



Airline Stocks Soar on Traveller Numbers: Is the Rise Sustainable?

Description

This week started with renewed optimism for airline stocks after last week's dips on weak earnings. Stocks of the top four U.S. airlines and **Air Canada** ([TSX:AC](#)) surged above 2% in the early trading session today as the Transportation Security Administration (TSA) [data showed](#) an uptick in travellers. This brought some relief to the airline stocks after the last week's red line. Last week **United Airlines** ([NASDAQ:UAL](#)) and **Delta Air Lines** ([NYSE:DAL](#)) reported billions of dollars in third-quarter losses.

Airlines see a surge in traveller numbers

Airlines worldwide have been growing desperate to fly after the COVID-19 pandemic reduced air travel by 95%. Only cargo and essential travel were allowed. The total number of people that went through TSA checkpoints dropped 96% year over year (YoY) to as low as 87,500. As the economy re-opened in July, domestic air travel saw an uptick, while international travel was still low.

But on October 18, the number of people that went through TSA checkpoints passed the 1 million mark for the first time since March 15. This represents a 60% decline from last year, but on the bright side shows a 35% recovery in travel demand. The fact that people are gradually flying again gives some assurance that the already delayed travel demand is finally returning.

What do these traveler numbers mean to airlines?

Airlines have been burning cash over the last six months as they were not allowed to fly. When they got permission, there weren't enough passengers. Air Canada had to cancel and merge hundreds of flights in September as it was unable to fill the seats. It was operating at less than 20% capacity, burning \$15-\$17 million cash daily, despite the government's wage subsidy and low oil prices. AC is on the verge of reporting a loss of \$4 billion in the first nine months of 2020.

United and Delta have already reported more than \$5 billion in losses so far this year. In the third quarter, they operated at 25% capacity reporting more than 75% YoY decline in revenue. But a YoY figure will only be negative. As airlines are in a recovery phase, revenue of United and Delta surged

70% and 110% sequentially. And a 1 million traveler throughput reassured investors that this sequential revenue growth is here to stay.

Hence, airline stocks surged on TSA figures. Airlines have a long way before they even become profitable. But the 1 million traveler number indicates that the first step towards recovery has begun.

Airlines have a long road to sustainable recovery

There are many roadblocks before airlines can show sustainable recovery. Hence, don't be surprised if their stocks drop once again when American Airlines and Southwest Airlines report their third-quarter earnings on October 22.

Once the international borders open and people return to flying, airlines' cash burn will slow. The top five North American airlines were burning between \$15-\$40 million cash daily in the second quarter. They are already doing everything possible to cut costs. Lower cost and higher travel demand will mitigate their losses.

The next elephant in the room will be the expensive debt they took to increase their liquidity this year. The capital is slowly drying up for airlines, and their poor credit ratings aren't helping. Hence, when AC succeeded in refinancing \$1.5 billion in short-term debt and also keep the [Transat AT acquisition going](#) at a 75% reduced price, shareholders were happy.

The airlines which fail to generate enough revenue to repay the maturing debts could risk bankruptcy.

What should investors do?

The billionaire investor Warren Buffett exited airline stocks as he saw no value in them for the next few years. For him, staying invested in these stocks was equivalent to funding losses. If you are looking at airlines from a long-term perspective, I would suggest you look into other stocks that are still churning profits. The entire industry would take at least three years to stabilize. By then, only the major airlines with better liquidity would survive. Many would fall prey to bankruptcy.

It's hard to tell which side AC will land. Wait until its earnings release on November 3, and then take advantage of the stock's \$14-\$20 price range to make some short-term gains.

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