Tim Hortons vs Canadian Tire: Which Should You Buy?

Description

Even though they sell completely different products, **Tim Hortons** (TSX: THI)(NYSE: THI) and **Canadian Tire** (TSX: CTC.A) have a lot in common.

Both companies have very strong brands in Canada, and try to appeal to Canadians' sense of national pride as they compete against larger American competitors. Both are facing saturation issues in Canada, but at the same time have struggled with expansions into the United States — only Tim Hortons remains there. Both are pushing ahead with technology improvements in an effort not to be left behind. And finally, both are fairly recession-resistant, offering products that people will buy even when times are tough.

So which stock is the better option at this point? Below we take a closer look at each company.

Tim Hortons

There are perhaps no franchises in Canada as strong as Tim Hortons. The company has the top-rated brand in the entire country and a dominant market share. Profitability is high; over the past 12 months, return on equity was over 43%.

But Tims faces a very familiar problem: few growth opportunities and growing competition in Canada. The company is countering by trying to expand its afternoon share, introducing new menu items, and growing store locations where it can (such as in the United States). Overall, Tim Hortons still plans to grow earnings per share by 11% to 13% from 2015 to 2018.

At over 21 times earnings, Tims is very richly priced, but that's what you have to pay if you want a franchise of this quality. You shouldn't expect to hit any home runs by investing in this stock.

Canadian Tire

It’s amazing how similar the situation is for Canadian Tire. The number of flagship locations has barely budged in the past decade, evident of the fact that there isn’t much room for store growth. And competition from companies like **Walmart** is intensifying.

Canadian Tire does have one leg up on Tims, and that is its other stores. The Mark’s banner is performing well, and Tire is aggressively expanding its presence in sports, mainly through its Sportchek banner. On the other hand, Tire isn’t as profitable, partly because its franchisees hold much more bargaining power than Tim Hortons’ franchisees do.

The numbers are not entirely comparable, because Tire also owns a large financial services business as well as its own REIT. But return on equity is only 11%, about in line with its five-year average. On the bright side though, Tire trades at less than 16 times earnings.

A familiar trade-off

These two companies have a number of things in common. So when deciding which to buy, there’s a simple trade-off between quality and value. On the quality side, Tim Hortons is very profitable, has a great brand, and a fantastic track record. On the other, Tire is cheaper and still has significant growth opportunities in Canada.

At the end of the day, deciding which one to own is a matter of personal preference and comfort level. You shouldn’t rule out owning both — or avoiding the two altogether.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:CTC.A (Canadian Tire Corporation, Limited)

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