Corus Entertainment Inc. (TSX:CJR.B): A Dividend Cut Is Imminent

Description

Are you a **Corus Entertainment Inc.** (TSX:CJR.B) shareholder? I feel for you. The company has been in a downward spiral for years. Corus has not posted positive share growth since 2014, and regardless when you bought over the past 20 years, you'd be in the red.

Its two-year return is negative 50%, and its performance year to date is not much better as its share price has lost 44%. Ouch.

Investors who are holding on are doing so for one reason: the dividend. Thanks to its rapid decline, the company now yields a whopping 17.7%! This type of yield is unheard of. It is also not sustainable.

I have no doubt that a dividend cut is imminent. When that happens, what then?

A positive event

Believe it or not, a dividend cut is actually a good thing. Paying out a 17.7% dividend is bad financial policy. At the moment, Corus's payout ratio is 110% of earnings.

Bulls will point to the company's strong cash flow. In 2017, the company's dividends accounted for 93% of free cash flow. True, it's enough to cover dividends, but it's still very high.

The problem with these high payout ratios is that the company is not re-investing in its operations. Corus operates in a very competitive industry that requires high levels of capital expenditures. The company needs to start investing earnings back in the company.

Without this re-investment, the company will continue to struggle.

There are plenty of examples where a dividend cut was viewed as a positive by the markets. This is especially true for companies with high levels of debt. Corus is highly indebted and has a debt-to-equity ratio of 77.45. Need I say more?

No other option

To improve its debt position, Corus has attempted to sell non-core assets. That’s easier said than done.

The company had a deal to sell two of its French-language specialty channels to Bell for $200 million. Unfortunately, the federal watchdog stepped in and blocked the deal on competition concerns.

A dividend cut is the company’s only option at the moment. The question then becomes, how much will it need to be cut? Expect a significant cut.

Barclays analyst Philip Huang expects Corus to slash its dividend in half. “Given our expectation of continued soft ad revenues and low visibility, we believe a dividend cut of greater than 50% would be prudent.”

It could be more. If Corus were to cut its dividend in half, it would still have a yield of approximately 9% based on today’s share price. That is still too high. A more reasonable yield to aim for would be approximately 5%. To get there, the company would need to cut dividends by approximately 70%.

Stay on the sidelines

Once Corus cuts its dividend, it can pay down debt and re-invest in the company. Until the company can reduce its debt and return to growth, investors should stay on the sidelines.

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