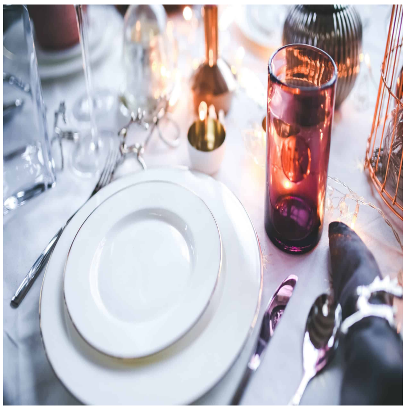

1 Headwind That Could Stop Cara Operations Ltd. in its Tracks

Description

Cara Operations Ltd. (TSX:CARA) is a the company behind famous Canadian dine-in restaurant brands such as Swiss Chalet, Milestones, and St-Hubert. Cara has a strong presence in Ontario, so an investment in Cara is a great play on the increase in consumer spending that is expected with a strengthening economy. Unlike Canadian provinces like Alberta, Ontario is poised to see strong economic growth over the next few years, and that's a huge plus for Cara, but there is one major issue that could send Cara to new lows: the rise of restaurant food-delivery services.

Most of Cara's brands are casual dine-in restaurants. These are the restaurants that require guests be seated and served by staff on site. A gratuity is also expected afterward, but with the rise of food-delivery services, the whole sit-down-and-eat model will most likely take a big hit as the general public becomes more accustomed to having food from their favourite restaurant delivered to their doorsteps.

Can't Cara's dine-in restaurants deliver? What's the big deal?

Sure, dine-in restaurants could deliver, but sales are still likely to take a hit because dine-in restaurants are quite behind when it comes to the logistics of food delivery. It's not an easy task, and to have such a service in place requires a hefty investment just to keep up with competitors.

Even if Cara's brands had a delivery platform in place, guests probably wouldn't make impulsive orders from home like they would if they were seated in a restaurant. That means orders of alcohol, appetizers, dessert probably won't be common. Alcohol in particular is a high-margin product, and a sharp reduction in the sale of this product will be a major thorn in any dine-in-business's side.

What about all that real estate not being put to good use?

Cara's brands are located in consumer-dense locations around Canada, and if the "stay at home" trend picks up, the real estate won't be put to good use. What's the point of having brick-and-mortar dining locations if consumers are just going to opt for home delivery?

It’s not unreasonable to speculate that some of Cara’s restaurant locations may be shut down if restaurant traffic decreases by an alarming amount due to the rise of the “stay at home” trend.

Bottom line

The rise in restaurant delivery is a gigantic negative for dine-in restaurants like Cara, and I’m not sure how management will respond over the next few years.

Sure, Cara owns some fantastic Canadian brands, but this won’t matter because I believe the headwinds are serious and major adaptations are going to need to happen to stop Cara from falling farther into the abyss.

The stock currently trades at a reasonable 14.24 price-to-earnings multiple, which is very cheap, but I believe there’s too much uncertainty in regards to the fate of dine-in restaurants over the next few years. For this reason, I’d recommend trimming your position and sticking to the sidelines for now.

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