



Air Canada's (TSX:AC) Fears Materialize, International Travel Restrictions Extended Till Halloween

Description

As it is, things were not going well for **Air Canada** ([TSX:AC](#)) that the Canadian government gave another bad news. What the airline feared the most materialized. The Justin Trudeau government has extended the international travel restrictions yet again till Halloween (October 31). I won't be surprised if these restrictions are extended to Christmas. At this rate, AC could lose its holiday season recovery.

What are these international travel restrictions?

You hear a lot about international travel restrictions, but what exactly are they. AC CEO Calin Rovinescu describes these restrictions as “four overlapping barriers to travel and economic recovery.”

- Restriction on foreign travelers
- 14-day quarantine rule
- Interprovincial travel barriers
- Government's advice to avoid non-essential travel

The travel conditions are bad worldwide, but Rovinescu blames the government for having one of the most stringent travel restrictions in the world. He has been requesting the government to ease these restrictions.

In an attempt to strengthen his case, AC opened COVID-19 test booths and offered complimentary medical and quarantine insurance. However, an international traveler flying on an AC flight tested COVID-19 positive, reducing hopes of 14-day quarantine rule easing anytime soon and impacting international business travel.

Then came another threat of a spike in COVID-19 cases in Ontario and Quebec, according to [Reuters](#). The spike in cases reduced hopes of ease in interprovincial travel restrictions, which will impact domestic travel. And now,

The financial impact of international travel restrictions on Air Canada

Before the pandemic, AC earned 70% of its revenue from international travel, which means the above restrictions take away this revenue. The remaining 30% revenue from domestic travel will be impacted by interprovincial travel restrictions and low demand. In September, AC consolidated and canceled hundreds of flights as it failed to fill a sufficient number of seats needed to bear the cost of the flight.

For an airline to break even the flight cost, it needs to fill 70-75% passenger seats. With the fuel cost down, the break-even point would be less.

All North American airlines reached the bottom in the second quarter as the pandemic was at its peak. At that time, AC reported a loss of \$1.75 billion as its revenue dipped 88% year over year (YoY) to \$527 million. The airline would likely report another billion-dollar loss in the third quarter, increasing its nine-month loss to \$3.8-\$4 billion. No entity can continue to make losses till perpetuity.

To reduce its cash burn, AC increased its cost reduction program from \$500 million in the first quarter to \$1.3 billion in the second quarter. The program included halving its workforce by cutting 20,000 job cuts and reducing its fleet size by a third by retiring 79 aircraft. At that time, the airline assumed that international travel would begin in the fall. This assumption is unlikely to materialize.

The entire third quarter went by in travel restrictions with some uptick in domestic travel. Even if AC's revenue grows 50% sequentially, it won't cross \$800 million while its operating expenses will continue to be around \$2 billion. The slow recovery in air travel could see AC make cost-cutting more aggressive.

Air Canada's three-year test

AC's current liquidity of \$9.1 billion gives it a two-year time frame to report losses. If its losses don't reduce and travel demand doesn't return by 2023, bankruptcy is in the cards. I don't know about 2023, but its 2020 and 2021 losses would most likely be in billions of dollars.

How would Halloween be for Air Canada?

The October month would be very volatile for AC, as it would release its third-quarter earnings around Halloween. AC stock has been hovering around the \$14-\$20 price range. If the airline reports losses above \$1 billion and announces further restructuring, the stock could lose its support at \$14 and make a new low.

The [short-term volatility play](#) is still valid for the stock, but I would suggest you adopt a wait and watch approach towards the month-end. A better stock than AC is **Cargojet**, which is benefitting from the grounding of passenger planes, low oil prices, and a surge in e-commerce volumes.

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