Cineplex Inc. (TSX:CGX): It's All About Bums in Seats

Description

The rumours of **Cineplex Inc.'s** (TSX:CGX) death were greatly exaggerated.

The beleaguered entertainment company reported record second-quarter results August 10 that included higher sales and earnings over last year.

"Cineplex reported record second quarter results including increases in revenue across all reportable segments," president and CEO Ellis Jacob said in a statement. "In addition to growing our revenue sources, we continue to focus on optimizing our cost structure across our ecosystem."

Many doubted whether Cineplex had the right stuff to right its ship, but the company's second quarter demonstrates that people will still go to the movies if the quality of content is there. In the second quarter, the higher quality of films led to 3.5 million more people taking in a movie in April, May, or June.

As I stated earlier this year, bad content kills.

If you don't have good movies for customers to watch, you're not going to have higher attendance numbers. The movie theatre business is all about getting bums in the seats. Good movies in the second quarter led to higher attendance which led to higher revenue and earnings. It's not an easy business, but it's a simple one.

"When the pictures are there, people come," Cineplex CEO Ellis Jacob said. "They love the theatrical experience. We like rain. But even with the great weather we've had, we've still done extremely well."

How good was the quarter?

Cineplex's adjusted EBITDA increased 78% in the second quarter to $67.8 million. More important, adjusted EBITDA margins increased by 610 basis points to 16.6%; as a result, its adjusted EBITDA margin for the for the first six months of the year increased by 230 basis points to 15.2%.

Cineplex's best year in terms of bottom-line profits over the past decade was 2012, when it generated $120 million, or close to double its profits in 2017. In the second quarter of 2012, Cineplex's adjusted EBITDA was $47.3 million; in this year's second quarter, it was 43% higher than in Q2 2012.

An outstanding performance, for sure. So, before you write off Cineplex stock, you might want to take a closer look at its business. It's not nearly as dead as some people might think.

But is it enough?

Ellis Jacob, Cineplex's CEO, has admitted in the past that diversifying the company's business beyond movie theatres is essential to its long-term success, as you're not always going to have home-run quarters like the one it just had.

That's why it has made investments in its media business, Rec Room, Playdium and Topgolf entertainment facilities along with its eSports gaming platform. In the second quarter, all of these non-theatre parts of its business experienced healthy year-over-year revenue gains of high single-digit to low single-digit growth.

Its non-theatre businesses now account for almost 25% of the company's overall sales, and although the Rec Room's $15.7 million in revenue in the second quarter wasn't quite as high as expected, the future for this concept still appears bright.

That said, the company continues to look at opportunities that allow it to utilize its entertainment operations experience beyond its own theatres and other entertainment facilities such as Rec Room.

My Foolish colleague Joey Frenette thought Cineplex stock was expensive in June, when it was trading at 31 times trailing earnings. I'm not sure what his thoughts are after the company's record results.

Personally, I would say that the company's stock isn't expensive if you plan to hold for the long haul, because if it's able to profitably grow non-theatre revenue to around 40% of overall sales within the next 2-3 years, $50 is going to seem very cheap.

But that's a big if.

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