Is Cineplex (TSX:CGX) Stock a Lost Cause?

Description

It's truly heartbreaking to see the iconic Canadian name to fall from grace. **Cineplex** (TSX:CGX) was a blue-chip dividend stock in the past decade or so.

In the last few years, there has been growing noise in the markets pointing to the ever-declining traffic to its theatres. The company had been combating that with higher prices from ticket and concession sales — at least until the pandemic hit. For the long term, it had also invested in other areas of entertainment, such as recreation rooms and golf.

Early in the year, Cineplex got really close to being acquired by U.K.-based Cineworld for $2.8 billion (or $34 per share). The deal was called off in June. Cineworld blamed Cineplex for breach of contract, but Cineplex insisted it did no wrongdoing. Cineplex had commenced an action in the Ontario Superior Court of Justice to claim compensation from Cineworld.

Regardless of how this case goes, the theatre business remains in really bad shape due to the COVID-19 pandemic-induced government-mandated closures. Even when locations reopen, there are social-distancing restrictions. Whether people will actually go also comes into question.

To preserve capital, Cineplex was forced to suspend its monthly dividend since February.

Cineplex's cash burn

There are two words to describe Cineplex's current business: *cash burn*.

The pandemic has substantially weighed on Cineplex's every line of business, damaging revenue and cash flow.

The actual revenue decline in Q2 was 95% to $22 million against Q2 2019. Theatre attendance was nil due to forced closures.

In fact, in Cineplex's Q2 report, it admitted that "[s]ince March 15, 2020, Cineplex has experienced a net cash burn of approximately $15 to $20 million per month as a result of having to close its theatres and [entertainment] venues." The Q2 net cash burn was $53.9 million, or roughly $18 million per month.

Is Cineplex stock a lost cause?

The hope is that the worst is over, as Cineplex has been reopening its entertainment locations gradually in phases with a focus on safety guidelines and allowable public gathering sizes.

From the end of 2019 to the end of June, Cineplex's cash and cash equivalents had dwindled by approximately half to $13.8 million.

Thankfully, in July, Cineplex was able to increase its liquidity through the offering of convertible debentures that raised about $316 million. Of course, it came with the cost of interest. The debentures bear an annualized interest rate of 5.75% through September 30, 2025.

The increased liquidity and the company's cost management should help the business survive the next 12 months.

The stock trades at a meaningful discount to normalized levels (whatever the new normal may be). What's Cineplex stock worth at normalized levels? Analysts think a price of $14 per share sounds about right. That'd imply upside potential of 68% from $8.33 at writing.

It could take a year or two for the realization of the new normal. Needless to say, Cineplex stock is a high-risk investment right now that's only suitable for speculative investing.

The Foolish takeaway

Cineplex is not necessarily a lost cause. From the current levels of about $8 per share, it can potentially trade at $14 over the next two years for annualized returns of close to 30%! However, near-term risks are also sky high.

For surer returns, investors can look into investing in growth areas such as cybersecurity through a fund like the **Evolve Cyber Security Index Fund** or blue-chip dividend stocks.

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