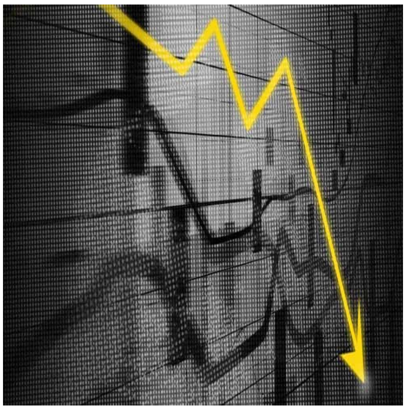

Why Cineplex (TSX:CGX) Stock Fell to 2-Year Lows Last Week

Description

Canada's leading theatre chain operator **Cineplex** (TSX:CGX) stock was trading comfortably around $13 levels for a while. However, last week, the stock broke below its typical range and hit two-year lows.

We all know how the pandemic dented its business for about two years and pushed it into a debt spiral. But things gradually started changing this year. People are returning to big screens, and an encouraging growth spurt was also seen on its top line. So, what's wrong? Why is the stock moving south?

Cineplex-Cineworld deal

Well, even if the foot traffic at the theatres is increasing, that will not solve all of Cineplex's problems. The company piled up a huge debt load during the pandemic to keep its operations going. The interest from that debt is knocking profitability significantly. However, there was a glimmer of hope in getting rid of a large chunk of this debt burden.

Remember the Cineworld-Cineplex deal before the pandemic? Cineworld, a British entertainment conglomerate, made an offer to buy Cineplex. But it walked out of the deal in mid-2020, given the uncertainties the pandemic would bring. So, the Ontario court ordered Cineworld to pay $1.24 billion in damages to Cineplex. Now, you may think that the pandemic was not all that bad for Cineplex, considering the settlement. But Cineworld has not paid for these damages yet. And it will likely not pay in full anytime soon.

Why? Cineworld confirmed last week that it is looking to file for bankruptcy. For almost all similar reasons as Cineplex, Cineworld also kept piling up its debt in the last few years, which amounted to over $6 billion. There was never going to be a quick recovery from the pandemic blues as once it seemed. Plus, Cineworld has appealed against the court ruling, and the next hearing is scheduled for October 2022. So, although Cineplex is to receive its settlement, the bankruptcy proceedings could take time.

Note that receiving the settlement sooner could substantially change Cineplex's prospects. At the end of the second quarter of 2022, Cineplex had $1.8 billion in net debt. So, if it obtains those funds in time, Cineplex could pay off a large chunk of its loans. Plus, it will save millions of dollars in debt-servicing costs. It has spent around $120 million in interest expenses in the last 12 months.

If the payment from Cineworld is delayed longer than expected, the debt covenants will likely turn more unfavourable for Cineplex. So, it's crucial for Cineplex to get the payment soon and in full.

Should you buy CGX stock now?

As stated earlier, moviegoers are returning to big screens in a big way. Cineplex witnessed jaw-dropping revenue growth of 418% year over year in the last 12 months.

The recent correction in CGX stock could be an opportunity. Plus, the settlement amount and how it could turn things around give massive hope. However, given the time delay and uncertainties associated with it, it could fuel the volatility in CGX stock, at least in the short term. However, if you have the stomach for its large swings, CGX could be an attractive bet.

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