



To Save or Not to Save Air Canada (TSX:AC)?

Description

Government bailouts of distressed companies have always been a sensitive issue. If a government spends billions of dollars, taxpayers will have to carry the burden. The COVID-19 pandemic [paralyzed the global airline industry](#) in 2020. **Air Canada** ([TSX:AC](#)) is facing bankruptcy if no federal aid comes soon.

Finally, the administration of Prime Minister Justin Trudeau is offering the Large Employer Emergency Financing Facility (LEEFF). Canada's flag carrier and giant airline company could qualify for this new loan program. Air Canada has yet to announce if it would avail of the LEEFF.

Pre-corona performance

Before the coronavirus outbreak, Air Canada is boasting of 27 consecutive quarters of operating revenue growth. In 2019, the company's full-year performance was mighty impressive too.

Air Canada posted a record \$19.13 billion in operating revenues and operating income of \$1.650 billion. EBITDA was \$3.636 billion, while EBITDA margin stood at 19%. Furthermore, last year saw a record unrestricted liquidity of \$7.380 billion.

Notwithstanding the grounding of its Boeing 737 MAX fleet, Air Canada was able to meet and deliver all vital financial metrics goals for the year. In the past decade, investors were more than happy with the 2,085.14% total return.

There was even a 1.8% capacity increase plus record \$17.23 billion system passenger revenues. However, COVID-19 blew Air Canada out of the sky in the first quarter of 2020.

Sudden reversal

The current narrative of Air Canada is entirely different. With [travel demand collapsing](#) due to travel restrictions and social distancing, capacity is down by 90%. Also, the company reported a \$1 billion

loss and \$1.3 billion increase in net debt following the drawdown on its available credit lines.

Air Canada will have no wings anymore if the bleeding continues — it needs a lifeline fast. The 75% wage subsidy by the federal government came in the nick of time. Companies with more than 30% drop in revenue qualify for the program. Air Canada can apply for the money to recall 16,500 laid-off employees.

Strings attached

The LEEFF is similar to the US\$25 billion loan aid package the U.S. is offering to American airline companies. According to the Prime Minister's office, the loan amount starts at \$60 million. To qualify, companies must have at least \$300 million in annual revenues. Air Canada could be eligible, but not the smaller carriers.

However, the financial assistance program has conditions or strings attached to it. It bars airline companies from paying dividends, doing stock buybacks, or using the funds to pay executives.

Companies applying must preserve employment and maintain investment activities. Similarly, there must be a demonstrated commitment to respect collective bargaining agreements and ensuring the protection of workers' pensions.

Baseline scenario

The bridge financing will allow larger companies to continue operating, but with a drawback. Air Canada will accumulate more debts and pay back the loan from earnings down the road.

Air Canada is a job creator and an economic driver in the country. While the LEEFF will serve its purpose, don't expect a quick rebound. Industry experts see that travel will return to normal by 2023.

This baseline scenario could move until 2024 if there's another wave of the virus or an extension of lockdowns.

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