Fast Food Stocks Could Pass Food Inflation to Consumers

Description

The global economy is well on its way to a deep recession. That's if it isn't already there yet. Interest rates have surged enough to curb economic activity. Meanwhile, consumers are squeezed by high inflation so spending is down. All considered, economic growth should be negative in many parts of the world next year.

Investing during a recession is tricky. Many seemingly undervalued businesses go under. While growth stocks tend to be more volatile in such an environment. Investors looking for safety need to turn their attention to resilient sectors such as energy and utilities.

I believe fast food retail is another recession-resistant sector. Here's a closer look at my thesis.

Recession-resistant

The convenience and cost-effectiveness of fast food is particularly appealing when consumers are financially stressed. The rising price of food is a key driver of inflation. Consumers see this in their local grocery stores. However, prices are even more magnified at casual and fine-dining restaurants. These establishments have to price in labour, commercial rent, and utilities on every bill.

Another concern is tip inflation. The average tip in Canada has surged from 15%-20% to 20%-25% in recent years.

That's why consumer demand is shifting to fast food chains. The most famous fast food chains have reported strong earnings throughout 2022. I expect this trend to continue for the next few years as consumers grapple with the loss of purchasing power.

Canada's top fast food stocks

Restaurant Brands International Inc. (TSX:QSR) and **Pizza Pizza Ltd.** (TSX:PZA) are top picks in this sector.

In the third quarter of 2022, RBI reported 14% growth in revenue year over year. Digital sales were up 26% over the past year. Every brand under the RBI umbrella, including Burger King, Tim Hortons, and Popeye's reported net growth in sales. The company also expanded its dividend payout and committed to lowering its debt burden with the excess cash flow.

Meanwhile, Pizza Pizza saw its royalty pool expand by 15.4% in this recent quarter. The management team has raised the dividend payout by 3.7%. At the moment, the stock offers a lucrative 6.25% yield. That looks as tempting as the brand's flagship pizzas!

While other sectors of the economy are pulling back, fast-food chains are deploying even more cash for expansion. Pizza Pizza opened six new locations this year. Restaurant Brands wants to expand its network from 28,000 to 40,000 over the next 8 to 10 years. That's a clear sign of the resilience of this undervalued sector despite economic headwinds.

Bottom line

It's difficult to invest during rampant inflation and a declining economy. However, some sectors of the economy offer a reprieve to both consumers and investors. Low-cost fast food chains are one such sector. Investors looking for durable dividends should add high-quality fast food stocks to their watch list in 2023 and beyond.

CATEGORY

1. Investing

TICKERS GLOBAL

1. NYSE:QSR (Restaurant Brands International Inc.)
2. TSX:PZA (Pizza Pizza Royalty Corp.)
3. TSX:QSR (Restaurant Brands International Inc.)

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Date
2025/06/30
Date Created
2022/11/30
Author
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