with some probability. For the McDonald’s company, if the value can be sold smoothly, there will no impact on the value of exchange. If the value cannot be sold, there will be gain to the non-default. Because the value is invalidated and the non-default rescue from the liability.

2.5 Corporate governance and operational risk
Operational risk is defined as inequal processes, people and system in the internal and external company. It can be including in internal risks and external risks. The example of internal risks are systems and process, health and safety, environmental, fraud and reputation and strategic risk while example of external risks are accidental, intentional, disease, geological and weather and environmental. By having operational risks in the company, it will decrease the satisfaction of the customers, affected company image and relationship with shareholders and stakeholders (Segal, 2019).

Operational risk in McDonald’s company is always placed under supply chain of food. According to Fearne, Hornibrook et al, (2001), fast food industry nowadays not only need to
care about food safety legislation, it also needs to increase customer satisfaction, the cost of the food and services been provided. Christopher, Peck, & Towill, (2006) said that the company must establish just-in-time principle in their company and maintain re-stock level of the stock in supply chain to ensure they able to provide the food for the customers without made them feel disappointed. Supply chain can be divided into two types of risk which included risk when the problems of coordinating demand and supply follow by disruptions to normal activities (Kliendorfer and Saad, 2015).

By referring to the Shetty, et al. (2019), the operational risk arises when it is lacked regular checks in performance and inequal control of internal and external company. The reasons of bank’s workers will be creating fraud activities which counted as operational risks been identified. Therefore, it is clearly said that if corporate governance mechanism unable to control the standard of the workers in the company, it will directly lead to operational risk. In the areas, corporate governance is having significant relationships towards operational risk.

2.6 Corporate governance and market risk
Market risk is well-known as systematic risk. It can be defined as when an investor involved in the financial markets, the possibility he or she might be faced and lead to performance level (Chen, 2019). Market risk can be caused by fever sources such as terrorist attacks, disasters, political issues etc.

According to Chen, (2019), basically, investors and analysts will use value-at-risk (VaR) model to measure market risk. This model is a statistical risk management method that quantifies a stock’s potential loss. It can be used to count the probability potential loss that occurred. Even VaR model is well-known, however, it has its limitation where it is acceptable for short-term period and less accurate for long-term measurement.

According to Al-Hadi, Hasan, & Habib, (2016), if market risk has been disclosed, it will affect a company’s implied cost of capital and investor confidence can be improve as well (Dobler, 2008). However, by referring to Al-Yahyaee, (2014) and Verrecchia, (2001), some of the managers aware of inside information do not report to shareholders regarding poor performance of the company. With the help of corporate governance mechanism, it not only helps to align shareholders’ interest, it also provides advisory role of management for board of
directors (Al-Hadi, Al-Yahyaee, Hussain, & Taylor, 2019). Corporate governance leads the board of directors to be more qualified and enough knowledge to guide managers.

2.7 Corporate governance and performance of a company
As clearly know there is always significant relationship in between corporate governance and company performance (Naciti, 2019; Kumar & Zattoni, 2016). This is a simple principle when a company does not apply the principles of corporate governance, it will lead to depreciation level performance of the company. When the performance of the company become very worst, it will lead to bankrupt. Company’s stakeholders and stockholders play important role to company’s performance. However, some of the papers found that the relationships between corporate governance and performance of a company is not always significant (Munisi, 2014).

According to Munisi, (2014), company performance in corporate governance’s studies are usually measured by using accounting performance and market valuation. Alternatives will be used as well for accounting performance and market valuation which is well-known as ROA and Tobin’s Q.

The dependent variable in the study is company profitability which measured here by the Return on Asset (ROA) and defines as:

$$\text{ROA} = \frac{\text{Net Profit after Tax}}{\text{Total Asset}}$$

By having corporate governance, it changes the mind thinking of boards of directors. This action affects the performance of the company. When there is a decision situation involved a conflict of interest between corporate management and stockholders, the efficiency of the board director to engage will become a critical determinant for the decision outcome.
3.0 METHODOLOGY

3.1 Introduction
Methodology is a method to be used in a data collection and information research. Normally the research methodology used to achieve the study goals in order to achieve a good outcome at the end of the research. The purpose of this research was to identify McDonald’s company’s corporate governance and its determinants. The main tool used in this research to collect data through the Social Science Statistical Package (SPSS) version 25. In this research the main tool uses to collect data through SPSS version 25.

