Air Canada (TSX:AC) Plunges 6% on Earnings — Buy the Dip or Bail Like Warren Buffett?

Description

Air Canada (TSX:AC) nosedived 6% after a weaker-than-expected earnings report that saw a massive $1.7 billion loss, marking the second consecutive quarter of losses amid the COVID-19 pandemic. Management pointed the finger at government-mandated travel restrictions (really no surprise here), also noting that Canada's restrictions were "among the most severe in the world."

Air Canada: More turbulence ahead

The Canadian airline derives a huge chunk of its normalized revenues from international flights (just 42% of 2019 revenues were from domestic or transborder flights). So, it's not a surprise to see Air Canada take yet another big hit to the chin amid the pandemic that could easily worsen before an effective vaccine arrives.

Despite clocking in yet another brutal quarter, Air Canada continues to do its best to keep rolling with the punches.

"Without government industry support as travel restrictions are extended, we will look at other opportunities to further reduce costs and capital, including further route suspensions and possible cancellations of… aircraft on order," said Air Canada CEO Calin Rovinescu in a call with analysts.

Air Canada's management has done a decent job given the horrific hand they were dealt

The company has already done an exceptional job of improving its chances of survival, with capacity cuts, reduced cash burn rates, and ample liquidity raises. With a greater liquidity positioning and far less leverage than its airline peers south of the border, Air Canada looks like the most prudent investment in playing the gradual recovery of the air travel industry.

Despite Air Canada's superior financial footing, the company's large international exposure could mean that it will the slowest to rebound if the global economy has to live alongside the coronavirus for an extended period, with on and off social-distancing practices and travel restrictions depending on the severity of COVID-19 cases at any point. Indeed, Air Canada is a play on the advent of a coronavirus vaccine.

Fortunately, Air Canada's solid liquidity position buys the company enough time to continue riding out the storm. Many pundits see an effective vaccine being ready for broad distribution at some point in 2021 (possibly in the summer).

Even if it takes until late 2021 to get people vaccinated, I see Air Canada surviving on its own, as it continues doing everything in its power to batten down the hatches.

Air Canada remains a high-upside speculative bet

Although many experts would agree that a vaccine is likely by next year, some bears think that a vaccine could take much longer. Such a scenario would be detrimental to all airlines.

As such, even the best commercial airline stocks ought to be seen as more a wise speculation than a sound investment given the wide range of possible outcomes with this pandemic.

If you're not comfortable with the possibility that Air Canada could crumble in a bear-case scenario, then you're better off following in Warren Buffett's footsteps by eliminating your exposure to the industry.

But if you're a young investor who understands the risks, a name like Air Canada may be capable of tilting the risk/reward in your barbell portfolio's favour.

Foolish takeaway

While there was a lot of hair on Air Canada's latest quarter, I do find it encouraging that management expects cash burn rates to fall further to $15-17 million per day from $19 million in the quarter prior.

Lower cash burn rates mean more time to wait for a vaccine to land. With shares back at the $15 range, I'd only consider buying if you see yourself buying more should shares retreat to the single-digits in what could be another full year of COVID-19 disruptions.

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