Why Cineplex (TSX:CGX) Is a Top 2021 Turnaround Play

Description

What a destroyer of wealth **Cineplex** (TSX:CGX) stock has been over the past few years. A worst-case scenario has essentially unfolded for the Canadian movie theatre kingpin, which has seen its top-line crumble like a paper bag amid the COVID-19 pandemic.

As you may remember, I called Cineplex's initial downfall back in July 2017, when the stock was a Canadian dividend darling near its all-time high in a piece titled "4 Reasons Why It May Be Time to Sell Cineplex Inc."

A bear-case scenario has panned out

At the time of publication, CGX stock was trading at around $50 and change. Shares plunged as low as $4 and change back in October, a time when I changed my tune on the name, urging investors to buy the stock that I thought had become far too cheap, even considering the profound headwinds that still lied ahead.

Just what headwinds are still plaguing Cineplex? The threat of continued COVID-induced disruptions, intensifying competition in the video-on-demand (VOD) space, the fragile balance sheet, the uphill road to recovery for the movie theatre industry, and the derailment of Cineplex's diversification initiatives.

There are no quick and easy solutions for Cineplex's management team for quickly overcoming such profound headwinds. That said, I'm still not buying that Cineplex is going to go under at the hands of the insidious coronavirus or any of the other headwinds that'll likely persist well after the pandemic ends. I see some severely-discounted tailwinds, which, while not strong enough to offset the slew of long-term headwinds, could be enough to move the needle in battered shares of Cineplex over the coming 18 months.

Can Cineplex overcome its growing number of headwinds?

In my 2017 bearish piece, I went into four specific reasons why I thought Cineplex stock was due to crater in the coming months:

- Difficulty coming up with new concepts
- The continued rise of the stay-at-home economy
- Health-conscious consumer behaviour that would weigh on Cineplex’s concession business
- The ridiculous valuation at the time (can you believe the stock used to trade at 40x trailing earnings in its glory days?)

The three former bear points persist, with the first two now exacerbated by the COVID-19 crisis. Indeed, things have got from bad to worse in 2020 for Cineplex, which continues to fight for its life amid the latest surge in coronavirus cases, which could threaten to shutter cinemas for many more months to come.

With a slate of seemingly unsurmountable and powerful headwinds, it can be tough to justify a contrarian investment in Cineplex. But, as someone wise once said, any stock can be a buy if the price is right. At today’s depressed valuations, I think Cineplex is such a “cigar-butt” stock that’s worth picking up for the many puffs that remain.

While video streamers have only gotten stronger in this pandemic-plagued year, I do not believe that they’ll steal away the entire slice of the pie from the old-school movie theatres. Moreover, with a potential post-pandemic discretionary spending boom on the horizon and a likely pent-up demand for social activities, I think Cineplex stock has a high chance of posting options-like upside if it survives this pandemic (I think it will).

Cineplex is a deep-value play worth taking a chance on

Cineplex may not have the best balance sheet in the world, but it looks good enough to get the company to the light at the end of the tunnel. Once Cineplex gets there, I think bums will fill seats faster than most think, even if Cineplex is due for a movie drought going into late 2021 and early 2022.

Many people who’ve been apart from their friends for months are likely itching to catch a flick, dinner, and a few games at the arcade at their local Cineplex in the company of friends.

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joefrenette