Will Airline Stocks Ascend to Start the Year?

Description

The aviation consultancy To70 released its Civil Aviation Safety Review for 2017 on January 2. It revealed that 2017 was the safest year in history for airline passengers. A senior aviation consultant stressed caution, attributing the numbers to good luck, but also stressed the incredible improvement in airline safety over the years.

In December, I'd discussed whether a plunging Canadian dollar could generate headwinds for airline stocks. Reduced purchasing power for Canadian travelers could feasibly eat into revenues in 2018. However, the loonie has started off strong so far. The Canadian dollar hit the $0.80 mark as North American markets reopened on January 2.

Air Canada (TSX:AC)(TSX:AC.B) stock rose 1.2% on January 2. Shares of the largest Canadian airliner climbed 90% in 2017 on the back of successive earnings beats and a year that saw record passenger traffic. However, the stock has been down marginally since releasing its third-quarter results on October 25. Air Canada posted record operating income of $1.004 billion and operating revenues of $4.88 billion in Q3 2017.

Air Canada is expected to release its fourth-quarter and full 2017 results on February 18. The extreme cold in North America has resulted in complications for airliners and passengers traveling during the holiday season. Air Canada also stands to benefit from U.S. tax reform that saw corporate rates slashed to 21% from 35%. The tax cut is estimated to raise corporate revenues by up to $6 trillion over the next decade. Air Canada sees over 20% of its revenues from the U.S.

WestJet Airlines Ltd. (TSX:WJA) rose 0.11% on January 2. The stock climbed 14% in 2017. In an October article, I'd compared WestJet and Air Canada and recommended the former. In the third quarter, WestJet reported net earnings of $138.4 million, or $1.18 per diluted share, in comparison to $116 million, or $0.97 per diluted share, in Q3 2016. Segment guests jumped 10.7% to 6.5 million in the quarter, and total revenues rose 8.1% to $1.21 billion.

The stock also offered a quarterly dividend of $0.14 per share, representing a 2.1% dividend yield. In early December, WestJet announced a partnership with **Delta Air Lines, Inc.** to pursue an ultra-lowcost carrier launch. The move will allow WestJet to compete with Air Canada in U.S. markets. Currently, WestJet sees about 16% of its revenues come from the U.S.

Tax reform will intensify competition for revenues between the two largest Canadian airliners in 2018, which is good news for shareholders.

CAE Inc. (TSX:CAE)(NYSE:CAE), a Montreal-based manufacturer of technologies and training services for airliners, is also an attractive option in 2018. Shares of CAE climbed 24% in 2017. CAE receives a whopping 36% of its revenues from the U.S., making it a very attractive target in light of tax reform.

In its fiscal 2018 second-quarter results, CAE reported revenue of $646 million compared to $635.5 million in the prior year. Operating profit also jumped to $109.3 million from $76.2 million in the second quarter of fiscal 2017. The company even announced a quarterly dividend of $0.09 per share with a 1.5% dividend yield.

With the global economy picking up steam, airliners will likely continue to see passenger traffic increase. U.S. tax reform may serve as a boon to these companies, which should draw in investors to start the year.

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Author
aocallaghan