

# Corus Entertainment Inc. (CJR)

Group 2: Rahul Bedi, Rabih Chour, Tilak Mathur, Evan Reidel, Jason Sookdeo

## **Initial Screening**

As of March 14, 2018, Corus Entertainment (CJR) has a share price of \$7.19 while possessing a P/E ratio of 7.53 and P/B ratio of 0.57 along with a market cap of approximately \$1.49B. CJR is currently trading near its all-time low of \$6.93 compared to its 52-week high of \$14.10. Additionally, CJR's share price has undergone a precipitous decline from \$25 since 2014. Average annual trading volume is 775,672 indicating the company is widely traded. Furthermore, Corus has significant analyst coverage including all of the major financial institutions. The market cap exceeds the threshold for Canadian equities of \$500M. However, CJR meets both of the initial targets for P/B and P/E with each being significantly below the thresholds of 13 and 1.2 respectively, signaling that CJR may be potentially undervalued.

## **Industry and Company Analysis**

CJR is a media and content company operating mainly in the Canadian market with revenues broken into two general streams: television and radio. The television division generates 90% of the firm's revenues, which can further be broken down into advertising, subscription, and content licensing revenues. The remaining 10% is generated by the radio division but represents a periphery area of the company's business. To combat the immense changes in the media industry with the shift of consumers away from television and traditional mediums, Corus has shifted to place greater focus on valuable content and providing advanced data analytics to corporate customers. Investors must be aware of the risks stemming from technological advancement, business cyclicity, and governmental regulations.

As we take a closer look at CJR's operations, earnings have increased on average YoY more than 42%. However, this large jump was primarily driven by acquisitions including 100% ownership of Shaw Media further extending their dominance in television and media content in Canada. The company has an EBIT margin of 30% and a net income margin of 11%, which have remained stable over the past ten years. However, the media industry is facing disruption from technological innovation and changes in consumer preferences. Despite this shakeup, Corus still possesses a dominant leadership position with the Canadian industry and have taken steps to diversify and innovate to meet the disruption. As such, we have rated the business risk of CJR to be *Medium*. This suggests an optimal capital structure of between 30-49%. Additionally, CJR's D/V of 47.66% (average of the previous 10 years) suggests *Medium* financial risk; however, we have designated *High* financial risk as previous debt and current analyst coverage reflect a BB rating. We believe a BB rating accurately represents the true financial risk of CJR. This corresponds to a before tax cost of debt of 5.20% (Spread = 2.79%), an ERP of 5.9%, and cost of equity of 11.10%. A WACC of 7.63% is derived, and the first pass ROIC of 6.40% indicates that our NAV should be greater than our EPV. This analysis indicates that CJR does not have franchise value and can not earn returns greater than its cost of its capital.

**NAV:** The NAV/share is \$20.72 as calculated in Exhibit 3.

**EPV:** The EPV/share is \$9.80 as calculated in Exhibit 4.

## **Catalyst/Franchise**

Based on our analysis NAV is significantly greater than EPV, which supports our initial hypothesis that Corus can not earn a return greater than its cost of capital. This is further supported by an ROIC2 of 4.32%. This represents a catalyst value of \$10.92. We believe that overcapacity plays a role in this disparity, which reflects the changes taking place in the industry in terms of new entrants; however, we believe management is the main cause of the catalyst. While they've done a reasonable job positioning Corus' offering, they've still moved too slowly in adapting to the industry's keen focus on content being available across multiple viewing platforms. It is likely that Corus' top line will remain stagnant if management continues to act slowly in embracing the evolution of viewing technologies. Additionally, the Shaw family owns approximately 85% of the Class A voting shares and clearly has strong influence over the company's future. To date the family has managed the company relatively well and there is no indication they are seeking to lessen their control of Corus, which means a status quo outlook. Additionally, it is unlikely that the management or board will materially change in the short-to-medium term. As such, we have assigned a 20% catalyst probability value.

**Intrinsic Value:** Based on the discussion above, the intrinsic value of the company is \$11.99 as calculated in Exhibit Summary.

**Entry Price:** We recommend that investors purchase at a share price of \$7.99.

**Recommendation:** We recommend a **BUY** based on the current price of \$7.19