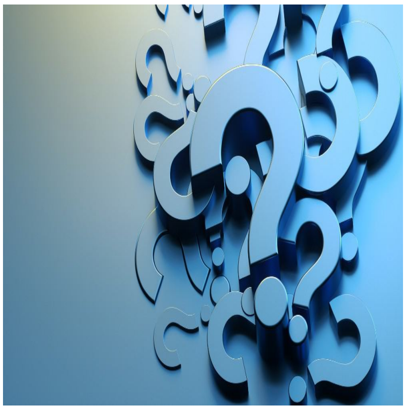

Will Air Canada (TSX:AC) Stock Zoom Past $20?

Description

Air Canada (TSX:AC) used to be a millionaire-maker stock. In 2012, shares were priced below $1. At the start of 2020, they were above $50. A $5,000 investment became $250,000 in less than a decade.

Yet the coronavirus has taken a troubling toll. Now valued at $16 apiece, Air Canada stock is stuck near multi-year lows.

Market sentiment has never been lower for airline stocks. Past recessions and disasters were difficult to stomach, but the COVID-19 crisis could see *dozens* of airliners go bankrupt. We may be looking at a dying industry, at least in terms of the current investor base.

Many airline stocks will eventually go to zero. Others, meanwhile, look like terrific investments. That's because the number one driving force industry profits is *consolidation*. As competitors exit the market, surviving incumbents can gobble-up market share. While the overall pie may be smaller for years to come, some companies will command a significantly larger slice than before.

If Air Canada can withstand the downturn, share should eventually zoom past the $20 mark.

Airlines are difficult

Warren Buffett is arguably the best investor of all time. Following his advice is prudent. What does the Oracle of Omaha think of airline stocks?

In 2007, he wasn't a fan. "If a far-sighted capitalist had been present at Kitty Hawk, he would have done his successors a huge favor by shooting Orville down," Buffett famously wrote in a shareholder letter that year.

Buffett's biggest complaint was that airlines consistently built too much capacity, flooding routes with too much supply, making it difficult for anyone to profit long term. According to Buffett, these companies were "attracted by growth when they should have been repelled by it."

This thesis was largely true, even for Air Canada. Before the company's incredible run this decade, shares sank from $20 in 2006 to $0.90 in 2009, a rapid destruction of shareholder value.

"Historically, airlines have gone bankrupt a lot," highlights the *Intelligencer* magazine. "Airlines have huge upfront costs to buy airplanes and build networks, then they compete fiercely on price, which pushes profit margins down to a level that can't support those capital investments, especially through economic downturns when demand for air travel dips."

Buy Air Canada stock?

Despite Buffett's historical opposition, he began *buying* airline stock in 2014. Last year, he was a major shareholder in four different airlines. What changed?

In recent years, competition finally grew rational. Capacity additions were kept under control, reducing oversupply. All of this was made possible through industry consolidation. Today, four companies control 80% of the domestic U.S. market. In Canada, just two firms dominate: Air Canada and WestJet.

The secret to airline success is clear. If you want to profit, buy as the industry consolidates. Due to the coronavirus, that dynamic could happen on an unprecedented scale. Most competitors have already dramatically reduced expansion plans. Several will eventually go bankrupt.

As the largest operator in Canada, Air Canada has an opportunity to thrive long term. The market opportunity will be smaller for years to come, but the company should seize a larger market share. After conditions normalize, the company will likely *keep* those market share gains.

This should prove a volatile investment. No one knows how the next few months will shake out. But if you're willing to bet long term on the value of rapid industry consolidation, Air Canada stock should top your buy list.

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