1 Relatively Unknown Earnings-Growth Superstar to Buy Now

Description

If you're a growth investor looking for the next five-bagger, then you're probably speculating on small-cap stocks that have questionable fundamentals. I'm a long-term investor, not a speculator, but I'm always on the hunt for the next big growth stock. In some cases, you don't need to take a huge amount of risk to find the next big thing. There are small-cap stocks that have histories of improving fundamentals, and investors may be overlooking these hidden gems.

The markets are overheated right now, and many investors may be fearful of the next market crash. After all, we are in the late stages of a bull market, and it's very hard to find value on the TSX or the American exchanges. But if you're willing to dig a bit deeper to find such hidden gems, you're likely to discover the next big thing.

MTY Food Group Inc. (TSX:MTY) is a Canadian franchisor in the quick-serve restaurant industry with about 48% of its locations in the U.S. and about 43% in Canada. The company operates under 48 brands that are primarily located in food courts in shopping malls, movie theatres, train stations, or even convenience stores.

If you're a Canadian, then odds are that you've eaten at one of MTY's food court restaurants without even knowing it. Here are just a few brands under the MTY umbrella: Vanelli's, Thaï Express, Jugo Juice, Extreme Pita, Sushi Shop, Manchu Wok, Veggirama, Koya Japan, Taco Time, Mr.Sub, and Yogen Früz.

A quick glance at the fundamentals

MTY has seen earnings and gross margins improve by considerable amounts over the last five years. The company also has a solid dividend which has been growing since it was first issued, and given the recent earnings-growth rate, I believe the company could be the next big dividend-growth king.

With an impressive ROE above 20%, it's apparent that the management team knows how to make the most out of its investment initiatives. The company has been growing through acquisitions, but it has taken on considerable debt doing so.

Last year, MTY announced the friendly takeover of Kahala Brands, which would add approximately 2,800 stores across the world. The deal cost about US$310 million, but it will be a huge driver of free cash flow for many years to come. With the U.S. exposure, MTY is a terrific way to play a strengthening U.S. economy under President Trump.

Potential risks

MTY is a very scalable platform which offers long-term investors earnings-growth potential. However, I would be cautious, as the company has quite the debt load. I don't believe the debt will be a problem, but it's likely that more acquisitions will be on hold while debt repayment becomes a higher priority.

There are also pundits that believe that the "death of the shopping mall" is imminent. I do not believe this is the case, but if mall traffic goes down, MTY may start feeling the pressure since less mall traffic means less hungry customers at food courts. I believe the management team will be quick to adapt if the "death of the shopping mall" starts to make a dent in the company's sales.

Valuation

MTY trades at a reasonable 17.85 price-to-earnings multiple and a 3.2 price-to-book multiple, both of which are lower than the company's five-year historical average multiples of 22.9 and 4.3, respectively. The stock is now over 11% down from its highs, so I think the stock is attractively valued given the promising growth prospects.

If you're not afraid of the death of the shopping mall, then now could be the time to load up. If you're not sure, then you might want to buy small chunks as on any further dips that present themselves over the next few months.

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joefrenette