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Six Flags Good For Another Bite After Avoiding Major Blows

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Summary

- After rising for 6 years, Six Flags had been stagnating for the past 12 months over these concerns.
- Earnings is a small component but the threats of a new competitor, natural disaster and cyber security are the major clouds over its head.
- Having avoided the latest natural disaster and dormant about its two other threats, investors should have another go at the company.

Six Flags (SIX) is a household theme park company in the United States after being in the business for over 56 years. As a parent or teenager, you would have your thrills there. As an investor, what do you know about this \$5.34 billion company that is priced at \$59 today? If you look closer, you will realize that SIX have not been able to break out of the \$50 to \$65 range for the past 12 months.

Six Flags had a meteoric rise from \$6 in Aug 2010 to \$62 in April 2016. Over 90% of its shares are held by institutional investors. Its ten times' rise in 6 years is fueled by its reputation as the best regional theme park in the United States that incorporates virtual reality and thrilling rides earning \$1.3 billion in revenue last year.

For 6 years, this was enough for management to hit earnings targets of \$350 million and \$500 million but here are some of the major new challenges for its management.

Competitor

In the latest earnings call in July 2017, Six Flags' CEO boasted that one of their key competitive advantages is that it is extremely difficult for competitors to enter their space due to high capital expenditure. Shortly after that, Triple Five completed the \$3 billion funding for a new theme park American Dream in New Jersey. American Dream is situated closer to New York than Six Flags' largest theme park, Great Adventure. It is set to open in March 2019. So far, the entire mall, which includes the American Dream, is estimated to take \$4.8 billion to build.

While the new attraction will not be as large as Great Adventure in size, it has a variety of new entertainment options that will lock in families and reduce demand for another adventure park. This comes at a time when Six Flags is trying to increase its season pass ticket sales to boost sales and encourage families to spend more on its restaurants. While

the actual opening is 2 years into the future, it is a source of worry for investors. Can management hit its audacious goal of \$750 million in earnings in 2020 with this new competition?

Natural Disaster

The leisure industry is weather averse and rain over the Easter period turned the second half earnings of 15 cents per share in the previous year to 6 cents loss this year. This is despite their policy of consistently adjusting their price up to drive up revenue and maintaining strict cost discipline.

More recently, a series of natural disasters hit in the industry hard. On 26 August 2017, Hurricane Harvey forced Six Flags to close their Fiesta Texas theme park for 2 days. The Hurricane season in the US is not over yet and experts expect another 3 hurricanes from now until the end of the year.



Abandoned Six Flags Park in New Orleans. Source: Daily Mail

The worst-case scenario would be when a super hurricane such as Hurricane Katrina hit one of their existing theme parks. Hurricane Katrina flooded their New Orleans theme park, which forced them to close in August 2005. That was a major hit to their finances, which contributed to their bankruptcy in August 2009.

This is why investors are worried about the damage done to their Mexico theme park when a 7.1 magnitude earthquake hit in September 2017. Will it be another New Orleans? If another major disaster destroyed one of its theme parks, Six Flags might have to spend nearly \$3 billion to build a competitive theme park, which would amount to over 56% of its market capitalization. Its latest investment in China is estimated to cost \$2.4 billion to build. Luckily, for investors, initial assessment shows that the damage to their Mexico theme park is minimal.

Cyber Security

Since Six Flags opened its doors in 1961, it had a history of innovation. It was the first theme park to introduce the roller coaster, mine train ride, parachute drop and river rapids. Some of which are still staples of theme parks today. Recently, it introduced virtual reality to millions with the Superman Roller Coaster Ride.



Superman VR Ride. Source: SIX Flags

After introducing virtual reality to critical acclaim for 2 years, new security flaws had emerged in virtual reality goggles, which would require cyber security measures. According to Singapore's IT Solution System, cyber security specialists are currently facing a global shortage and attackers have been more successful in their attempts in the recent years. Lloyds of London estimates that the scale of cyber-attack damage is equivalent to losses reserved for a major natural disaster. Juniper Research is even more pessimistic and predicts that the global damage will lose \$2.1 trillion in 2019.

It remains to be seen how much of these damages will land on Six Flags and how the impact will be. For instance, if a hacker was successful in placing a ransomware while its riders are struck in the middle of a roller coaster and force them to experience nauseating images, it would be a major blow to its reputation in addition to financial damages.

Good For Now

American Dream is not set to open until 2019, its Mexico operation had escaped the wrath of nature's fury and its virtual reality sets had not been in the cross-sight of hackers like how hospitals have been targeted. Currently, Six Flags is actively expanding to Asia and the Middle East with projects in China and Dubai respectively.

Since it emerged from bankruptcy in 2010, it had returned over \$1 billion in cash dividends and \$1.85 billion in share repurchase to investors. Years of steady economic recovery following the 2009 global financial crisis had resulted in steady employment gains, which

had strengthened consumer confidence. This will increase discretionary spending in theme parks as the US population compares consumer loans to get attractive cash advances in expectation of a better future.

However, the perfect storm seems to be building up and we just need 1 or 2 major hits for a capital-intensive business like Six Flags to go bankrupt again. Until then, it is a dividend cash cow notwithstanding the missed lofty target of \$600 million profit and worth a bite by investors. After all, it is in the roller coaster ride business.

Disclosure: I/we have no positions in any stocks mentioned, and no plans to initiate any positions within the next 72 hours.

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