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Title:
An Analysis Of The Journal Register Company (JRC)

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Summary:
Let me begin with some of the eye – catching metrics that might lead an investor to consider purchasing shares of the Journal Register Company (JRC). This newspaper company has a price – to – earnings ratio of 11.3, a price – to – sales ratio of 0.93, a 5 year average return on capital of 17.6%, and a five year average pre-tax profit margin of 27.4%.

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Article Body:
Let me begin with some of the eye – catching metrics that might lead an investor to consider purchasing shares of the Journal Register Company (JRC). This newspaper company has a price – to – earnings ratio of 11.3, a price – to – sales ratio of 0.93, a 5 year average return on capital of 17.6%, and a five year average pre-tax profit margin of 27.4%.

Now, for the bad news. The Journal Register Company has an enterprise value – to – EBITDA ratio of 9.07 and an enterprise value – to – revenue ratio of 2.24. Obviously, this company is carrying a lot of debt. So, perhaps the multiples on the common stock price are deceptive.

Before I go any further, let me take a moment to point out the fact that, in the case of Journal Register, the shares you buy are literally common stock; that is, the security is common to all owners. This is a rarity in the publishing business, where families often maintain control of their newspapers via ownership of a class of stock with (much) greater voting rights.

So, how should an investor value the Journal Register Company? Should he use JRC’s market cap or its enterprise value? I have usually encouraged a full and careful consideration of all debt when making any investment. In the case of

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JRC, such debt makes up a large portion of the company’s enterprise value. Is it really best to lump the debt and equity together to determine the true price Journal Register is selling for?

I think it is.

There are situations in which the leverage inherent in a debt – heavy capital structure works to the benefit of the common stock holder. The most obvious example is a highly leveraged, growing company selling at a bargain price. The increase in earnings is amplified by the fixed debt, because the debt creates a sort of break even point, much like a traditional fixed cost. Just as greater production can give tremendous benefits to the owner of a large plant, or greater sales can give tremendous benefits to the owner of a large store, greater pre-tax earnings before interest charges can give tremendous benefits to the owners of common stock.

Does this scenario apply to Journal Register? Perhaps, but I don’t think so. Long – term, the economics of the newspaper business will likely be quite poor. Even for Journal Register’s properties, I am projecting a fall in circulation with no end in sight. Some may disagree with this assessment. However, I believe they are being overly optimistic. Past performance is only a good estimate of future performance insofar as the future resembles the past. I believe the future of newspaper publishing will be sufficiently different from the past to render any estimate of Journal Register’s future performance based solely on its past performance quite inaccurate. So, for the most part, the leverage inherent to Journal Register’s capital structure will likely be working against the long – term investor.

Economically, Journal Register’s assets are encumbered. The legal reality is immaterial to the shareholder. The company can not sell of its assets without either paying off its debt or maintaining control over sufficient free cash flow to meet its obligations. Today, money is cheap. It may not be so cheap in the future. Journal Register is insulated from interest rate changes on its current borrowings. However, the company can not guarantee that, if it were refinance its debt as it came due, interest charges would remain as low as they are today. This is true for every business, but it takes on greater importance in the case of the Journal Register Company, because of the company’s debt heavy capital structure, today’s historically low interest rates, and the likely future trend of newspaper circulation.

Together, these three factors form a kind of perfect storm. But, it is important that the facts be assessed calmly. There is no need for exaggeration. The Journal Register Company is not in any grave peril. There would be no risk of

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insolvency, if the company did not borrow further, and committed its substantial free cash flow to paying down its debt. A look to the recent past suggests the company is unlikely to follow such a conservative course. That is not necessarily a bad thing.

There may be value in future acquisitions. In fact, the current climate is perfect for making acquisitions that truly add value to the company. But, other companies with operations capable of regularly generating lots of free cash flow have sometimes found themselves in financial difficulties, because of an overly ambitious capital structure and reduced profitability within their chosen industry. I am not suggesting the Journal Register Company will find itself in such a position. If it is well – managed, there is no reason for Journal Register to face such peril. But, it is rarely wise to assume a company will be well – managed.

The problem with the Journal Register Company as an investment is not the risk created by its debt. It is easy to overstate that risk. The problem is the price. The Journal Register Company is not as cheap as it appears to be. Newspapers will not be going the way of the Dodo anytime soon, but they are already in decline. This decline will not be reversed.

Investors need to remember the importance of growth. Newspapers are not growing. There is no need to chase stocks with lofty multiples merely to acquire some short – lived hyper growth. But, there is a need to avoid companies that will not grow their earnings. There are many stocks trading at higher P/E ratios than JRC that are, in fact, better bargains.