WestJet Airlines Ltd. (TSX:WJA) Stock Is Down 50%: Now Is the Time to Buy its 4.5% Dividend

Description

WestJet Airlines (TSX:WJA) hasn't been flying high recently. Since late 2017, shares have been on a relentless decline, falling from more than $22 to just $12 today. The last time such a prolonged decline occurred was between 2014 and 2016, when shares bottomed out at around $10.

Following its bottom, the stock went on to double in less than 12 months. Can shareholders expect a similar 100% rise this time around?

The airline industry is hitting a rough patch

In early December, airline stocks experienced their biggest single-day loss in almost three years. While slowing economic activity was partially to blame, the biggest fear concerned falling oil prices.

Typically, falling oil prices are a boon to airlines, as the cost of fuel can represent 50% or more of their variable costs. When fuel prices fall, most airlines get the breathing room they've been craving for months or even years.

Historically, the airline sector has been a difficult one. The past few decades have been riddled with countless bankruptcies, and the long-term profit margin of the entire space trended close to 0%. Things have been changing, however.

This year, the International Air Transport Association (IATA) projects airlines to earn a record-breaking $38 billion in profits. This is quite the anomaly. In 2008, airlines lost a combined $5 billion, earning just $4 billion in 2011. While there are many factors involved, including more rational pricing and better capacity efficiencies, falling oil prices have given airlines billions in extra capital.

So, what's the problem here? Many savvy investors are worried that airlines will use this capital to overextend themselves — something they've done during many other boon times. If the majority of airlines add extra flight capacity, it can cripple industry profits for years to come.

In a nutshell, investors are worried that airlines won’t be able to help themselves, burning away the profits they’ve been yearning for to pursue growth at all costs. Some analysts, like Hunter Keay, who covers airlines at Wolfe Research, even think a recession would be preferable. “We trust airlines to react better to a recession than we trust them not to behave poorly with lower oil prices,” he wrote in a report.

Buy when others are fearful

The fears that have pushed WestJet Airlines down 50% aren’t new; they’ve happened many times before.

In 2014, oil prices peaked at nearly $100 per barrel, bottoming at around $30 per barrel in 2016. Shares of WestJet followed suit nearly symmetrically. Like many times before, these conditions provided a perfect buying opportunity. Shares doubled in nine months after oil prices rose to just $40 per barrel. Airlines, it seemed, had learned their lesson, refusing to add copious amounts of capacity to their networks.

There’s always a risk that airlines will return to their old habits, but it’s clear that the industry has taken a large shift. Warren Buffet was skeptical of airlines for decades — and for good reason. But in 2018, he told *Bloomberg* that he “wouldn’t rule out owning an entire airline.” How things have changed!

With recent pressures, WestJet now pays a 4.5% dividend — its highest levels in years. Getting paid nearly 5% to wait out the rough patch isn’t a terrible problem to have. Once investors realize that the industry will stay rational, as it has proven capable of during recent times of turmoil, look for WestJet stock to rebound sharply.

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