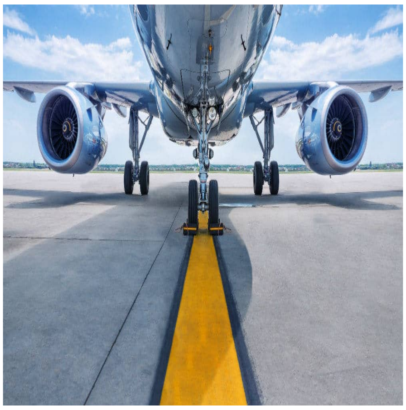

What's Next for Air Canada (TSX:AC) Stock?

Description

The last month hasn't been good for **Air Canada** (TSX:AC)(TSX:AC.B) stock. Shares are down more than 50% over the last 30 days and more than 70% versus the 52-week high set in January.

Everybody knows why Air Canada stock has suffered so much, of course. The coronavirus has caused worldwide travel to virtually grind to a halt. Domestic flights are still happening here in Canada, but most folks are choosing to stay home. And the only international flights coming to Canada are bringing folks home from abroad.

The company has responded by cutting costs to the bone. Most aircraft are now grounded, and non-essential staff have been laid off. Capacity is expected to decline by 85-90% in the next quarter compared to the same period last year. Air Canada is also in the process of drawing down all its available credit lines — a process that should add $1 billion in cash to the company's accounts.

Another piece of good news for Air Canada stock is, the company should be able to participate in the federal government's wage-subsidy program — something that will allow the company to retain staff while the federal government temporarily helps with paying wages.

But will this be enough to keep the company afloat? And what will happen to Air Canada stock in the next few weeks? Let's take a closer look.

Does Air Canada need a bailout?

Let's take a second to take a closer look at Air Canada's balance sheet to try and determine how much cash the company has.

At first glance, it looks to be pretty good. At the end of 2019, Air Canada had more than $7 billion in current assets — things like cash, short-term investments, receivables, and inventory. Even if we exclude receivables and inventory, the company's cash and short-term investment balance was approximately $6 billion.

Investors must remember the company generated free cash flow for the first two months of the year — something that would have added to the cash pile. And Air Canada just added $1 billion to that amount by drawing down its available credit lines.

Unfortunately, the company also has significant short-term costs as well. Current liabilities were close to $8 billion at the end of 2019, and there are a lot of folks who are getting refunds for tickets that were booked months ago. In other words, much of the cash is going out the door as refunds. Sure, many people will end up re-booking in a year or three, but that doesn't really help shareholders who are looking at the next few months.

All of this translates into an unfortunate reality. I think the company will end up needing a bailout. And if that happens, how will Air Canada stock be impacted?

Nobody really knows, of course. The government could end up helping the entire sector with loans to get the big operators through this mess. Or it could insist on an equity ownership position that essentially wipes out current shareholders. Remember, that's what happened with the big car companies back in 2008-09.

Air Canada stock currently trades hands at around $16 per share. That indicates investors think there's some value here. The market is betting there's a good chance the company will get a bailout that benefits current shareholders. After all, shares are up significantly over the last few days. But at this point, nobody really knows the details.

The bottom line

If you have the ability to see into the future and see what kind of bailout Air Canada will end up getting, then invest in the company.

If you're like the rest of us and have no idea what the aid package will eventually end up looking like, I'd exercise a lot of caution around Air Canada stock. It's a risky gamble, but one that could end up paying off big time.

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