Forget Air Canada (TSX:AC): Buy This Diversified Airline Stock Instead

Description

Many retail investors are invested heavily in **Air Canada** (TSX:AC), steadfast in their belief Canada's largest airline stock will recover. People will fly again. It's only a matter of time.

But an investment in Air Canada isn't nearly that simple. If air travel bounces back quickly, Air Canada shares should be a solid short-term investment. But what if they don't? The airline stock could struggle for years if numbers don't come back.

Remember, flying is most efficient if the plane is full. Air Canada will struggle if it's forced to fly with half-empty planes, something governments could force on the industry to help keep passengers safe.

Ultimately, most investors don't know what the air travel world will look like six to 12 months from now. Yes, Air Canada just raised a bunch of cash via equity and debt offerings, but nobody really knows if the fresh $1.6 billion in the company's coffers will be enough to make it through this storm.

Investors looking for airline stock exposure might want to take a different approach. Let's take a closer look at how you can do this, a move that could very well end up as a safer way to play this volatile industry.

Remember Westjet?

Many investors promptly ignored Westjet after the company was acquired by **Onex Corporation** (TSX:ONEX). These folks — myself included — were disappointed an excellent Canadian airline stock was no longer available for investment.

But perhaps investors should look at things a little differently. An investment in Onex today gives them substantial airline exposure as well as a whack of other assets.

As I type this, Onex shares trade at approximately $67 each, recovering nicely from March's lows of below $40 per share. The stock is still down a little bit from the $80-$90 range shares traded at back in January and February, but long-term holders have to like the recovery.

Onex is essentially two separate businesses. The first part uses shareholder capital, outside money, and debt to make investments in both public and private companies. Westjet is one of the largest positions, but it's certainly not the whole company. Onex has stakes in dozens of investments.

The other part of the company is asset management. How this works is relatively simple. Onex uses its own cash to begin a private equity fund. It attracts other investors to the fund. It then collects management fees on the outside investments. This part of the company has grown substantially, and recently surpassed $300 million in annual revenue.

The investment case

Onex is a compelling investment on a sum-of-the-parts basis.

At the end of the first quarter, Onex's investments were worth a little more than $77 per share. Remember, that was when the market had barely recovered from the bottom and investors were incredibly pessimistic. The value of the portfolio — including the stake in Westjet — has undoubtedly recovered even further.

Remember, shares currently trade hands at just over $67 each, so investors are buying at a nice discount to the sum of the parts.

There's also the asset management business. That part of the company earned $80 million in profits in 2019 and is growing nicely as assets under management increase. If we value it at just 10 times earnings, that's an extra $800 million. There are approximately 100 million shares outstanding, which adds an additional $8 per share to our valuation.

Add it all together and this quasi-airline stock is worth approximately $85 per share on a conservative basis. Investors can buy today at $67 per share — a discount of more than 20% of the parts.

The bottom line on this airline stock

The beautiful part of Onex is that it allows investors access to the airline sector without putting all their eggs in that volatile market. They're also getting an interesting opportunity on valuation perspective. It's nice to buy assets for less than what they're worth.

Add in Onex's consistent share repurchases, its steady dividend, and its sharp management team and it combines to be a pretty compelling investment thesis. It sure looks a lot better than simply buying a risky airline stock and hoping for the best.

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