Corus Entertainment Inc.: The Market Is Over-Reacting on Both Ends of the Spectrum

Description

In a number of recent articles, I've touched on what I believe to be a serious over-reaction by the market for companies operating in growth industries or with higher-than average top-line growth rates. Industries that post sky-high revenue numbers with a lack of profitability have absolutely stolen the limelight from companies that may have declining revenues, but improving bottom line or cash flow numbers.

According to the laws of finance, at the end of the day, a company should be worth the sum of its discounted future cash flows, not its discounted future revenues. Sure, revenues indicate strength in building market share and traction within a niche. However, if a company is never able to translate its market share into true profitability, then investors need to ask whether paying for revenue growth is a prudent idea over the long term.

Corus Entertainment Inc. (TSX:CJR.B) is a small Canadian entertainment and media company that has plummeted on what can only be called a dismal earnings report. On Wednesday, shares of Corus were down approximately 17% following its earnings release, which was well-covered by fellow Fool analyst Joseph Solitro.

Foolish readers will note that by every fundamental metric, Corus decreased year-over-year except for cash flow generation. The company more than tripled its operating cash flow and more than doubled its free cash flow generation, executing on its promise to shareholders that the company will continue to improve cash flow numbers.

In the company's Q1 earnings call presentation, free cash flow generation was once again in focus for 2018 as the company works to continue to reduce its debt load down to 3.0 times net debt to segment profit and works to maintain its dividend. While Corus' dividend payout ratio remains high, concerns that a dividend cut will take place should be reduced, at least for the current fiscal year.

While it's true that Corus is operating in a declining sector, the fact that the company's management team has improved cash flow generation is a key indicator that the underlying business model (content creation and development) could continue to be a viable asset over the long term. How Corus eventually chooses to integrate itself with streaming platforms is a discussion for another day. However, the “cable discount” the company is currently receiving may provide an attractive entry point for investors considering a deep value play with a very high dividend yield of more than 12.4% as of Wednesday close.

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