



TFSA Investors: Is Air Canada (TSX:AC) a Buy Before the Economy Recovers?

Description

As a TFSA investor with plenty of cash on the sidelines, you should welcome market crashes with open arms, because they allow you to pay less and get more of the wonderful businesses on your radar.

[Air Canada \(TSX:AC\)](#) (TSX:AC.B) stock has arguably been one of the most compelling deep-value plays following the coronavirus-induced stock market crash. While the TSX Index fell just over 37% from peak to trough, Air Canada stock nosedived over 75%. On a peak-to-trough basis, shares of the Canadian airline got cut in half, twice!

Air Canada and the airlines live up to their dangerously cyclical reputation, again

Just because a stock is “cheap” based on historical valuation metrics doesn’t mean that it’s undervalued, especially given the profound operational disruption caused to the airline industry. The airlines, as you may know, have a reputation for folding during times of economic hardship. Their extremely cyclical nature combined with high fixed operating costs makes them look like government bailouts just waiting to happen.

Over the last few years, though, Air Canada and many of its peers have meaningfully improved their fundamentals. Heck, you could even say they’re now economical enough to ride out recessions and are independent enough to survive over the long run. Had this economic downturn not been caused by a pandemic, I’m pretty sure Air Canada wouldn’t be in nearly as much turmoil as it’s in right now.

Yes, another government bailout for the airline industry does not look good for airline stocks as an investment. In the grander scheme of things, however, I think this coronavirus crisis could be the last time that the airlines line up to receive their bailouts, even if another pandemic causes lockdowns and travel restrictions across the board. Why?

Not only do low jet fuel prices and more fuel-efficient aircraft (eventually, the **Boeing** 737 MAX will

regain the confidence of the airlines) bode well for the long-term margins of the airlines, I think the industry has learned an invaluable lesson after the latest crisis that will make them more investible in the future.

As you may know, airlines are swelling with profits when times are good. And they're going to become even more profitable come the next economic upswing given the margin-expanding tailwinds I just described. The low-single-digit price-to-earnings multiples of the airlines are all too common, and many investors (other than Warren Buffett) look away because they know the P/E ratio will mean nothing once the next inevitable economic downturn hits.

The real issue with investing in airlines like Air Canada is that they're just sitting ducks waiting to be shot down by the next inevitable economic downturn. Liquidity dries suddenly dries up, and their financial health quickly diminishes. Where did all the cash go from those years of substantial profitability?

Making the airlines investible again

Massive amounts of cash have been wasted on share repurchases over the years. Air Canada clawed back around \$800 million of its own shares since 2015 and, believe it or not, that's a modest amount compared to some of the U.S.-based airlines that had multi-billion-dollar share-repurchase programs.

Given the high degree of public scrutiny over the "wasted" money on airline buybacks of late, I think the days of such massive airline buybacks are coming to an end. And in its place is a massive rainy-day cash pile similar to the floats of insurance companies.

Insurance companies always have cash on hand for when crises hit, and given the airlines are in a crisis every decade or so, it's about time for the airlines to have something similar, so they're liquid enough not to be at high risk of bankruptcy every time a recession hits.

With such assurance, airline stocks like Air Canada will suddenly become a staple (and not a value trap) for TFSA investors. Air Canada is more liquid than prior to the Financial Crisis. Come the next crisis, I think it'll be even more liquid — so much so such that nobody will even bring up the thought of bankruptcy, regardless of what the next crisis entails.

I'd buy Air Canada here and [hold it for the long haul](#), as its taboo fades over the years.

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