



## Air Canada (TSX:AC) Stock: Is a Bailout Coming?

### Description

**Air Canada** ([TSX:AC](#)) stock is [surging](#). On March 19, shares were \$12. Today, they're above \$18. That's a 50% spike in just three months.

But long-term investors aren't very excited. Before the coronavirus pandemic, the stock traded above \$50 per share.

Still more than 50% off its pre-pandemic highs, analysts are split on what will happen to Air Canada. In some scenarios, we experience a return to normal and shares skyrocket higher. In other scenarios, the business goes bankrupt.

There is a chance, however, that the future lies somewhere in the middle. The airline may not go bankrupt, but it might need a sizable government bailout.

### A bailout is coming

Owning planes isn't cheap. Maintaining and storing planes is similarly expensive. To justify this cost, airlines like Air Canada need to fly at full capacity, or pretty close to it. Even at 90% capacity, airlines find it difficult to make money.

This is a difficult industry. Profits are so elusive that legendary investor Warren Buffett avoided it at all costs for decades.

"The airline business has been extraordinary," Buffett told *The Telegraph* in 2002. "It has eaten up capital over the past century like almost no other business because people seem to keep coming back to it and putting fresh money in. You've got huge fixed costs, you've got strong labor unions, and you've got commodity pricing. That is not a great recipe for success."

You can likely connect the dots here. The COVID-19 situation caused airlines to cut capacity *immensely*. Last quarter, Air Canada slashed 95% of its capacity. Competitor **Delta Airlines** reportedly lost \$50 million every day.

The only way for airlines to plug this cash burn is to sell debt or equity. But most companies are maxing-out their debt capacities, meaning they're selling stock on the open market at fire-sale prices.

"Airline balance sheets are getting stressed with more debt, and equity values are being diluted as carriers issue more stock," [reports Barrons](#).

Air Canada has been forced to follow suit. The business lost more than \$1 billion last quarter. This quarter should result in additional losses. We should see more stock and debt issuances shortly, but eventually, the market will call it quits.

At today's cash burn, the company may have less than five quarters of liquidity.

## Bet on Air Canada stock?

Unless conditions improve dramatically over the next few months, a government bailout is almost guaranteed for Air Canada. The business is responsible for nearly *half* of Canada's domestic air traffic. It employs tens of thousands of people. The government has a vested interest in making sure operations continue without disruption.

Should you take a bet on AC stock? It depends on your risk tolerance.

During the financial crisis of 2008, dozens of companies received bailout funds in the U.S. and Canada. Some were terrific investments. **Bank of America** stock, for example, has risen 500% since 2009. Many businesses, however, ultimately went to *zero* despite receiving government support.

Betting on Air Canada right now is a roll of the dice. While bailout funds seem inevitable, the timing and terms are completely unknown. Unless you're looking for a high risk, high reward opportunity, steer clear of shares.

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