Cineplex (TSX:CGX) Takeover: Why it's a Great Deal!

Description

Cineplex (TSX:CGX) is one of Canada's largest entertainment organizations, with theatres and location-based entertainment venues in 10 provinces. It also operates businesses in digital commerce, cinema media, digital place-based media, and amusement solutions.

The company's share price closed at $24.01 on Friday December 13, 2019, before opening at $34.02 after the release of news regarding the takeover. Here is why I believe Cineplex shareholders got a good deal.

Intrinsic price

Based on my calculations using a discounted cash flow valuation model, I determined that Cineplex has an intrinsic value of $40.47 per share. Assuming less-than-average industry growth, the intrinsic value would be $37.67 per share, and higher-than-average industry growth would result in an intrinsic value of $43.74 per share.

At the pre-takeover share price of $24.01, I believe Cineplex is significantly undervalued. Investors who are holding Cineplex will receive a 42% premium to Friday's closing price. I believe this is a very good deal for shareholders, as the takeover offer is more than the halfway point between the last closing price and the intrinsic value. Thus, investors are theoretically deriving a greater advantage than the acquiring company, **Cineworld Group**.

Cineplex has an enterprise value of $3.157 billion, representing the theoretical price a buyer would pay for all of Cineplex's outstanding shares plus its debt. One of the things to note about Cineplex is its moderate leverage with debt at 28.1% of total capital versus equity at 71.9% of total capital.

Financial highlights

For the nine months ended September 30, 2019, the company reported a mediocre balance sheet with negative retained earnings of $239 million, down from negative $180 million in 2018. This is not ideal for investors, as it suggests the company has more years of cumulative net loss than net income.

Further, the company reports cash and equivalents of $30 million on short-term debt of $112 million. Given the presence of credit facilities this is not a material issue; however, I would like to see a company with this history have enough cash on hand to cover its short-term debt obligations.

Overall revenues are up year over year from $1.185 billion in 2018 to $1.222 billion in 2019 (+3%), driven by growth in the company's media and amusement divisions. Pre-tax income is strong at $41 million (although down from $67 million in 2018).

Cineplex is a dividend-paying entity with a dividend yield of 7.5% pre-takeover. The cash flow statement does not indicate repayments of long-term debt, which I would like to see more of since the company reports 28.1% of its total capital as debt.

If senior management can implement a strategy of debt reduction, Cineplex will undoubtedly deliver greater value to its shareholders, as less cash is being consumed by interest payments.

Foolish takeaway

Investors who'd bought shares of Cineplex prior to the takeover have received a very generous offer. With the scales tipping in the favour of investors, the $34 per share offer is a much higher premium to the $24.01 closing price than the discount from the company's intrinsic value of $40.47. Essentially, investors are getting a better deal than Cineworld.

I am not a fan of Cineplex's negative retained earnings and its increasing debt; however, this will not be a problem that shareholders need to worry about anymore. As online streaming services put pressure on traditional movie theatres, investors have the perfect opportunity to get out ahead.

CATEGORY

1. Investing

TICKERS GLOBAL

1. TSX:CGX (Cineplex Inc.)

PARTNER-FEEDS

1. Business Insider
2. Msn
3. Newscred
4. Sharewise
5. Yahoo CA

Category

1. Investing

Date
2025/08/25

Date Created
2019/12/17
Author
cliu