This Tasty TSX Stock Is a Great Buy Now

Description

MTY Food Group (TSX:MTY) was nothing short of amazing, as it drove total returns of more than 20% *per year* from 2010 to 2019.

Due to COVID-19 impacts, the tasty TSX stock fell as much as 66% from $60 per share to as low as $20 in March.

Now that the stock price seems to have somewhat stabilized, it's good time to start a position.

The business

MTY Food Group franchises and operates quick-service and casual-dining restaurants across a long list of brands, including original concepts and many that it acquired over the last two decades.

To give you a taste of MTY's offerings, here are some of its banners: Big Smoke Burger, Jugo Juice, Kimchi, Koya Japan, Manchu Wok, Tandori, Taco Time, etc.

At the end of fiscal Q1, MTY Food Group had 7,300 locations, of which 137 were corporate, 7,140 were franchised, and 23 were in joint ventures. Many of its locations are in malls and office towers.

MTY's recent results

MTY's fiscal first-quarter results were good. During the specific period of December to February, it experienced system sales growth of 45% to $999.5 million and revenue growth of 41% to $150.8 million against the same period in the prior year.

The growth was largely attributable to contributions from acquisitions. MTY also experienced organic growth in system sales of $11.4 million during the quarter.

MTY's Q1 EBITDA margin expanded by 80 basis points to 27.2%, leading to a boost of 45% in its EBITDA to $41 million. Free cash flow also climbed 23% to $30.7 million. Earnings per share increased by 31% to $0.76.

Same-store sales climbed by 2.1%. Specifically, Canadian same-store sales were up 1.6%, making it the 10th consecutive quarter of positive growth. Same-store sales in the United States increased by 4.3% and international locations experienced a decline of 5.7%. Notably, MTY's geographical split is 54% in the United States, 39% in Canada, and 7% international.

COVID-19 impacts on MTY Food Group

MTY expects COVID-19 impacts to last for about two to three quarters, which means there could be better buying opportunities over the next six to nine months or so to accumulate shares.

Management took steps to reduce costs and expects the business to be close to cash flow neutral in fiscal Q3 (the June to August period).

The near-term focus of MTY is the reopening of its closed locations. The long-term focus for customer value creation, after the pandemic, will be on innovation, food quality, and customer service.

At the current juncture, the stock is a turnaround play. Investing in the stock today suggests that you're in the camp that believes people will still go to malls and work at office towers after the pandemic.

It's impossible to determine the change (if any) in consumer behaviour after the pandemic. And this is the risk that investors are taking by investing in the stock today.

Valuation

MTY's earnings are expected to recover to about 76% of pre-COVID-19 levels by next year. Assuming a reasonable forward price-to-earnings ratio of 15, that'd imply a fair price of about $37. This suggests 38% near-term upside.

For now, there's too much uncertainty. Therefore, I didn't add any returns from a dividend. However, I expect some sort of dividend to be declared in the future when the macro environment improves.

The Foolish takeaway

MTY stock is riskier than it was pre-COVID-19. However, it's also trading at a fraction (roughly 45%) of where it was then. Therefore, the tasty stock will likely deliver outsized returns over the next one to two years. That said, it's too early to tell if consumer behaviour will change in light of the pandemic.

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