3.2 Statistical Technique
The company we choose is the McDonald’s company. We select the use random data in this statistical technique. We also collect McDonald’s five-year annual report, which is 2014 until 2018. The annual report is to investigate and identify the firm’s internal factor and investigate and identify the firm’s internal and external factors.

3.3 Statistical Package for Social Sciences (SPSS)
To measure the data, SPSS was used to obtain better results. The SPSS software that assists researchers in carrying out an error-free statistical data analysis. The SPSS normally used to conduct a data collection-based analysis that is descriptive statistics, bivariate statistics, and predicted numerical results. In addition, the SPSS conducts the measurement of linear regression and correlation between variables in this researcher.

3.4 Data Analysis
The data analysis depends on the future dependent variable conceptual framework of the study and two independent variables. The framework for research is stated as follows:
The research framework is to determine the influence of the dependent and independent variables and multiple regression analysis was used. The multiple regression can be presented in the equation from as follows:

\[
LR = \beta_0 + \beta_1 ROA + \beta_2 CR + \beta_3 QR + \beta_4 ACP + \beta_5 OR + \beta_6 OM + \beta_7 CGI + e \quad \text{Equation 1}
\]

\[
LR = \beta_0 + \beta_1 GDP + \beta_2 INFLA + \beta_3 IR + \beta_4 ER + \beta_5 STDV + e \quad \text{Equation 2}
\]

\[
LR = \beta_0 + \beta_1 \text{INTERNAL FACTOR} + \beta_2 \text{EXTERNAL FACTOR} + e \quad \text{Equation 3}
\]

3.5 Sampling Technique
Analysis unit is that the entity’s major being studied during a research. The population of this research is the McDonald’s companies. In addition, data are collected from McDonald’s annual report for five years from 2014 to 2018. The information collected for dependent and independent variables that are an internal and external factor for firms to measure.
4.0 FINDINGS AND ANALYSIS

4.1 Introduction
The main reason for finding and analysis for investigate and identify the trend of the McDonald's for the five years by computing the ratios. There has important component in the finding and analysis which is financial statement, income statement, balance sheet and cash flow statement. These components allow the researcher to identify the descriptive analysis, correlation, coefficient and residual statistics.

4.2 Descriptive Statistics

<table>
<thead>
<tr>
<th>Descriptive Statistics</th>
<th>Mean</th>
<th>Std. Deviation</th>
<th>N</th>
</tr>
</thead>
<tbody>
<tr>
<td>ROA</td>
<td>.148680</td>
<td>.0223467</td>
<td>5</td>
</tr>
<tr>
<td>CURRENT RATIO</td>
<td>1.879120</td>
<td>.7993502</td>
<td>5</td>
</tr>
<tr>
<td>QUICK RATIO</td>
<td>1.853400</td>
<td>.7946618</td>
<td>5</td>
</tr>
<tr>
<td>AVERAGE-COLLECTION PERIOD</td>
<td>25.772280</td>
<td>10.6682009</td>
<td>5</td>
</tr>
<tr>
<td>DEBT TO INCOME</td>
<td>.092860</td>
<td>.0111995</td>
<td>5</td>
</tr>
<tr>
<td>OPERATIONAL RATIO</td>
<td>1.109200</td>
<td>.0665556</td>
<td>5</td>
</tr>
<tr>
<td>OPERATING MARGIN</td>
<td>.344360</td>
<td>.0675939</td>
<td>5</td>
</tr>
<tr>
<td>GDP</td>
<td>2.420000000000000</td>
<td>.544977063737548</td>
<td>5</td>
</tr>
<tr>
<td>Inflation</td>
<td>1.500</td>
<td>.8916</td>
<td>5</td>
</tr>
<tr>
<td>InterestRate</td>
<td>2.0300</td>
<td>.43243</td>
<td>5</td>
</tr>
<tr>
<td>ExchangeRate</td>
<td>1.1360</td>
<td>.06877</td>
<td>5</td>
</tr>
<tr>
<td>STDV</td>
<td>1.451880091477797</td>
<td>.490694480983325</td>
<td>5</td>
</tr>
<tr>
<td>CGI</td>
<td>.640</td>
<td>.0894</td>
<td>5</td>
</tr>
</tbody>
</table>

