



Why WestJet Airlines Ltd. Continues to Be First Class

Description

While most airlines are characterized by low returns and inappropriately large amounts of leverage, there is always an exception to the rule. **WestJet Airlines Ltd.** (TSX:WJA) was not only profitable during the hectic 2009-2011 period, but has also performed consistently well since.

What has allowed WestJet Airlines Ltd. to continually differentiate itself from struggling peers?

The business

WestJet Airlines is a Canada-based provider of airline service and travel packages. The company offers service to approximately 88 destinations in 20 countries in North America, Central America, the Caribbean and Europe. It has a fleet of approximately 113 aircraft, including eight Bombardier Q400 aircrafts and five Boeing 737 NG 800 aircrafts.

Focus on returns

While many airlines (especially the low-cost carriers) have emphasized growing the size of the company through new routes and destinations, WestJet Airlines management has always focused on real returns on capital rather than simply revenue growth.

This disciplined approach has allowed the company to generate impressive returns over the past decade, especially for an airline. WestJet Airlines posted positive profit margins throughout the financial crisis, boasting an average return on equity of 13.5% over the past 10 years. Management targets an overall return on capital of 12%, which it has achieved in each of the past three years.

Management is also shareholder-friendly, repurchasing stock in seven of the past 10 years. All of the purchases were below the current share price, creating another level of value for investors. In February, the company boosted its dividend for the fifth time since introducing it in 2010.

A proven ability to manage fuel costs

WestJet's ability to turn a profit in each of the past 10 years is due in part to its skilled fuel cost management. Fuel costs are consistently only about one-third of revenues. Even when revenues

dipped by around 15% per mile flown in 2009, the company was able to reduce fuel costs by almost 32% per mile flown.

The company has also made multiple moves to permanently reduce fuel costs over the long-term. During the 2014-2015 period, the airline swapped 10 of its oldest Boeing 737-700s for 10 new Boeing 737-800s. The company also announced in 2013 an order for 65 Boeing 737 MAX aircraft with delivery dates of 2017-2027. The engines in these planes reduce fuel burn and CO2 emissions by roughly 13%.

Capitalizing on new revenue streams

WestJet posted ancillary revenues of \$216.5 million (US\$174.29 million) in 2014, an annual increase of 31.2%. The company has almost doubled ancillary revenues per customer since 2010, impressively growing from \$6.03 to \$11.05.

The carrier attributes the growth to increases in the number of guest bookings, pre-reserved seating and Plus seating upgrade sales, the continued penetration of its MasterCard program, and the introduction of a first bag fee.

An inability to capitalize on additional revenue streams such as these have haunted other airlines into bankruptcy.

A long-term winner

While there will always be booms and busts in the airline industry, WestJet looks to focus on the same qualities that allowed it to outpace its competitors over the past decade. Continuing its impressive operational management and strong focus on creating shareholder value, investors should consider this company as one of the only airlines to consistently buck the industry trend of low returns.

CATEGORY

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