Air Canada (TSX:AC) Q2 Results: What We Learned

Description

Last week, **Air Canada** (TSX:AC) released its second-quarter results. The news was terrible.

Total revenue declined of 89% year-over-year. Passenger volumes fell by 96% versus the year before. Cargo revenue actually increased, but not nearly enough to offset the decline in passenger traffic.

Lower revenues crushed the bottom line. Air Canada posted an operating loss of $1.6 billion, with negative EBITDA of $836 million. Executives stressed that the company still has $9.1 billion in liquidity, but it's clear that the clock is ticking.

"As with many other major airlines worldwide, Air Canada's second quarter results confirm the devastating and unprecedented effects of the COVID-19 pandemic and government-imposed travel and border restrictions and quarantine requirements," the company explained.

The most valuable insights, however, were buried deep in the conference call. When executives opened the call up for public questions, their answers were quite revealing.

Read the details

The most obvious takeaway from the call was that Air Canada executives wanted to assure the market that it has plenty of capital to ride out the current storm.

"Our company is fundamentally very solid. Since mid-March, we have raised $5.5 billion in new equity, debt and aircraft financings in the capital markets, providing us with over $9 billion in liquidity as of June 30. The speed and magnitude of this capital raising is also unprecedented," stressed CEO Calin Rovinescu.

He worked hard to frame this as a vote of confidence from the market, even explicitly stating it in such terms, explaining the capital raise as "…a testament to the confidence capital markets have in our airline and in what we have achieved over the decade."

I wouldn't be too sure of his framing, however. Market analysts remain very bearish on airlines. **Boeing** CEO Dave Calhoun, who knows his customers well, noted in an interview that we'll likely see a major airline bankruptcy this year. The cost to ensure airline bonds against insolvency has soared since February.

If you run the numbers, airlines simply can't sustain the current environment. Something has to change.

Will Air Canada survive?

For airlines to survive, passenger traffic will need to pick up quickly, sizeable and sustainably. Air Canada executives are pitching this future hard.

"It appears we passed one hurdle in the second quarter and that travel is resuming, primarily in the domestic market, albeit very slowly at a markedly reduced level," CEO Calin Rovinescu said optimistically.

Unfortunately, the company can't afford a slow recovery. Air Canada is losing more than $1 billion every 90 days. It has less than 24 months of capital remaining. If the COVID-19 crisis lasts that long, shareholders will likely end up with nothing.

Even if the company can survive through emergency cash raises, the stock price likely won't benefit.

"The sad reality is that unless airlines raise new capital, they will go bankrupt," says Vitaliy Katsenelson, chief investment officer at Investment Management Associates.

"This capital, though it might save them, will reduce the value of their businesses. Equity issuances would permanently dilute shareholders, as future earnings will be shared with a much-increased shareholder base."

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