Looking to Buy TSX Stocks? Avoid This Major Mistake

Description

Often, when investors are researching **TSX** stocks, they will look to a historical price chart to get an idea of how the stock has performed in the past. This is an important step and can give you great insight into how volatile a stock is and what kind of consistency and performance it's had in the past.

However, problems can start to manifest when you rely too heavily on the historical price of a stock as a reason to invest in the business. Oftentimes, investors will see a stock that has sold off substantially and assume it can get back to the levels it was trading at before.

And while that's always a possibility, there is by no means a guarantee that companies will be able to recover.

Struggling TSX stock

Take a stock like **Air Canada** (TSX:AC), for example. Airlines have been one of the hardest-hit industries of the coronavirus pandemic, and Air Canada may be one of the worst-impacted stocks.

It could be years before the company sees the capacity levels it had in 2019. So, we know it could take a while for the stock to see a major recovery. Despite that, investors will see the stock down roughly 70% from its 52-week and think it could be a good deal.

At Wednesday's closing price of $16.50, an investor may think there is significant potential for a more than 200% return if the stock could return to its $50 highs. This would be a considerable gain if it could materialize, which could lead investors to want to invest today.

However, assuming it can return to its pre-pandemic high would be a significant mistake. First of all, with any TSX stock, there's no guarantee of anything. However, especially now amid a pandemic and a massive economic shock, it will be considerably more challenging for Air Canada to reach its pre-pandemic stock price.

Several factors are keeping Air Canada from returning to 2019 capacity levels any time soon. Plus, in addition to all the reasons why capacity may not come back fully, there are also a few reasons why it will be harder for the stock price to reach pre-pandemic highs.

How TSX stocks are valued

In order to understand why Air Canada may struggle, the first thing to understand is how stocks are valued. The price of a stock represents what investors are willing to pay for the equity of a company. Yet many TSX stocks, including Air Canada, are also highly capitalized by debt. This is why enterprise value (essentially market cap plus net debt) is a much better gauge of value.

Basically, the longer the duration of the pandemic, the harder and less likely Air Canada will be to get back to its pre-pandemic highs.

This is because the company is going to need to raise cash in the short run to weather the storm. The problem with that is if the company raises equity, it dilutes shareholders. That means to see that $50 price an investor is targeting, the TSX stock would have to reach a market value for its equity that's higher than before, as there would be more shares issued.

On the flip side, if the company were to take on more debt without expanding capacity (enterprise value stays the same), the market value of the equity would also be worth less than before, as more of the company would be capitalized by debt.

Bottom line

Charts are essential in investing and play their role. However, it should only be a small part of your investment research. If you rely too heavily on the past performance of a TSX stock, you could be making a big mistake.

CATEGORY

1. Coronavirus
2. Investing

POST TAG

1. Editor's Choice

TICKERS GLOBAL

1. TSX:AC (Air Canada)

PARTNER-FEEDS

1. Business Insider
2. Koyfin
3. Msn
4. Newscred
5. Sharewise

6. Yahoo CA

Category

1. Coronavirus
2. Investing

Tags

1. Editor's Choice

Date
2025/08/27
Date Created
2020/08/28
Author
danieldacosta