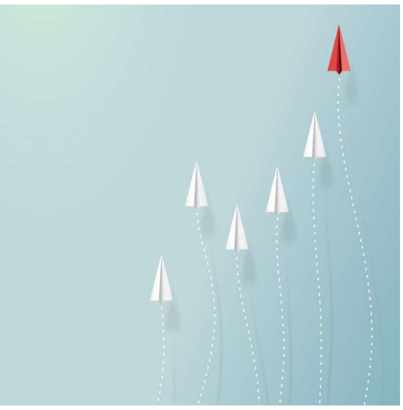

Forget Air Canada (TSX:AC): This Stock Has More Upside

Description

Air Canada (TSX:AC) is a popular pick these days. At the start of the year, shares were valued at $50. After a steep and dramatic plunge, the stock price is now $16.

It's no wonder why growth and value investors alike are snapping up shares. In the eight-year period preceding the COVID-19 crisis, the company's stock rose by nearly 5,000%. The current valuation looks like a steal.

Air Canada may be a profitable investment, but it's not necessarily the best stock pick in the airline industry. It has name recognition, but lesser-known competitors could have significantly more upside. In fact, one stock in particular could ultimately *benefit* from Air Canada's resurgence.

If you want to bet big on high-upside airline stocks, take a close look at **Chorus Aviation** (TSX:CHR).

A perfect partnership

You're forgiven if you've never heard of Chorus Aviation. The firm has a market cap of $460 million. Air Canada, for comparison, is worth $4.2 billion.

But size isn't the only factor causing Chorus Aviation to fly under the radar. Its business model is purposefully built to not be seen. That's because the company operates as a shadow carrier, operating routes under the banners of bigger companies.

Chorus Aviation has two subsidiaries: Jazz Aviation and Voyageur Airways. But you can't book a flight directly through them. You may have flown with them before without even knowing it. That's impressive considering the company transports 11 million people every year across Canada through 25,000 flights.

One of Chorus Aviation's biggest partners is actually Air Canada, which operates a vast network of routes throughout the country. Jazz Aviation, a subsidiary of Chorus Aviation, services many of the smaller regional routes, all under the guise of Air Canada Express.

This is a fantastic business to be in. Air Canada essentially contracts out its routes to the company, splitting the revenue. Chorus Aviation can take advantage of Air Canada's reach and brand power, while Air Canada can expand more aggressively without dedicating their own resources.

Better than Air Canada?

What makes a Chorus Aviation a better buy? Two factors: valuation and future prospects.

Today, CHR stock trades at a 25% *discount* to its book value. Over the last five years, however, the valuation has averaged a 260% *premium* to book value. It's easy to determine that shares are trading at fire-sale prices.

Air Canada is also trading at a discount to its historical average, but the current trading range isn't nearly as compelling. Today, AC stock trades almost exactly at book value, while over the last five years, it averaged several times that figure.

So, should you buy Air Canada at book value or Chorus Aviation at a 25% discount to book value? Both may be bargains long term, but if I had to choose one stock, I'd pick CHR.

For years, large airlines will remain cost conscious. They'll go to any means possible to preserve cash flow. Contracting routes to Chorus is a low-risk way to cut costs quickly. Air Canada, for example, can keep its large network running without fronting the cost of aircraft and crew.

Shadow carriers like Chorus Aviation should experience greater demand in the years to come given they provide much-needed operating flexibility. If you want to bet on a flailing airline industry, this looks like your best bet when it comes to the risk/reward payoff.

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