Cineplex (TSX:CGX) Stock: Is Bankruptcy Next?

Description

On Tuesday, **Cineplex** (TSX:CGX) released fiscal 2020 first quarter and year-end results. Unfortunately, it was an unmitigated disaster. On the day, the stock price lost 18.95% of its value to touch a 52-week low of $8.04 per share. Ouch.

Is the company redeemable? Let's take a deeper dive into the quarterly conference call to find out.

Failed acquisition

For months, the biggest unknown was the takeover by leading U.K. theatre chain Cineworld. The company had agreed to purchase Cineplex for $34.00 per share. Then the pandemic hit, and the company's share price cratered.

Cineworld was under pressure from critics of the deal. This was a company that was already highly leveraged, and was about to take on additional debt to acquire Cineplex.

In mid-June, Cineworld officially withdrew from the acquisition citing breaches of the condition of the agreement. On its call, Cineplex further disputed this claim.

"We believe that Cineworld had no legal basis to terminate the agreement. We believe that Cineworld is in fact in breach of the arrangement and attempting to waive their obligations under the arrangement agreement in light of the COVID-19 pandemic." – Ellis Jacob, President & CEO.

One thing is clear – the deal is dead. Any hopes shareholders had of being acquired are now in the rear view mirror. This is especially true now that Cineplex has adopted a shareholder rights plan.

This is a company that will need to go at it alone. Will it succeed?

Going concern

Without Cineworld, the company's ability to survive is centered on controlling cash burn. The company successfully entered into a credit facility amendment – a positive step. The company will now seek out additional financing options and asset sales.

However, their ability to execute on these events are unknown. Given this, the company included the language around "going concern" along with first quarter results. This rattled the markets. "Going concern" is an accounting term for a company with the resources to continue operating indefinitely. When this is at risk, as is the case with Cineplex, it means that it may not have the resources to continue operating.

CFO Gord Nelson explains:

"Cineplex will explore financing options and potential asset sales, but as of the date of our filing yesterday there is no [indiscernible] event. And as such, there is no certainty and accordingly we have included the going concern language in our financial statements."

To be honest, this is not all that surprising. Company operations have come to a screaming halt during the pandemic. It is now about finding a way to survive until the economy can reopen.

On the bright side, management remains confident given the success others in the industry have had in securing financing.

"As our peers and others have had successful financing events, we are confident that we will be able to deliver on this requirement prior to August 31, and as such the going concern would no longer be required assuming no other changes to the future outlook." – Gord Nelson, CFO.

Is Cineplex a buy today?

This is a tough question to answer. Cineplex is the largest cinema operator in the country. Unfortunately, it will be a long road to recovery. The entire industry is facing a new norm.

Even in the event of an economic recovery, Cineplex may never be the same. In the short-to-medium term, it will be a fight for survival.

While I'm confident the company will secure the financing required, there is a real risk of insolvency here. Given this, an investment in Cineplex is only for those with a high tolerance for risk.

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