Why the Worst May Be Yet to Come for Cineplex (TSX:CGX) Stock

Description

The coronavirus pandemic's had a devastating impact on the economy. One of the hardest-hit companies is undoubtedly **Cineplex Inc** (TSX:CGX), which depends on foot traffic to its theatres. It's a business model that has limited ways of adapting if people stay indoors.

While movie theatres are starting to open up in Canada, with social distancing measures in place, they won't be operating anywhere near capacity even if the demand is there.

Shares of Cineplex have cratered in 2020, losing more than 75% of their value through the first six months of the year. And if you're thinking the stock is cheap and maybe you should buy it — don't. Shares of Cineplex could be headed even lower in the weeks and months ahead.

Here's why the stock is still a very risky buy.

Future quarters will be worse than Q1

Cineplex released its first-quarter results in June, when it reported a quarterly loss of $178.4 million. It's a steep loss and only the second one the company's reported in the past 10 quarters. The last one came a year ago and it was much more modest — a loss of just $7.4 million.

The last quarter ended March 31, which means that the results still included two full months where COVID-19 wasn't keeping people indoors.

The next quarter, which runs from April through to the end of June, will likely be much more catastrophic. Box office revenue in Q1 totalled $111 million, was down 29% from the prior-year period.

Investors can expect to see a much worse performance in the second quarter. The sad reality is that Q1 may end up being the company's strongest quarter of the current fiscal year when all is said and done.

Unsurprisingly, the stock fell 19% the day investors learned of the company's results.

Is the stock in danger of going bankrupt?

A very real question for investors is whether Cineplex can even make it through the pandemic. With limited money coming in and the company still having to pay rent for its facilities along with staff to help operate underused movie theatres, there may not be enough cash coming in to keep the lights on.

It's a perilous enough situation that on June 29, Cineplex amended an agreement with lenders so that its financial covenants could be suspended. The company reported that a total of $664 million is currently outstanding on its credit facilities.

It appears unlikely that Cineplex will be able to continue operating as it may simply run out of time waiting for the pandemic to end and for the economy to recover.

Even before the pandemic, Cineplex was generating small profit margins that typically weren't higher than 6%. There wasn't a lot of room for the company to handle any adversity to begin with, much less the one-two punch of a recession and pandemic that's crippled the business down to a skeleton of its former self.

Bottom line

Cineplex is in a lot of trouble. This isn't a stock that investors should be buying anytime soon. Unless the economy's able to get return to levels witnessed before the pandemic hit, there's no reason to gamble on Cineplex.

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