SELL ALERT: Dump Your Cineplex Stock Now, if You Still Can

Description

Cineplex stock could be headed for a rough ride in the near term. I'm going to discuss in this article why investors who may have profited off of the rebound in **Cineplex** (TSX:CGX) to take their profit and run. Run as fast as you can.

There's a real debt problem here

Some may know the feeling of having creditors chase after you. For publicly traded companies, when one isn't able to meet debt covenants (i.e. meet minimum lending requirements), things turn sour really quickly.

As fellow Fool contributor David Jagielski pointed out in his recent article, Cineplex's current ratio doesn't look good. In fact, its current ratio is terrible. With current liabilities outweighing current assets by more than four times, Cineplex will need access to cash — fast. Given issues around debt covenants of existing debt, issuing new debt (or equity for that matter) could be costly for the company. Accordingly, shareholders are likely to be the ones to feel the pain in this regard.

Asset sales are good but not enough

Cineplex's management team recently announced the sale of its flagship headquarters property in Toronto as a way of raising cash. The sale will fetch $57 million for Cineplex. This is much-needed liquidity, given the predicament the company is in with respect to its current liabilities. While Cineplex is planning on leasing this space back from the acquirer, consolidation looks to be on the horizon for the company moving forward.

Times aren't going to get better soon

If this past summer is any indication of what is on the horizon for Cineplex in the wake of the pandemic, things don't look good. With attendance down more than 90% across its locations, Cineplex's ticket revenue has become a serious cash flow problem. In the near term, the inability to earn enough cash flow to cover the company's expenses could cause more solvency issues.

Over the long term, low attendance numbers are likely to persist, as secular trends shift attendance away from theatres toward streaming platforms and on-demand movie options. I see this shift accelerating over time, reducing the thesis for owning a stock like Cineplex long term.

Bottom line

Any investor seriously considering buying Cineplex for a long-term hold right now should check their thinking. This pandemic may be short-lived. However, even in a best-case scenario, the long-term outlook for the cinema industry is dire. In my view, this is a toxic stock that very closely approximates a value trap right now. Investors ought to either steer clear of this stock or dump it now, in my view. This is not a stock that is worth owning long term.

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