



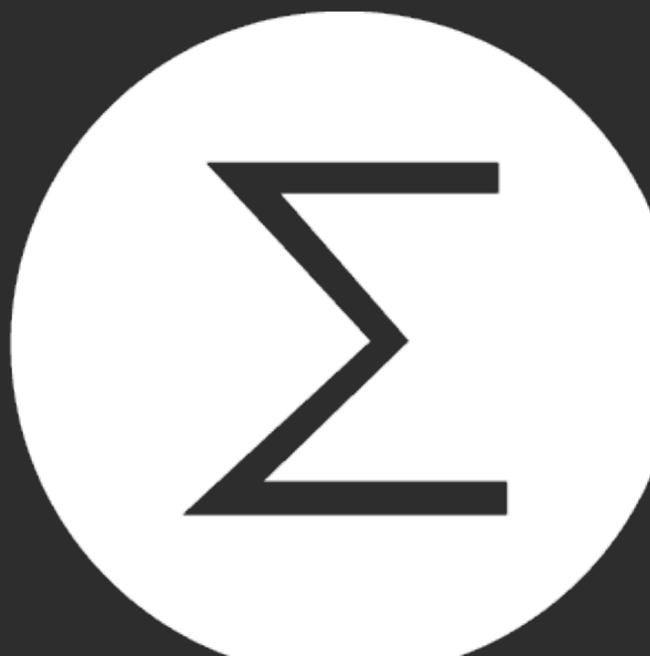
SUMZERO

MARKET COMMENTARY



CURTAINS OR COMEBACK?
MOVIE THEATERS AND
STUDIOS ADAPT OR DIE
DURING PANDEMIC

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INTRODUCTION

The news that **Disney (DIS: US)** plans to release the live-action version of *Mulan* with an additional \$29.99 on-demand price tag to Disney+ subscribers shone a spotlight on one of the biggest questions impacting the film industry as the COVID-19 crisis continues to hamstring the economy: *how will new cinematic releases be affected if movie theaters remain closed or if audiences stop going to movies?*

While filming and production have been delayed or halted altogether on some features, Hollywood has a backlog of big-budget films that had completed principal shooting before the pandemic took hold of the country in early March. Some of those films were intended to be seasonal blockbusters, timed to lure kids on summer break and bring tourist season moviegoers in front of the silver screen with the hope of breaking new records and staying in theaters - where the money is - as long as possible before retiring to video-on-demand and eventually [syndication and streaming](#).

Once major markets like New York City and Los Angeles began suffering under the burden of social distancing measures enacted by state and local governments, studios began realizing that what they had initially thought would be minor delays might, in fact, be the beginning of the end of moviegoing.

The organic solution required little imagination. Studios - which now also comprise platforms like **Amazon (AMZN:US)** that produce their own content - looked to premium video-on-demand (PVOD) to release new movies on streaming services like Amazon Prime Video, Disney+, Hulu, Apple's (AAPL: US) iTunes or AppleTV, and AMC's (AMC: US) On-Demand. The groundwork had already been set: consumers were no strangers to paying extra for live, on-demand sporting events and premium-priced rentals of films in either limited release or fresh off the theater circuit. The questions became those of how quickly people would embrace PVOD as the new moviegoing and how much they would pay for a new Hollywood studio movie that could easily be overshadowed by an equally intriguing new series or film produced and included by companies like Amazon, HBO, and Disney as part of their existing subscription packages. Could living rooms and laptops replace box office revenue, not just in the midst of a pandemic, but in the uncertainty of a declining and battered consumer economy and rising unemployment rate?

Universal Leads the Way

One of the first tests came with **Comcast (CMCSA: US)** subsidiary, Universal Pictures' relatively low-budget (\$7M) science-fiction thriller *The Invisible Man*, which was released in U.S. theaters on February 28, 2020. Despite the looming pandemic, the movie's opening weekend was a success, [topping the box office with \\$29M](#) from 3,610 theaters. The following weekend, it dropped 47%, losing its first place ranking to Disney's *Onward* opening, and [bringing in \\$15M](#).

