



## Better Buy: Air Canada vs. WestJet Airlines Ltd.

### Description

Recently, Warren Buffett's **Berkshire Hathaway Inc.** (NYSE:BRK.A)(NYSE:BRK.B) announced it had purchased shares of three of North America's top airlines. Although it was likely one of Buffett's top lieutenants who made the purchase, it still sent a strong message to the market.

In total, Berkshire invested more than US\$1.5 billion in **American Airlines**, **United Continental**, and **Delta Air Lines**. Buffett also disclosed that Berkshire has begun accumulating **Southwest Airlines** shares.

By the time Berkshire is done buying Southwest, it could easily have 8% or 10% of its assets in airlines.

That's a big departure for Buffett, who is famously anti-airline. After a mediocre result investing in U.S. Airways in the 1990s, Buffett very publicly swore off the sector forever. Even if it wasn't Buffett directly who made the investment, it still speaks volumes. Many investors are now willing to take another look at the sector.

The nice thing about investing in Canada's airlines is the protection they offer. Both **Air Canada** ( [TSX:AC](#))(TSX:AC.B) and **WestJet Airlines Ltd.** (TSX:WJA) own the skies domestically, enjoying a comfortable oligarchy. They have a little more competition on international routes, but those are more than subsidized by domestic flights.

Which Canadian airline stock should you prefer? Let's take a closer look.

### The case for Air Canada

Air Canada shares are insanely cheap. It's the cheapest airline in North America on a price-to-earnings basis.

Over the last 12 months, Air Canada earned \$3.34 per share. That puts it at just 4.3 times trailing earnings. No, that's not a typo. It really is that cheap.

Analysts are bullish for 2017 too. A total of seven analysts cover the company; they expect it to

generate \$3.59 per share in earnings. Target prices are all over the map: one-year price estimates vary from a low of \$7.50 per share to \$25.

Recent results were strong. The company reported traffic growth of 18.9% on a year-over-year basis and operating income of \$896 million, an improvement of 10% versus the same period last year.

Growth looks good over the long term as well. Air Canada is a true international airline with routes all around the world. As people in places like China, India, and the Middle East get richer, they will travel more, coming to Canada either as tourists or to visit relatives that have immigrated here.

### **The case for WestJet**

WestJet is a terrific operator with a focus on costs. It has consistently posted costs of about 25% less than Air Canada on a per-mile-flown basis.

This advantage is mostly because of a couple of factors. WestJet has been able to keep unions out of its company, and it has a much simpler fleet than Air Canada. It only uses three different airplane models.

At least one of these advantages may be going away, however. WestJet pilots and flight attendants are again working on forming unions. Nothing is official yet, but organizations hoping to unionize each group of employees are making progress.

Because WestJet is substantially smaller than Air Canada, it still has growth potential in North America. It has also recently begun flying to Europe. It should also benefit from a global travel boom, although perhaps not as much as Air Canada.

Finally, WestJet has a terrific balance sheet. It has \$1.8 billion in cash, which almost offsets the \$1.9 billion it owes creditors. And because it is consistently profitable, it can pay investors a steadily increasing dividend. Shares currently yield 2.4%.

### **Which should you choose?**

For me, the verdict is obvious. Air Canada has a history of operational difficulties when times get tough. WestJet has historically navigated these times much better. WestJet also offers a solid dividend, a great balance sheet, and better growth potential.

Overall, I'm a WestJet man. But there is a case for buying Air Canada too, especially at today's valuation. Buying stocks at 4.3 times earnings isn't usually a bad idea.

### **CATEGORY**

1. Dividend Stocks
2. Investing

### **TICKERS GLOBAL**

1. NYSE:BRK.B (Berkshire Hathaway Inc.)
2. NYSE:BRKA (Berkshire Hathaway Inc.)
3. TSX:AC (Air Canada)

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**Author**

nelsonpsmith

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