# Now Isn’t the Time to Buy Air Canada (TSX:AC) Stock

## Description

Despite its long-term downward trajectory, **Air Canada** (TSX:AC) still has many fans. When a stock falls precipitously, dip buyers take notice, and AC has been getting a lot of attention from that group. Down more than 60% year to date, it certainly *looks* like a classic contrarian play.



But looks can be deceiving. While AC has fallen in absolute terms, it’s actually gotten far more expensive relative to earnings. The company’s massive $1.05 billion net loss in the first quarter was larger than any of the profits in the three prior quarters. As a result, trailing 12-month earnings are down, and the P/E ratio is up.

For the previous 12-month period, Air Canada earned $82 million. In the three quarters prior to Q1, the company posted profits in the $100-$350 million range. So, we’re now looking at 12-month earnings lower than previous single quarter earnings.

Of course, Air Canada’s earnings won’t stay this low forever. At some point, the company’s operations will resume, and earnings will get back to 2019 levels. However, the company projects it will take a full *three years* for that to happen. Take a protracted recovery and add equity dilution on top of that, and you’ve got a recipe for continued losses.

# Second wave

One of the biggest reasons Air Canada keeps heading downward is because it’s facing innumerable risks. One of the biggest is a second wave of COVID-19. Recently we’ve seen COVID cases spike in U.S. states like Texas, California, and Florida. A similar but more muted uptick in cases has been occurring in Ontario.

Lately, Air Canada has been lobbying the government hard to let it resume international routes. Unfortunately, if the “second wave” continues, then the government probably won’t give the company what it wants.

## Equity dilution

Another big concern for Air Canada is equity dilution.

In the first quarter, Air Canada revealed that it was bleeding cash, losing $1.05 billion and seeing its revenue decline. Because so many of its flights were grounded, the company couldn't pay for operating expenses. To keep itself afloat, AC raised $1.6 billion in debt and equity. The equity issue increased the number of shares outstanding. So, now Air Canada has a larger number of shareholders owning a shrinking amount of earnings. The value underlying each AC share is much lower than it was just months ago as a result.

## Foolish takeaway

When a big stock takes a dip, it's tempting to buy — doubly so when the underlying company is an indispensable service that society couldn't get by without. If it really came down to it, the federal government would probably step in to help Air Canada. Without it, the country would not have a truly international airline.

Unfortunately for shareholders, that doesn't make AC a buy. The fact that a company will probably survive doesn't mean it will thrive. AC is a stock that's been massively diluted, while earnings are down and not likely to recover for three years. This stock is just not a great value at the moment.



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