Why Investors Could Be Wrong About Cineplex (TSX:CGX) Stock

Description

Everything is rallying these days. TSX stocks are making new highs, Bitcoin has already gone to the moon, and don't even talk about the housing markets. While some of the excitement is understood amid the broader economic recovery, I find it strange that investors are still optimistic about **Cineplex** (TSX:CGX) stock.

The stock is comfortably holding $12 levels at the moment, close to its nine-month highs. Although the pandemic's end seems in sight, and there are some chances of Cineplex's recovery, I think the challenges it faces right now are much grimmer. It could be a classic case of investor myopia.

Management's warning

Cineplex reported an 88% year over year fall in Q4 revenues. The financial dent was evident and was much expected. What notably stood out was the management's downbeat commentary. It warned that, due to the ongoing closures and movie release delays, the company could breach its debt covenants in the next 12 months and might result in the event of default.

The management has been warning investors about its grave liquidity position since the middle of last year. However, the tone has turned remarkably negative in its Q4 earnings. Interestingly, investors seem to have overlooked this, as CGX stock has soared more than 10% since its Q4 release last week.

Cineplex's balance sheet has become extremely weak in the last few quarters amid the closures. At the end of Q4 2020, it had $16 million in cash. Investors should note that the top theatre company burned $25 million per month on average during the fourth quarter. Its cash-burn rate accelerated in Q4 compared to earlier pandemic-dominated quarters in 2020. The company might have to look for additional avenues to lower its cash burn to survive longer.

The worries could substantially amplify in Q1 2021. Ongoing closures and a mutating virus mean another quarter of losses and cash burn for Cineplex. Its cash-burn rate and current liquidity position clearly highlight the squeeze.

Some analysts see Cineplex stock as a value pick. However, CGX stock is not at all cheap. It is trading at a price-to-book value ratio of 31, which looks exorbitantly overvalued.

What can drive Cineplex's recovery?

There are few pointers that can change its fortunes. A faster vaccination is one big hope. CGX stock changed its course when the vaccine was launched in late October last year. And indeed, the sooner the population gets vaccinated, the faster its recovery will be. But things seem the opposite at the moment.

Also, even if a majority of the population gets a vaccine, how fast it can increase foot traffic in theatres will be interesting to see. Apart from vaccinations, government help could be a booster for Cineplex. But that seems unlikely at the moment.

My take

I see a high possibility that Cineplex might not make it to the pandemic's end. The management's cautionary commentary fortifies that point. Selling the head office building and asking for extensions from lenders were some of the early red flags for investors. You can play on Cineplex's volatility for short-term gains, but I think the risk/reward scenario is highly unfavourable for long-term investors.

CATEGORY

1. Coronavirus
2. Investing
3. Stocks for Beginners

TICKERS GLOBAL

1. TSX:CGX (Cineplex Inc.)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
3. Msn
4. Newscred
5. Quote Media
6. Sharewise
7. Yahoo CA

Category

1. Coronavirus
2. Investing
3. Stocks for Beginners

Date

2025/08/20
Date Created
2021/02/19
Author
vinitkularni20