



Air Canada Surges With Better-Than-Expected 2nd-Quarter Update

Description

Air Canada's ([TSX:AC](#))(TSX:AC.B) shares rallied yesterday as the company significantly increased its guidance for the second quarter, saying that its earnings before interest, taxes, depreciation, amortization, impairment and aircraft rent, or EBITDAR, will be significantly better than current analyst expectations of \$475 million.

Driving this better-than-expected performance is higher revenue and lower fuel costs. Management highlighted a very strong Canada Day long weekend with over 930,000 passengers carried and lower-than-expected fuel costs.

This positive update on the upcoming second-quarter results follows a year of consistently beating expectations as the company continues to see a strong revenue environment (demand) and continues to impress with its cost-reduction initiatives. Management initially set a target to reduce its cost per available seat mile, or CASM, by 15% and is now tracking closer to a 21% reduction.

In the first quarter of 2017, for example, EBITDAR came in at \$342 million. This was 35% better than consensus expectations of \$253 million. Revenue increased 9%, and its CASM decreased by 6% to 11.6 cents.

Another key to the story is the company's cash flow and its free cash flow generation. This has not been an easy one to come by. After years of struggling, free cash flow in the first quarter of 2017 was \$470 million compared to -\$142 million in the same period last year.

So, going forward, Air Canada expects to continue to reap the rewards of the revamping of its operations. From its \$1.25 billion refinancing plan, which reduced the company's average cost of debt by 150 basis points, to actions such as fleet reconfiguration, the higher-density Rouge airplanes, and its investment in fleet modernization, management at Air Canada is still in the midst of transforming the airliner.

We are increasingly seeing the results of these changes, and we can expect to see more of the same in the coming years as the airliner continues its transformation. With the healthy consumer and the lower fuel prices continuing to cooperate, we can expect continued good times ahead.

The company will be hosting its Investor Day on September 19, at which time we will get an update on management's three-year plan and outlook. As analyst estimates get revised upwards in the coming week, the shares will be re-rated and better reflect the new and improved results and outlook. The key risks remain the economy and the strength of the consumer and fuel prices.

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