A Stock So Cheap You Can't Afford Not to Own It!

Description

With the recent bout of volatility to start the year, it still looks like Mr. Market is having trouble pricing stocks with a high degree of efficiency. With sentiment trending lower of late, I think now is as good a time as any to be greedy, as there are plenty of value opportunities scattered across the TSX that are ripe for a bounce.

I believe **Air Canada** (TSX:AC)(TSX:AC.B) fits the bill as a stock that's trading substantially lower than its intrinsic value. Heck, the stock trades 3.49 times trailing earnings! I'm not sure one could ask for a cheaper multiple on the P/E front. It's so cheap that it actually looks like the stock may be a value trap where earnings are expected to fall off a cliff in order to correct the absurdly low P/E multiple.

I can tell you that Air Canada is no value trap, although traditional valuation metrics may indicate that the discount is too good to be true. There are many reasons why Air Canada has traded at such a huge discount, but given the recent Q1 2018 earnings beat and near-term catalysts on the horizon, I don't think any of these reasons are justifiable given the tremendous discount that shares trade at today.

For the first quarter, Air Canada clocked in a smaller adjusted loss per share at -$0.19, thereby beating analyst expectations of -$0.44. Despite the lower than expected losses, most of the concern was centred around the 16% rise in fuel prices, which dampened the 11.4% rise in traffic.

The increased operating expenses were to be expected, and given the immense cost-savings potential from initiatives like the insourcing of Air Canada's loyalty program, I think the perfect storm of expenses will be followed by immense savings come 2020 when the new loyalty program is launched. Moreover, the low-cost carrier Rogue will take to the skies this summer, and if it shows promise (and I think it will), Air Canada will be more than able to scale up effectively in order to meet the demands of budget-conscious customers relative to some of its smaller competitors.

Further, if fuel prices remain higher for longer, I think the downside is limited, especially when you consider that this is the main topic of discussion when it comes to the airlines of late. As such, higher fuel prices are already baked into shares and should the likely scenario of a fuel price pullback occur, I think Air Canada could easily double within the next two years.

Given the dirt-cheap valuation, it looks like the stock is misunderstood and is being unfairly shunned thanks to the extremely cyclical nature of the industry. Warren Buffett gave his stamp of approval on the airlines though. Will you?

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