



Air Canada (TSX:AC) Stock Tanks As Flights Get Cancelled

Description

Air Canada ([TSX:AC](#)) stock slid 5.6% on Friday as news broke that the airline was continuing to cancel flights. That day, the *CBC* reported that AC and WestJet had cancelled 439 flights in September. The news was a major blow to those who had been hoping for a quick travel rebound.

The culprit for the slashed flights was weak demand. While international travel restrictions are slowly being lifted, individuals remain wary of travelling. As a result, passenger volume is still lower than normal.

None of this was unexpected. In its Q1 press release, Air Canada said it would take three years to revert to 2019 revenue levels. What we're seeing so far only confirms that.

Still, in the second half of this year, AC stock had been rallying—as if investors expected a quick recovery. The latest news on flight cancellations has apparently diminished their enthusiasm.

Serious financial problems

Air Canada's prolonged period of lower revenue is problem enough as it is. However, it has long-term financial implications that are even worse.

Airlines are capital intensive businesses. They require [heavy amounts of debt](#) to operate. As a result, they cannot run with depressed revenue for long without serious financial problems. In Q2, AC had \$515 million in revenue, and over \$150 million in interest expenses. Throw other fixed charges in there, and Air Canada's revenue is barely covering fixed costs—let alone total costs.

It's this reality that led to Air Canada's highly publicized 2020 losses. In Q1, the company lost \$1.05 billion. In Q2, it lost \$1.7 billion. The company's stock slid when those earnings were announced. Later, it began rallying. Investors presumably expected better earnings to come. However, with the airline cancelling hundreds of flights, it's looking like Q3 will be another loser.

Another earnings miss likely

It's very likely that Air Canada's third quarter will see another big miss. The exact magnitude is hard to predict, but a company insider reported a few months ago that the airline was losing \$20 million a day. If that number still holds, then we'd expect a \$1.84 billion loss in Q3. That is, \$20 million times 92—the number of days in the third quarter.

Foolish takeaway

For months now, investors have been bidding up Air Canada stock on hopes of a quick travel rebound.

That's beginning to look premature. With Air Canada still cancelling flights, another billion dollar loss is looking likely in Q3. An earnings miss is always bad news for a stock, but in Air Canada's case it will be worse than for most. The company has enormous fixed costs that it can't cover right now without taking on more debt.

The company just recently issued a \$1.6 billion package of debt and equity. At this rate, another one will probably be needed. Perhaps a [second bankruptcy](#) is even in the cards.

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