



Will WestJet Airlines Ltd. Outperform or Lag its Peers Long Term?

Description

The question many investors have with respect to companies operating in industries dominated by a handful of companies or fewer (an oligopoly) focuses on how a specific company will perform over a given period of time relative to its peers.

Comparing a company to its peers is important to do in any industry; however, in industries with an oligopolistic structure, such as the Canadian airlines industry, comparing companies is even more important. Typically, one company will do well at the expense of the other. Thus, understanding the industry is almost as important as understanding the underlying business model of the company being analyzed.

In the case of **WestJet Airlines Ltd.** (TSX:WJA), it is true that the Canadian airline remains very cheap compared to its longer-term averages. With a five-year average price-to-sales multiple of 0.8, price-to-book multiple of 1.8, and price-to-earnings multiple of 11.4, the company's current valuation multiples of 0.6, 1.3, and 10.5, respectively, do seem cheap indeed.

Earnings growth has become the standard of late, with fuel prices declining and the airline taking advantage of an "unhedged" strategy in which the company earns more when fuel prices go down, as the company's earnings are not inhibited by [hedges](#) that would eat into current profits. Should fuel prices increase, however, WestJet may be seriously hurt as the profitability of the industry in general is linked closely to fuel price fluctuations over time.

Valuation aside, one of the most serious headwinds for WestJet of late has been the move by the airline's pilots to unionize. With unionization being a big deal in the airline industry, as pilots' unions typically demand whatever they want and get nearly whatever they want (an airplane can't fly without a pilot), indications that flight attendants may unionize have provided an additional headwind to this company. One of WestJet's main differentiation factors from **Air Canada** ([TSX:AC](#))(TSX:AC.B) has long been the company's anti-unionization structure. Many advertisements focus on the fact that WestJet pilots and flight attendants are "shareholders too."

Bottom line

When comparing WestJet to its larger peer Air Canada, one can make the argument that the lack of differentiation between the two firms should result in either a price increase in the case of Air Canada or a reduction in the stock price of WestJet, or both, given the fact that these airlines now have very similar operational structures. As such, I would recommend investors looking at the Canadian airline space consider a long-AC, short-WJA strategy to play the Canadian airlines, at least over the medium term.

Stay Foolish, my friends.

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Date

2025/08/02

Date Created

2017/07/04

Author

chrismacdonald

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