



Oh No! Southwest Airlines Has Terrible News for Air Canada (TSX:AC)

Description

Southwest Airlines ([NYSE:LUV](#)) is widely regarded as one of the best-run airlines in the world. It does such a good job that Warren Buffett owned millions of shares before the pandemic began.

As with every other airline, the company's stock plummeted when COVID-19 first hit. Shares are still 25% below their pre-pandemic peak.

Things won't get better anytime soon. The latest financial results should send a chill through every airline investor, including people who own stock in **Air Canada** ([TSX:AC](#)).

This news is scary

At the start of 2020, Warren Buffett [owned](#) millions of shares in four different airlines. He went from an industry bear to a major bull.

"It's true that the airlines had a bad 20th century," he explained. "They're like the Chicago Cubs. And they got that bad century out of the way. The hope is they will keep orders in reasonable relationship to potential demand."

That last part refers to the industry's inability to balance supply with demand. From 1993 to 2013, for example, Southwest Airlines stock returned 0%. That's two decades of lost time.

The issue was rampant competition. Dozens of airlines competed across every route. Whenever profits appeared, additional planes were deployed to the area, pushing pricing down yet again.

Around 2014, everything changed. Competition rationalized. That's when Buffett jumped in. To him, the investment case was all about making sure too many planes weren't chasing too few passengers.

Over a five-year period, Southwest Airlines stock rose *six times* in value. Buffett was pleased, as were other airline investors.

Then the coronavirus pandemic began. Today, Buffett doesn't own a single airline share. He recently revealed that the "world has changed for airlines," adding that the balance between planes and passengers is a thing of the past.

This week, Southwest Airlines posted its biggest-ever loss. It lost US\$1.2 billion during the quarter versus a US\$660 million profit the year before.

"Bookings have improved in recent months, the carrier said, but it warned a recovery is still far off," [reported CNBC](#).

As we'll see, this is *terrible* news for other airlines, especially Air Canada.

What Southwest Airlines tells us

The clock is ticking for airlines. There's no denying that.

Take a look at Air Canada. Last quarter, the company ended with \$9 billion in liquidity. Over the previous six months, it lost roughly \$3 billion, so simple math suggests Air Canada has just 18 months of financial runway left.

Many investors were planning on the cash burn to end in 2020. The recent news from Southwest Airlines proves that won't be the case. Investors should expect another billion-dollar loss for Air Canada.

This year, several carriers have already gone bankrupt. In North America, insolvencies have been rare. Markets have proven willing to stopgap the multi-billion-dollar losses for several quarters in a row. But unless that money train keeps coming, a dire future is in the cards.

There's only one way out of this mess for carriers like Southwest Airlines and Air Canada: passenger traffic has to pick up rapidly. I'm not willing to make that bet.

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Date

2025/07/02

Date Created

2020/10/27

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