



Pandemic 2.0: Stay Away From Air Canada (TSX:AC) Stock

Description

Air Canada's ([TSX:AC](#)) worst fears have materialized. Just when the airline was preparing to fly internationally, the second wave of pandemic infected its recovery. The stock has dipped 13% to less than \$15. The month of October already brought a lot of bad news. The U.S. airlines posted their highest quarterly net loss in the third quarter even though they saw a slight improvement in passenger revenue.

COVID-19 pandemic has infected Air Canada

Canadian government extended international travel restrictions until November 21 as the coronavirus cases surged in Canada, the U.S., and Europe. It's not like the government doesn't want to ease U.S. border restriction. Prime Minister Justin Trudeau stated that the government will not ease the travel ban until COVID-19 cases slow in the U.S., the country [most affected by the pandemic](#). Some countries in Europe are tightening travel restrictions to control the spread.

When AC itself is not sure whether its planes can take off, any amount of restructuring is in vain. It planned to launch a revamped Aeroplan loyalty program in November, but even that won't stop cash from burning.

AC will release its third-quarter earnings on November 3. Looking at the earnings of U.S. airlines, AC's net loss could widen to more than \$2 billion as the airline canceled several scheduled flights. A flight earns profits when more than 75%-80% of seats are filled. While AC saw some uptick in domestic travel, it is not enough to breakeven. This means AC lost money on the flights.

Can Air Canada survive pandemic 2.0?

AC can't control demand, but it can control costs. It is significantly cutting costs and downsizing to makes its \$9 billion liquidity last longer. This liquidity won't last beyond 2021. If air travel demand doesn't return significantly (to the level where flight costs breakeven) by mid-2021, AC will be in serious trouble.

The air travel demand recovery is already slower than airlines expected. In the third-quarter earnings, airline bosses stated that leisure travel demand will not return till mid-2021, and business travel demand won't return for the next three to five years. The second wave of the pandemic will slow the leisure demand even further.

The capital is drying up for airlines, as investors don't want to hop on to the airline stocks that are entering the Bermuda triangle with no signs of return. Even Warren Buffett, the saviour investor in times of distress, has clearly stated his intentions to stay away from airlines.

In the third quarter, AC's liquidity could fall to \$7.5 billion and \$6 billion by year-end. With limited options to raise more capital, a bailout will be its last resort. Investors got the hint that AC is [considering a bailout](#) when a top government official stated that it is discussing options with airlines. AC's third-quarter earnings will probably shed some light on the possibility of a bailout.

Stay away from airlines until further notice

AC stock is too risky to even play a short-term bet in the \$14-\$20 price range. The odds are skewed toward bankruptcy or bailout than a recovery in the next few months. The discussions with the government officials suggest that a bailout could be in the cards. A bailout could protect the stock from falling to \$0.

But shareholder interests are the least of the priorities for the government. If the government bails out AC, it will be to save jobs and keep air travel alive. Until the third-quarter earnings, keep AC on your watch list.

A better stock than Air Canada

If you want to invest in airlines, **Cargojet** ([TSX:CJT](#)) is a better option. The air cargo company is making new highs as it is also handling the cargo volumes of passenger airlines. Moreover, the pandemic-induced e-commerce wave has kept its planes busy, and the lower oil prices have been pouring in higher profits.

Even when the pandemic eases and air travel demand returns, Cargojet's revenue will grow. The fourth quarter would be busy for the air cargo company as holiday season sales will shift online this year. While the odds are against AC, they are in favour of Cargojet. Flow with the tide.

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