Cineplex (TSX:CGX) Stock: This Could Be a Generational Buying Opportunity

Description

I didn't think I'd ever be worried about **Cineplex** (TSX:CGX) stock again.

You probably remember the news late last year when the company agreed to be acquired by U.K.-based movie theatre operator **Cineworld**, a deal that valued Cineplex stock at $34 per share. The company negotiated a window where it had the option to solicit higher bids, but none came. The two companies have now made most of the moves needed for the deal to become official.

And then, disaster struck.

Markets around the world collapsed amid COVID-19 panic. Movie theatres have been especially hard hit, as governments ban public gatherings. Cineplex decided to take the proactive route and temporarily close all its theatres, rather than waiting for orders to do so.

The rapid deterioration of the movie theatre business combined with Cineworld's perilous balance sheet has put this deal into serious jeopardy. Remember, Cineworld agreed to pay $34 per share for Cineplex stock. These days, Cineplex shares trade hands at just $7.11 each. The market is sending a crystal clear message here — the deal just isn't going to happen.

This means that investors must evaluate Cineplex on its own. And there's potentially a very interesting situation here. Let's take a closer look.

The Cineplex stock opportunity

There's little doubt the next few months will be a trying time for the movie theatre business. Even as life slowly gets back to normal, cash-strapped consumers will be trying to cut back wherever possible — including trips to the movies.

Some might argue things look bleak for the business over the long term as well. Streaming services give folks access to thousands of different movies and television series without leaving their couch. Flush with cash, these streaming services are spending billions on content in hopes of staying ahead of competitors. Besides, a streaming service with many popular shows has an easier time attracting customers.

However, I still think there's room for both streaming services and movie theatres in the market today. After all, going to the movies is still an experience enjoyed by millions of people.

Pivoting back to Cineplex stock specifically, let's take a closer look at the numbers. In 2019, people went to the movies more than 66 million times at Cineplex's 165 locations across Canada, spending more than $1.6 billion on admission tickets and snacks. This is still a sizable business that will bounce back once people get over virus fears.

We must also remember this business generates significant free cash flow during good times. In 2019, Cineplex told investors it made $168 million in free cash flow. Cineplex stock, meanwhile, has a market cap today of just $450 million. That's quite cheap.

Cineplex is also expanding into other areas of the entertainment business. Its Rec Room concept now has seven locations, with more planned over the next few years. It has reinvented its Playdium brand. And the company has leveraged its expertise in digital media into a division that helps other companies with their branding.

Can we count on the dividend?

Many investors used to own Cineplex stock — myself included — for the company's succulent dividend . The payout has been temporarily suspended, while the acquisition is pending. Many will argue we've likely seen the last of Cineplex's high dividend. If the company reissues a dividend, it'll likely be a token payout at best.

Such a strategy is probably the company's best long-term move. Directing cash flow towards paying back debt will help reassure nervous investors.

The bottom line

I think there's significant upside potential in Cineplex stock today. Once the company gets through these trying times, shares could easily rebound 100% or even 200% higher over the short term and even more over the long term. Remember, this stock was at $55 per share just a couple of years ago.

Investors need to remember one thing — this isn't a risk-free opportunity. There's potential the stock falls even further, and bankruptcy isn't off the table if virus-related lockdowns last for months.

This looks like an interesting opportunity. Just don't put all your portfolio into it.

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