Has a Cineplex Inc. (TSX:CGX) Turnaround Begun?

Description

The last week's strong price momentum has pushed **Cineplex** (TSX:CGX) stock higher by about 10%, and the stock is about 14% higher in the last month. It would seem the turnaround for Cineplex has begun. Has it really?

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Q2 results were not very meaningful

Cineplex reported its second-quarter results earlier this month with strong revenue growth to show. Specifically, compared to the same period in 2017, its revenue increased by about 12.4% to $409.1 million. This was obviously helped by attendance improvement of 5% and people generally spending more at the movies, either for the tickets or for the concession.

The profitability for the quarter was far too out of the world, with net income growth of 1671%, for example. If anything, this just showed that Q2 2017 was an especially bad quarter for the company.

Let's look at Cineplex's results for the first half of the year to see more smoothed out results.

Results for the first half of 2018

Compared to the same period in 2017, Cineplex's revenue increased by about 5.5% to $799.9 million.

Attendance declined 2.8%, but thankfully, Cineplex was able to get people to spend more on the movie tickets and for the concession.

Cineplex saw adjusted earnings before interest, taxes, depreciation, and amortization (EBITDA) increase by 24.5% to $121.4 million and adjusted EBITDA margin expand 2.3% to 15.2%. Its net income increased 62.7% to $39.6 million, which translated to diluted earnings per share growth of 61.5% to $0.63.

Is Cineplex's monthly dividend safe?

Some investors may be worried about the safety of Cineplex's dividend. Based on its earnings per share for the first half of the year, its payout ratio was about 135%. However, Cineplex's earnings have hardly ever covered for its dividend in the past. Yet, over the long term, Cineplex has increased its dividend at a pace that roughly matches inflation.

This phenomenon can only be explained by the entertainment company's free cash flow generation. In the first half of the year, its adjusted free cash flow increased 34.4% on a per-share basis to $1.298. Its payout ratio based on this free-cash-flow metric was under 66%, which more than covers for its monthly dividend.

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Has Cineplex's turnaround begun?

Cineplex's business performance is still largely dependent on people actually going to the movies, which in turn depends on what movies are showing. After all, box office revenue still makes up about 46% of the company's total revenue.

The stock has shown some strong upward action in the last two weeks. However, it has yet to make a higher high and higher low to indicate that it's really breaking out of the downtrend.

So, we can't say the company is turning around just yet.

Investor takeaway

Cineplex is still highly reliant on having entertaining movies to attract theatregoers, which doesn't sound particularly reassuring. However, the company has been investing elsewhere to diversify away from the movie business, and the stock is trading at the lowest valuation for the last six years. Therefore, investors looking for a turnaround story and an above-average dividend should take a closer look at Cineplex. It currently offers a yield of nearly 5.2%.

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