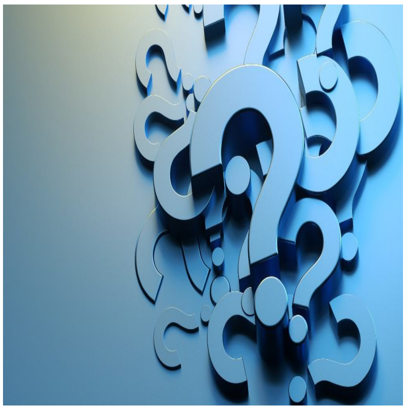

Is Air Canada a Millionaire-Maker Stock?

Description

Air Canada (TSX:AC) stock is under pressure once again, falling 4.2% on Tuesday alongside its U.S. peers, as summer travel recovery hopes are fading with rising COVID-19 cases across various states south of the border.

Here in Canada, COVID-19 outbreaks haven't been anywhere near as drastic. However, the risk of contracting the virus on a domestic flight is still a possibility, and with government-mandated travel restrictions a possibility later in the year, investors are going to need to brace themselves for what could be another several months' worth of turbulence.

Air Canada and the airlines may not hold their March lows

In many prior pieces, I warned investors that Air Canada was an all-or-nothing spec bet — and that only those with strong stomachs and a long-term horizon should even consider owning the name with a portion of their COVID-19 "barbell" portfolios.

Unlike the broader stock market, which is unlikely to retest its March lows because of backing from central banks like the U.S. Fed, the airline recovery story could still stand to deteriorate with time depending on how much worse this horrific pandemic becomes.

The airlines simply don't look like very economical businesses in a pandemic, with considerable fixed base costs, thinning margins, and a nosediving top line.

Sure, airlines could reduce capacity by not cramming passengers onboard every plane like they're fish in a can of sardines to improve upon the safety factor. But with socially-distanced passengers every few seats or so, it may not be worthwhile for an airline even to bother getting planes on less profitable routes in the air, even without government-mandated restrictions.

Turbulent times likely ahead for Air Canada

Just over a week ago, Air Canada announced that it's halting 30 domestic routes that have suffered from weak travel demand due to the pandemic.

With so few passengers on select flights, the airline would stand to lose money, thus decreasing its chances of surviving the COVID-19 crisis. The move, while criticized harshly by the likes of Canadian Prime Minister Justin Trudeau, is likely the right course of action given the dim recovery trajectory for the air travel industry and the fact that Air Canada's liquidity reserves won't last forever.

In a bear-case scenario, even a highly liquid airline like Air Canada could be at risk of falling substantially in price — perhaps to the low single digits — as air travel traffic could implode further at a magnitude proportional to the severity of COVID-19 outbreaks across the country.

Government-mandated restrictions or not, Air Canada will be fighting for its life as long as COVID-19 is still lingering out there.

Don't bet against the advent of an effective vaccine

That said, Air Canada could prove to be undervalued beyond proportion if an effective vaccine were to land within the next year. If Air Canada ultimately survives this crisis (and I think it will) and an effective vaccine lands, AC stock will deserve to trade at a multitude higher than its current 1.1 times book multiple.

While it's difficult to gauge the vaccine timeline, one can't discount to progress made in recent months. At the time of writing, there are 29 COVID-19 vaccines between phase one and phase three clinical trials, with one approved for limited use in China just last week.

Foolish takeaway

Should an effective vaccine be approved out of the blue, Air Canada stock could easily find itself more than tripling back to the $50 levels.

But until then, AC shares are too risky a bet for all but the most fearless of long-term investors who are bullish on the advent of a COVID-19 vaccine.

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