Is WestJet Airlines Ltd. a Buy After its 5% Earnings-Induced Decline?

Description

WestJet Airlines Ltd. (TSX:WJA), the second-largest airline company in Canada, announced its first-quarter earnings results before the market opened on May 3, and its stock responded by falling over 5% in the day's trading session. Let's break down the results and the fundamentals of its stock to determine if we should use this weakness as a long-term buying opportunity or a warning sign to avoid it for the time being.

A weak quarter of year-over-year declines

Here's a summary of WestJet's first-quarter earnings results compared with what analysts had expected and its results in the same period a year ago.

Metric	Q1 2016 Actual	Q1 2016 Expected	Q1 2015 Actual
Diluted Earnings Per Share	$0.71	$0.65	$1.09
Revenue	$1.03 billion	$1.03 billion	$1.08 billion

Source: Financial Times

WestJet's diluted earnings per share decreased 34.9% and its revenue decreased 4.8% compared with the first quarter of fiscal 2015. It noted that these less-than-stellar results could be attributed to the impact of economic weakness in Alberta, which has been an ongoing issue for the company, but it went on to state that the fundamentals of its business remain strong, and that it's seeing positive trends from the adjustments it made to its schedules and the strategic initiatives it has continued to undertake.

Here's a quick breakdown of 10 other notable statistics from the report compared with the year-ago period:

1. Net earnings decreased 37.7% to $87.6 million
2. Segment guests increased 8.4% to 5.33 million
3. Guest revenues decreased 7.4% to $886.2 million

4. Ancillary revenues increased 14.8% to $95.4 million
5. Other revenues, which includes ancillary revenues, increased 14.8% to $145.2 million
6. Revenue per revenue passenger mile (yield) decreased 11.6% to 17.22 cents
7. Earnings from operations decreased 37.5% to $123.3 million
8. Operating margin contracted 620 basis points to 12%
9. Cash provided by operating activities decreased 13.9% to $222.1 million
10. Repurchased 800,000 shares for a total cost of approximately $14 million

WestJet also announced that it would be maintaining its dividend of $0.14 per share in the second quarter, and it will be paid out on June 30 to shareholders of record at the close of business on June 15.

Should you buy WestJet on the dip?

The first quarter was very weak for WestJet, so I think the post-earnings drop in its stock is warranted. However, I also think the drop represents a great buying opportunity for the long term for three reasons.

First, it's undervalued. WestJet's stock now trades at just 8.6 times fiscal 2016's estimated earnings per share of $2.38 and only 8.2 times fiscal 2017's estimated earnings per share of $2.47, both of which are major discounts compared with its five-year average price-to-earnings multiple of 11.8 and the industry average multiple of 11.7.

Second, it has been actively repurchasing its shares. WestJet repurchased 1.44 million shares in fiscal 2014, 4.72 million shares in fiscal 2015, and 800,000 shares in the first quarter of fiscal 2016, and there are two million shares remaining for repurchase under its 2015 normal course issuer bid (NCIB), which expires on May 12. In its earnings report, the company also stated that it intends to submit an application for a new NCIB to repurchase up to four million shares as soon as its 2015 NCIB expires.

Third, it has a good dividend. WestJet pays an annual dividend of $0.56 per share, which gives its stock a yield of about 2.75% at today's levels. It is also very important to note that the company has raised its annual dividend payment every year since it began paying one in 2010, resulting in five consecutive years of increases, and I think its ample cash provided by operating activities will allow its streak to continue by announcing a slight increase before the end of 2016.

WestJet's ongoing share repurchases and its streak of annual dividend increases show that it's fully dedicated to maximizing shareholder value.

With all of the information provided above in mind, I think Foolish investors should strongly consider using the post-earnings weakness in WestJet Airlines to begin scaling in to long-term positions.

CATEGORY

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