Why Expansion Into China Is a Big Risk for Tim Hortons

Description

Restaurant Brands International (TSX:QSR)(NYSE:QSR) struggled to find any growth last year, as its stock was down more than 1%. Investors simply weren't excited with the company's results — in particular, with Tim Hortons. The popular coffee chain has fallen out of favour with Canadians in recent years, and that's a big problem.

In recent quarters, Restaurant Brands has seen Tim Hortons consistently generate growth of less than 3%. In its most recent quarter, the coffee shop's sales were up 2.8%, and that was up from 2.2% in the previous quarter and 2.1% from the period prior to that. What's alarming about those number is that they are system-wide sales, and same-store sales numbers are even worse.

Same-store sales growth looks at the growth achieved in stores that were in operation the previous year, whereas system-wide sales look at total sales numbers, which will benefit from an increase in locations. If we look at same-store growth, Tim Hortons achieved just 0.6% last quarter, no growth in the prior period, and -0.3% the period before that.

Growth is clearly an issue for Tim Hortons, as it continues to lag behind Burger King and Popeyes, the other two chains in Restaurant Brands's portfolio. It's keeping the stock from rising and achieving stronger sales numbers.

Focus is on global expansion

In recent years, Tim Hortons has been eyeing markets outside Canada to expand into, and rightfully so. After all, with a saturated home market, it's inevitable that the coffee chain would need to look beyond its immediate borders for more significant growth opportunities.

Previously, we heard of the company looking to expand into Spain. However, its biggest foray may be into China, where it expects to add 1,500 locations over the next decade. Many North American companies have been successful in expanding into the Far East, and it's something Tim Hortons hopes can stimulate some much-needed growth. Many Chinese consumers are familiar with the Tim Hortons brand in Canada, and the brand recognition will likely give it a good head start once it launches its first store.

The company hopes to start building stores in China soon, although it's unclear when we might see the first store open for business.

Is Restaurant Brands being too aggressive?

In a world where sales growth is vital to attracting investors, it's not hard to understand why Restaurant Brands is looking to fix its Tim Hortons problem. The concern, however, is whether a company with over $12 billion in long-term debt is taking on more than it can chew. Expanding into many different locations could prove to be too big of a risk for the company. After all, it has a massive U.S. market available to it south of the border that is still largely untapped.

While Tim Hortons has expanded into the U.S., it hasn’t gone all that well. And if it has trouble in the U.S., it might be a bit premature to focus on other markets.

Bottom line

I don’t like the idea of Tim Hortons expanding so much so quickly, particularly with a big market nearby. Although the move might pay off in the end, the stock is still a big risk today.

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