Think Restaurant Brands International Inc. Needs to Do More? Short its Stock

Description

The debate in the media appears to be heating up, with pro-business advocates arguing the recent Ontario minimum wage hike unfairly put franchisees of **Restaurant Brands International Inc.'s** (TSX:QSR)(NYSE:QSR) subsidiary Tim Hortons in a terrible position, with little left to do but cut costs and trim employee hours and benefits given the competitive cost-centric doughnut-and-coffee industry.

Pro-labour aficionados often rely on views similar to those highlighted in a recent piece by fellow Fool contributor Will Ashworth: employees are the ones being wronged here by Restaurant Brands. Mr. Ashworth's call for a boycott on the stock of Restaurant Brands takes the view that the parent company should be more active in this process, has the ability to do more, and is not doing enough to help its employees or franchisees currently.

Here are a bunch of reasons why I believe the "boycott Tim Hortons" campaign should be unequivocally ignored by investors:

Economics of the industry make it difficult to raise prices

While I have no way of knowing if Mr. Ashworth is actually short the stock, I can say that I completely disagree with his view that the parent company needs to raise prices based on the unique fundamental economics of the doughnut-and-coffee business Tim Hortons operates in. Tim Hortons does not operate in a vacuum, and is not the only option for Canadians in cities of any size.

Rivals have continued to scoop up market share, and while Tim Hortons has done a great job of growing in Canada and worldwide, the competitive race for market share from competitors such as **McDonald's Corporation** in urban centres is rough, and Tim Hortons has made it clear it is willing to compete on price in most markets.

Price matters for Tim Hortons customers

Tim Hortons's competitive advantage is not only that it's available for nearly every Canadian,supporting communities that may not otherwise have a coffee shop due to population size or density,but also that it will make coffee accessible and affordable for everyday Canadians — a noteworthy goal.

Tim Hortons competes with McDonald's in the coffee space, as opposed to competing with **Starbucks Corporation**. While many Canadians may prefer a cup of coffee from Starbucks over Tim Hortons (myself included), the long lines at Tim Hortons at universities across the country or in rural Canadian communities depend on the low prices set by Restaurant Brands's head office; after all, McDonald's makes a mean cup of coffee these days at very competitive prices.

Size matters

Mr. Ashworth's assertion that I am minimizing the impact of Tim Hortons on Restaurant Brands's bottom line is completely off base; if anything, I greatly overstated the impact of Ontario Tim Horton's locations in my previous article.

Let's do the math.

Based on estimates of one Tim Hortons per 8,000 Ontario residents, there should be approximately 1,700 Tim Hortons locations in Ontario. Assuming all locations are affected by this minimum wage increase, then out of approximately 3,800 Canadian locations, Ontario would represent a market share of approximately 45%. Given another 836 locations worldwide, the market share number drops to 36.7%.

If 10% of customers stop going to Tim Hortons based on the boycott (a ridiculously high number, but let's just assume), and multiplying this by the total impact Tim Hortons has on Restaurant Brand's overall bottom line (2016 annual system-wide sales total of $6.4 billion out of $24.6 billion, as of the company's most recent annual report), we get a total bottom line impact of 0.95%. Adding in the Popeyes Louisiana Kitchen acquisition in 2017 would make the numbers look far worse.

In other words, the impact of 10% of Ontario customers boycotting all Ontario Tim Hortons locations simultaneously for an entire year would have an impact of less than 1% on the company's top and bottom lines, yet Restaurant Brands's share price has dropped by nearly 10% since the end of November.

It seems like a Restaurant Brands stock is on sale for growth investors right now.

Bottom line

I would invite any investor wishing to boycott Restaurant Brands stock to go one step further and short the stock, if one believes that select Ontario Tim Hortons franchises will have any sort of impact on the company's bottom line.

Avoiding the stock because of this minimum wage debate is a downright silly idea given the company's exposure to this scandal and its fundamentals compared to its peers. Arguing that Restaurant Brandsis expensive, which I have done in the past, is very different than believing this debate has the ability to affect Restaurant Brands's long-term fundamentals and therefore its stock price in the near, mid, or long term.

Stay Foolish, my friends.

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