Buy the National Airline Air Canada (TSX:AC) Today

Description

Airlines are among the stocks most harshly impacted by the coronavirus pandemic. The Canadian flag carrier **Air Canada** (TSX:AC) has lost a whopping 63% since the start of 2020. There is growing speculation that it will be a difficult road to recovery for airlines. Government travel bans and border closures will impact travel and tourism for years to come. That has sparked conjecture that airlines are a poor investment, despite many appearing attractively valued. Air Canada's considerable potential coupled with its strong brand as the national flag carrier make it an attractive contrarian buy after suffering such a huge loss in market value.

Strong performance

Air Canada finished 2019 on a particularly strong note. It reported record operating revenue of $19 billion and unrestricted liquidity of $7.4 billion.

Impressively, Air Canada achieved those robust results with 25% of its fleet grounded because of the safety issues surrounding the **Boeing** 737 MAX. There is every indication that earnings will rebound toward the end of 2020 once the impact of the coronavirus pandemic is quantified.

Reducing costs and boosting liquidity

Air Canada has executed measures to manage the impact of the coronavirus on its operations. These include implementing a company-wide cost-reduction program. After reducing capital spending, this program will reduce overall expenses by around $500 million. This coupled with the furloughing of 16,000 employees and executive pay cuts will significantly reduce costs. Sharply lower oil will also benefit Air Canada, reducing the cost of fuel, which, after labour, is the second-largest operational expense.

Air Canada also boosted its liquidity by $1 billion, which, on top of its solid balance sheet, further enhances its ability to survive the coronavirus pandemic.

Robust fundamentals

The strength of the carrier's balance sheet is evident from its full-year 2019 results. Air Canada finished the year with $2 billion in cash and $3.8 billion in short-term investments. That is compared to total long-term debt, leases, pensions, and maintenance provisions of $15 billion.

This is a manageable two times annual net operating cash flow and three times EBITDA. The addition of $1 billion in liquidity will further strengthen Air Canada's short-term position.

While Air Canada will suffer from a cash crunch as revenues dry up and earnings decline, it won't be enough to push the airline into bankruptcy.

There is every indication that as the national flag carrier, Air Canada, if required, will receive a bailout from Ottawa. Initial signs are that the strength of Air Canada's financial position means that it won't need a bailout. It should be recognized that government bailouts are unpredictable, making such an event uncertain.

Positive long-term outlook

After the September 2001 U.S. terrorist attacks, it took roughly two years for air travel to return to normal. After the coronavirus pandemic, it may take even longer, but it will occur. Air Canada is uniquely positioned to capitalize from the tourism and travel recovery when it occurs.

Unlike the U.S. airline industry, there is significantly less competition in Canada. That, along with the strength of Air Canada's brand and status as the national flag carrier, endows it with a robust economic moat.

Foolish takeaway

If you had of bought Air Canada 10 years ago at the end of the last major bear market, you would have earned a return of 713%, even after the last price crash. That equates to an impressive compound annual growth rate (CAGR) of 23%. After the latest sharp decline in Air Canada's share price, there is every indication that it will generate similar long-term returns, although past returns are no guarantee of future performance.

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mattdsmith