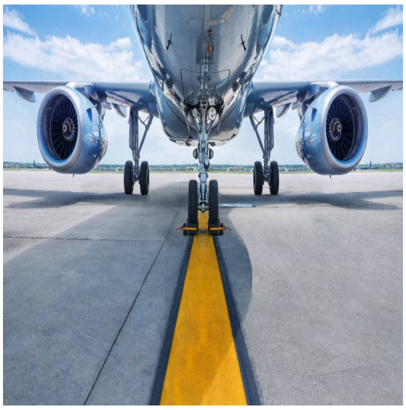

The Next 3 Years Are Crucial for Air Canada (TSX:AC) Stock: $0 or $30?

Description

AC is burning $15-$17 million cash every month. By the end of this year, its losses could widen to over $4 billion from $2.8 billion in the first half. The next three years are very crucial for the airline, as they will determine whether the stock will grow to $30 or fall to $0.

Air Canada's preparation for the COVID-19 crisis

International travel has taken a big hit, because it was the main reason why the coronavirus outbreak became a global pandemic. It started in China in November and spread globally in March. With no vaccine in place, it's not surprising that Canada closed its international borders for six months (March 21 to September 21).

AC knew that restricted travel is not just a two- or three-month affair, but it is here to stay for almost a year. It cannot support its current operations while running just 10-20% of its capacity. Hence, it is undergoing a major restructuring to avert bankruptcy.

- AC is retiring 33% of its fleet and it may also cancel orders for new planes.
- It has already halved its workforce.
- It has increased its liquidity to over $9 billion by raising money through debt and equity.

These efforts will slow the cash burn and give AC some more time to get flying again. The $9-$10 billion liquidity can keep AC afloat for around three years after restructuring. This is the time the airline estimates international travel will take to return to the pre-pandemic level. It is a bold estimate given the uncertain nature of the pandemic.

What does Air Canada's history say about the health crisis?

If I look at history, it took AC 10 years (2003-2013) to recover from the SARS epidemic and increase its stock price. SARS grounded 60% of AC's capacity to Asia. During this period, the airline reported bankruptcy (April 2003), restructured its business (September 2004), and once again started trading on the Toronto Stock Exchange (November 2006).

It was not until 2013 that AC reported its first profit of $6 million. That was the time its stock surged four-fold in just one year. In seven years, the stock rose 27-fold. If you had invested $10,000 in AC in 2013, your money would have grown to more than $270,000. Let me remind you, this 27-fold increase came after a 10-year waiting period and seven-year growth period. You could have got this return even if you purchased the stock when it started to grow.

The next three years are crucial for Air Canada

If you are holding onto AC to get that 27-fold growth, you will have to wait for more than a decade. Plus, you run a risk of losing your investment in the event the next three years don't see material growth in international travel.

I agree that AC is a lot stronger financially than it was in 2003, but the COVID-19 pandemic is also many times bigger than the SARS epidemic. The next three years are crucial for AC, as they will tell whether or not it can avert bankruptcy. It is only in 2024 that the airline will see some significant recovery. Then it will have to recoup all the losses and reduce the debt it piled up in those three years. It could take AC another six to seven years to return to profit.

Investor corner

Instead of blocking your money in AC over the heads-or-tails probability, you can buy stocks that are resilient to the pandemic. One such stock is **Descartes Systems**, a provider of supply chain-planning solutions. The company has both airlines and e-commerce sites as its customers. It has grown 25% this year and will grow even further.

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