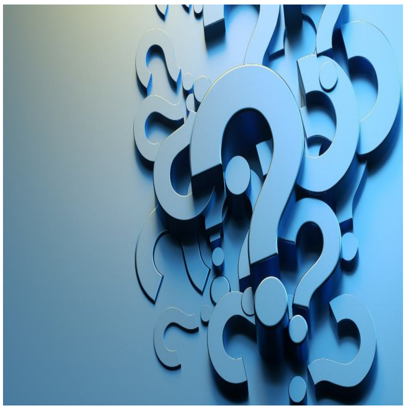
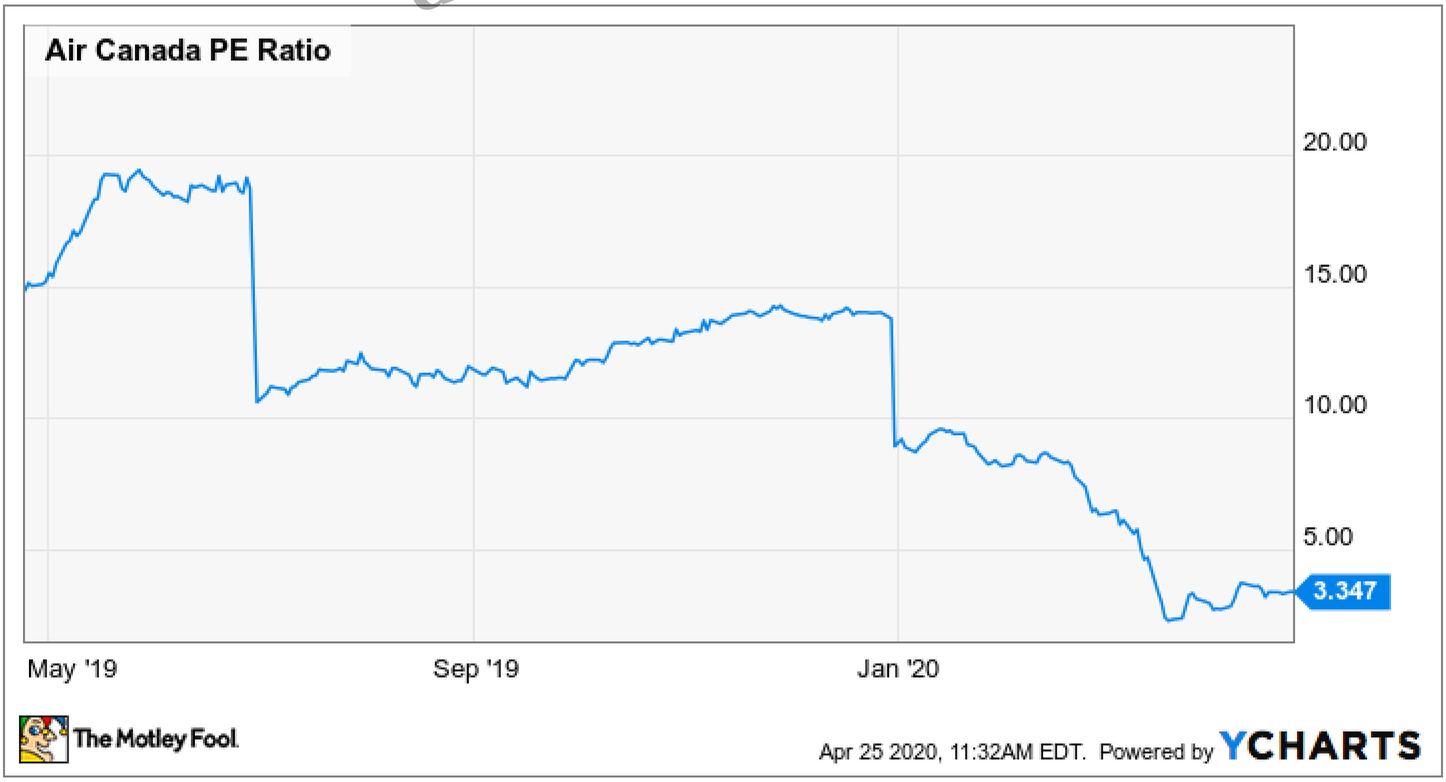


Is Air Canada Stock Too Cheap to Pass Up?

Description

Shares of **Air Canada** (TSX:AC) closed at a little over $18 on Friday. Prior to this year's market crash, the last time you'd be able to buy the stock at the price would've been 2017. The stock's currently trading at 3.4 times its earnings over the trailing 12 months.

While earnings will certainly look a lot different over the next 12 months as a result of the coronavirus pandemic, it puts into perspective how cheap the stock is, especially assuming that things will return back to normal, perhaps in a couple of years. Here's how that ratio's looked over the past 12 months:



AC PE Ratio data by YCharts

Investors have been willing to pay nearly 20 times its earnings when the economy was looking strong.

Why the stock could soar much higher

One of the reasons to be bullish on Air Canada right now is that oil prices are struggling as a result of a significant excess supply in the markets. Excess supply is a problem that's not new to oil and gas — and it's the reason the commodity price first started to crash back in 2014.

It was an issue then and it's a much bigger problem today. It's likely that in a few years, Air Canada and other airline stocks will continue to benefit from low oil prices, setting them up for some significant profits later on, making Air Canada an appealing investment to hold right now.

Does the company have enough cash to survive the pandemic?

There's little doubt that once things return to normal in the economy, airline stocks could surge — but getting to that point is a problem. It could take a year for us to see some normalcy again, but a safer bet would be to estimate that it'll take at least two years.

In order to weather that storm, a company is going to need some strong financials to get through that — as well as perhaps support from the federal government. As of the end of 2019, Air Canada had more than $2 billion in cash. Combined with short-term investments, that total came to $5.9 billion.

The company has had no problem generating positive cash flow from its operating activities. The company hasn't generated positive free cash flow in only three of the past 10 years.

With operations likely minimal over the next year and the company shedding many costs, burning through $1 billion is unlikely. It's also unlikely the government would just sit idly if Air Canada were to struggle to stay afloat.

Odds are that Air Canada will get through the pandemic and likely recover.

Bottom line

There's no question there's a lot of risk investing in Air Canada today. However, there are more reasons to buy the stock than there are *not* to. But this is not a short-term investment opportunity. Air Canada's shares may not increase in the next few weeks or months — it's possible they could even decline further.

But for investors who are okay with waiting for the economy and Air Canada to recover, their returns could be significant a few years from now.

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