



Forget Restaurant Brands International Inc.! Buy a More Attractive Peer Instead

Description

Restaurant Brands International Inc. ([TSX:QSR](#))([NYSE:QSR](#)) shares appreciated north of 6%, and **Popeyes Louisiana Kitchen Inc.** (NASDAQ:PLKI) appreciated north of 19% on Tuesday.

While lots of attention has gone to Restaurant Brands's acquisition of Popeyes Louisiana Kitchen, **Cara Operations Ltd.** (TSX:CARA), none other than our very own "Canadian Restaurant Brands," has fallen under the radar.

Cara is a profitable business with growth potential.

The business

Cara is Canada's oldest and largest full-service restaurant company. It grows by acquisitions and franchising its operations.

You'll recognize its brands, including Swiss Chalet, Harvey's, St-Hubert, Milestones, Montana's, Kelsey's, East Side Mario's, Casey's, New York Fries, Prime Pubs, Bier Markt, Original Joe's, Elephant and Castle, State & Main, and Landing.

At the end of September 2016, Cara had 1,127 restaurants, of which 1,080 were located in Canada and 47 were located internationally. Cara has 88% of its restaurants operated by franchisees.

For the trailing 12-month (TTM) period, Cara generated sales of \$372 million and net income of \$106 million, which led to earnings per share of \$2.09. As well, its operating margin was north of 24% and its return on equity (ROE) was north of 30%.

dining, salmon

Healthy economy in Ontario will benefit Cara

You can find Cara's restaurants across Canada. It has a strong focus in Ontario with about 59% of its locations there. So, strong economic growth in Ontario will encourage more Ontarians to eat out and

likely boost Cara's sales.

On Tuesday, the province of Ontario released news that the province's economic growth is outpacing the G7 countries.

Comparing Restaurant Brands and Cara

Restaurant Brands has a much bigger scale than Cara. Restaurant Brands is a global quick-service restaurant which combines the two iconic brands of Burger King and Tim Hortons, totaling more than 20,000 restaurants.

There are more than 15,000 Burger King locations in more than 100 countries. Nearly 100% of Burger King restaurants are owned and operated by franchisees.

Now, Popeyes, a different kind of quick-service restaurant with chicken concepts and more than 2,600 restaurants in 26 countries, is joining Restaurant Brands.

Restaurant Brands grows at a high rate. However, it also has a higher financial leverage than Cara.

For the TTM period, Restaurant Brands generated sales of more than US\$4.1 billion and net income of US\$616 million, which led to earnings per share of US\$1.45. As well, its operating margin was north of 40% and its ROE was north of 22%.

Although Cara only operates in Canada, it's more conservatively run. Last year it was affected by its operations in Alberta. However, it's expected to grow its earnings per share at a double-digit rate for the next two years.

At \$25.50 per share, Cara trades at a multiple of about 18.4, while, with the spike on Tuesday, Restaurant Brands trades at a high multiple of about 35.9.

Due to Cara's lower valuation and similar growth prospects in the next two years, it is a more attractive investment.

Investor takeaway

Conservative investors looking for growth in the restaurant space should consider Cara, which has a strong balance sheet and trades at an attractive multiple for its growth potential.

The shares also offer a dividend which is supported by a payout ratio of about 30%. Based on the current quarterly payout, the shares offer a safe yield of nearly 1.6%.

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Date

2025/08/14

Date Created

2017/02/24

Author

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