Bombardier vs CAE: Which Should You Add to Your Portfolio?

Description

The airline sector of the **S&P 500** is currently up 39.15%, much better than the overall market at only 6.45%. The consolidation that happened in 2013 helped airlines streamline their business models and get back on track to profitability.

This is great timing considering that the global economy is also back on its feet and airline traffic is continuing to show growth. In Canada alone, traffic is up 5%, while in China that same metric is up 8.4%. Instead of investing in the obvious airlines like **Air Canada** or **WestJet Airlines** let's compare two manufacturers directly exposed to the airline industry.

CAE

Our first company is **CAE** (TSX: CAE)(NYSE: CAE), which provides simulation technologies and integrated training services, mainly to the civil air travel industry and government military forces worldwide. Mainly a provider of airplane simulators (commonly known in the industry as FFS or Full Flight Simulators), CAE is the market leader in its field and possesses long-standing relationships with most of the airline companies in the world. Airline regulation requires operators to have a certain percentage of simulators for each fleet of airplanes they have. That means the better airline traffic is, the more simulators are needed from CAE to compensate the added fleet.

Its operating metrics are great with a net margin of 10% last quarter and reasonable long-term debt to assets of 26.4%. Building simulators is not cheap, and this sector is known to have some leverage, but the short-term liquidity of CAE does not need to be put in question. With a current ratio of 1.4 and positive yearly free cash flow, the company is in a great operational situation to benefit from the positive business cycle it is presently in.

The stock is currently trading at a 19 price-to-earnings ratio, not cheap by regular standards, but considering how great it has been operating in recent years it is understandable. The good news is that so far this year it is essentially flat and with earnings season commencing, an average quarter might send the stock down to more attractive valuation. At the current price, it is warranted to keep this one on your radar.

Bombardier

Unlike CAE, which is exposed to all the airplane manufacturers, **Bombardier** (TSX: BBD.B) is itself an aircraft manufacturer and sometimes a client of CAE. Also, unlike CAE, it has not benefited from the recent bull market in the aerospace industry. The primary reason for that slump is the constant delays of its new CSeries model of airplanes. This new aircraft was announced back in 2004 and in the beginning had a delivery date for 2013. Unfortunately, many delays have caused Bombardier to push back its delivery dates to clients and its effect has been felt with lower order backlogs and pressure on margins. Recently it was rumoured that Air Canada was considering ordering 20 CSeries planes, but the company instead decided to stay with its existing jets.

Just recently, Bombardier had to lay off close to 1,500 workers and while management did not say outright that the cause of the layoffs were related to the CSeries project, having a delivery date extended by two years puts a dent on estimated cash flows. The effect of the delays can also impact the financial situation of the company, which reported a net income margin of only 2.94% last quarter. Long-term debt is not yet a problem with a ratio of total debt to assets of 24.5 and the recent workforce cut should help the company stabilize its expenses while it continues to work on the CSeries.

There is a positive case to be made for Bombardier. The company’s transport division is doing great and benefiting from the booming rail sector economy in North America and even with all the extra costs added to project delays it is still posting positive earnings.

This Fool prefers CAE over Bombardier in the long run. I admire the courage of Bombardier’s management in trying to enter a new sector of the airline industry by building a brand new plane, but I think that the challenges associated with the project are not worth the rewards, especially when I can own a company that is exposed to all the aircraft manufacturers instead of only one. With CAE, regardless if Air Canada decides to buy more 737, A320, or CSeries jets, they’ll need simulators to train their pilots and CAE is the market leader for all three planes. Now if only it could come down a bit more in price.

CATEGORY

1. Investing

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1. NYSE:CAE (CAE Inc.)
2. TSX:BBD.B (Bombardier)
3. TSX:CAE (CAE Inc.)

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