Table 4.1 Descriptive Statistics for McDonald’s

Based on McDonald’s descriptive statistics are summary descriptive coefficients that summarize a given data set, which can be a representative of an entire population. Descriptive statistics are broken down into measures of concentration trends and variability (propagation). The corporate governance index for McDonald’s is 0.640 and the standard deviation is 0.0894.
### 4.3 Correlations

#### Table 4.3 Table of Pearson correlation

The correlation coefficient is a statistical measure of the change in the prediction of the change in the value of one variable to the value of another variable. In a positive correlation variable, the value increases or decreases in series. In a negative correlation variable, one value increases as the other value decreases.

<table>
<thead>
<tr>
<th></th>
<th>ROA</th>
<th>CURRENT RATIO</th>
<th>QUICK RATIO</th>
<th>AVERAGE COLLECTION PERIOD</th>
<th>DEBT TO INCOME</th>
<th>OPERATIONAL RATIO</th>
<th>OPERATING MARGIN</th>
<th>GDP</th>
<th>Inflation</th>
<th>InterestRate</th>
<th>ExchangeRate</th>
<th>STDV</th>
<th>CGI</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pearson Correlation</td>
<td>0.064</td>
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<tr>
<td>CURRENT RATIO</td>
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<td>QUICK RATIO</td>
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<tr>
<td>AVERAGE COLLECTION</td>
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<td>PERIOD</td>
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<td>DEBT TO INCOME</td>
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<td>OPERATIONAL RATIO</td>
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<td>OPERATING MARGIN</td>
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<td>GDP</td>
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<td>Inflation</td>
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<td>STDV</td>
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<td>CGI</td>
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</tbody>
</table>

Note: *p < 0.10, **p < 0.05, ***p < 0.001
The Pearson correlation is used to identify the relationship between dependent variables (Corporate Governance Index) and independent variable (Firm’s internal and external factor). The table below is used as benchmark to identify the relationship between variables:

<table>
<thead>
<tr>
<th>Size of correlation</th>
<th>Interpretation</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.90 to 1.00 (-0.90 to -1.00)</td>
<td>Very high positive (negative) correlation</td>
</tr>
<tr>
<td>0.70 to 0.90 (-0.70 to -0.90)</td>
<td>High positive (negative) correlation</td>
</tr>
<tr>
<td>0.50 to 0.70 (-0.50 to -0.70)</td>
<td>Moderate positive (negative) correlation</td>
</tr>
<tr>
<td>0.30 to 0.50 (-0.30 to -0.50)</td>
<td>Low positive (negative) correlation</td>
</tr>
<tr>
<td>0.00 to 0.30 (0.00 to -0.30)</td>
<td>Negligible correlation</td>
</tr>
</tbody>
</table>

From the table acquired by SPSS, we know that ROA had a very high positive correlation which was 1. ROA obtained a very high positive (negative) correlation which was 1 while inflation rate obtained negligible correlation which was 0.892 respectively.

### 4.4 Coefficients

According to the coefficients table shows that independent variable (inflation rate) has most influence on the GDP. The level of 5% with p-value is identification of significant that influence on the GDP. Moreover, dependent variable is most influence by the independent variables if p-value < 0.001. The p-value < 0.10 has the least influence while the p-value < 0.05 shows that medium influence of independent variable on the dependent variable. Furthermore, according to the table above the inflation rate is moderately positively significant that influence the Gross Domestic Product (GDP) with p-value < 0.05, \( t = 3.422 \).
4.5 Residuals Statistics

From the graph and table above, it shows that the points generally follow the normal (diagonal) line with no strong deviations. This indicates that the residuals are normally distributed.