Within a week, however, everything changed. Deadline reported that theaters in New York, Philadelphia, Washington DC, Boston, and Seattle had closed as COVID-19 took hold. On March 20th, Universal execs made an unprecedented decision to release [The Invisible Man – along with The Hunt, Trolls: World Tour, and Emma – on VOD](#) with a [rental price of \\$19.99](#) on Amazon Prime Video, iTunes, and Google Play. This was executed well ahead of the end of the typical 90-day theatre run, while also leaving the movie in whatever theaters they could: a few hundred drive-ins across the country. Disney followed suit with *Onward*, as did Sony (SNE: US) Pictures with *Bloodshot* and Warner Bros with *The Way Back* and *Birds of Prey*. By the end of March, eight of the top ten films on [Fandango were \\$19.99 PVOD releases](#). Viewers, it seemed, were happy to forego the expensive snack bar prices and pay a single-ticket price for a film that they could watch alone or with their friends and family (hopefully while practicing social distancing).

Universal (and subsidiary Focus Features) has since adopted that tactic as policy. In late July, the studio reached an [exhibition agreement with AMC Theaters](#) (AMC: US) that drastically cuts the theatrical exclusivity window from 90 days to 17 - to include three weekends - after which time the studio may opt to release its films to PVOD, including AMC's On-Demand service. While the details of the deal remained confidential, both parties acknowledged that it represented a shift in the way people consume entertainment content, though AMC Adam Aron also stated that he was "confident that moviegoers will come to (AMC) theaters in huge numbers in a post-pandemic world."

The End of Cinema?

More than one SumZero buy-side contributor previously long the company remained skeptical of Aron's assertion. After seeing AMC's stock price cut in half since last October, [Stoic Point Capital Management](#) Co-Founder [Raj Shah](#) closed his [position in the company](#), citing the ongoing pandemic crisis. "COVID-19 represents an incredible unknown to the outlook for theaters," Shah wrote in a final update, "and in particular the equity value. While a pandemic was certainly not among the pre-mortems, the lower quality nature of this asset and high leverage means it is prudent... to wait and see."

Echoing Shah's cautionary tone is [Firebird U.S. Value Fund](#) PM [Steven Gorelik](#) who closed his company's position in May "due to significant risk of bankruptcy as a result of COVID crisis." AMC, Gorelik writes, is particularly fragile when it comes to this kind of disruption, noting that "company cash flows turn negative with [an] attendance drop of 15%. Thanks to COVID closures and [the] new threat to the viewing window, this scenario is more than plausible and leaves AMC at the mercy of landlords and lenders." Despite recent debt restructuring and plans to [reopen all international theaters](#) and two-thirds of U.S. venues by August 20th, AMC continues to trade at a fraction of its 52W high of \$12.13.

Nevertheless, a comeback is not out of the question: the company's [stock price saw a 17% surge](#) on August 13th after the reopening announcement, which seemed to add confidence to [IMAX \(IMAX: US\)](#) and [Cinemark \(CNK: US\)](#) shareholders. Some on the buy-side have been confident throughout the pandemic: in his [idea long Cinemark](#), SumZero contributor [Pete Wahlstrom](#) concluded that while "not all of the bad news is priced in at current levels ... a lot of it should be; this business is not (nearly) as bad as feared." AMC's announcement came with a major push designed to encourage movie fans to return to cinemas: the company, which was founded in 1920, is marketing the reopenings as a [centennial celebration, offering 15-cent movie tickets](#) and hoping to cash in on [AT&T \(T:US\)](#) subsidiary Warner Bros' thriller *Tenet*, which will be released on September 3rd.

Although the absence of a vaccine and economic devastation have created uncertainties in the consumer discretionary sector, it's important to remember that the power of entertainment lies in society's need for escapism. Entertainment has the ability to provide refuge from the challenges of our daily lives, especially during a global pandemic and civil unrest. While the medium for film consumption may change, the appetite for cinematic entertainment isn't going anywhere.