4.6 Model Summary

<table>
<thead>
<tr>
<th>Model</th>
<th>R</th>
<th>R Square</th>
<th>Adjusted R Square</th>
<th>Std. Error of the Estimate</th>
<th>Durbin-Watson</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>.892a</td>
<td>.796</td>
<td>.728</td>
<td>.0116529</td>
<td>2.131</td>
</tr>
</tbody>
</table>

a. Predictors: (Constant), Inflation
b. Dependent Variable: ROA

Table 4.6 Model Summary Result
The model summary result table above shows that the adjusted R square is to 72.8% it implies by using the internal and external variable which is inflation rate. The McDonald’s company has 72.8% of the variance that show in model summary table. This shows that the variable used in the model able to explain 72.8% variance in GDP. Moreover, the remaining 27.2% of the adjusted R square is remain unknown that is unable to explain by the both internal and external variables. Furthermore, the ANOVA table above determinant the significant value of 0.042 which is more than the alpha value (p < 0.05). Its shows that the variable not perfectly significant to the represent model. However, the significant value above is not acceptable value because the model of the study is not acceptable and not reliable.

Table 4.6 ANOVA Result

<table>
<thead>
<tr>
<th>Model</th>
<th>Sum of Squares</th>
<th>df</th>
<th>Mean Square</th>
<th>F</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Regression</td>
<td>.002</td>
<td>1</td>
<td>.002</td>
<td>11.710</td>
</tr>
<tr>
<td></td>
<td>Residual</td>
<td>.000</td>
<td>3</td>
<td>.000</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td>.002</td>
<td>4</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

a. Dependent Variable: ROA  
b. Predictors: (Constant), Inflation
5.0 DISCUSSION AND CONCLUSION

5.1 Introduction
This study purposely projected to determine the firm’s scandal and its determinants of McDonald’s company for five years from 2014 until 2018. Furthermore, to achieve this research objective the McDonald’s company specific factors (GDP) and internal and external factors (inflation rate) were used in this research. In this chapter five conduct the discussion of result and recommendations.

5.2 Discussion of result
The aim of this research to investigate and identify the firm’s scandal and its determinants among the five years in McDonald’s company. This research is done to achieve the study objective as below:

1. To identify the internal factors of McDonald’s affect dependent variable.
2. To identify the external factors of McDonald’s affect dependent variable.
3. To investigate how internal and external factors are affecting the dependent variable.

According to the of both correlation table 4.2 and 4.3 determine that GDP has been influenced and effected by the internal and external factors. The correlation table indicate that unemployment is moderately positive and moderately significant correlated to the GDP with the value p < 0.05. Its shows that if any change or rise the GDP also might affect.

In additional, in the model summary (table 4.5) shows that 72.8% of the model is explained by the variables from the firm’s internal and external factor. The ANOVA table shows that a significant of 0.042 it’s indicated that the model is not reliable. Moreover, the firm’s internal and external factor has more impact toward the firm which will affect the GDP heavily. Furthermore, in other hand the firm’s specific factors do not impact much on the McDonald’s company.

5.3 Limitations
The limitations of this research are the five years McDonald’s company from 2014 to 2018. In this research, the annual report performs only for five years financial statements. In addition, due to the time constraint, the limited amount of information can be collected.
5.4 Recommendations
Lastly, based on the inflation rate finding and analysis has a moderate significant relationship with GDP. So, McDonald’s company should take primary action to reduce or avoid the company’s risk. McDonald’s company should practice efficiently managing assets and equity to increase the profit of the company. Inflation rate is a counting of how much people or worker working in a working area. The inflation rate effects the sustainability of McDonald’s company. To overcome or avoid this the government should implement some policies or strategies to make sure that the inflation rate is still under control and doesn’t affect any sector. For example, the government can help the unemployed with providing some capital to start their own business.
REFERENCES


