Is Cargojet (TSX:CJT) a Buy Ahead of its 3rd-Quarter Earnings?

Description

The aviation sector is going through a challenging period amid the decline in passenger demand due to the pandemic-infused travel restrictions. The decline in air travel has increased the airline companies' net losses, cash burn, and debt, thus eroding a significant part of their share value.

Meanwhile, **Cargojet** (TSX:CJT), an air cargo company, is an exception. It has returned close to 112% for this year. The increased demand for its services amid the surge in e-commerce and healthcare volumes and its impressive second-quarter performance has led to a rise in its stock price. Meanwhile, the company will report its third-quarter earnings tomorrow before the market opens. Let's look at what to expect from its third quarter.

Third-quarter expectations

In the second quarter, Cargojet had reported an impressive 64.7% year-over-year growth in its top line, with all its three segments — domestic air cargo, ACMI (aircraft, crew, maintenance, and insurance), and charter — reporting growth. Given the favourable market condition, I am optimistic about the company's third-quarter performance.

Cargojet provides air cargo services between 14 major cities in Canada. Through its unique overnight delivery service and an array of 26 aircraft, the company transports approximately 90% of Canada's domestic air cargo volume. Further, the company earns 75% of its domestic revenues through long-term contracts, which provides stability to its top line and cash flows.

Before the imposition of travel restrictions, passenger aircraft carried 40% of the global air cargo. With a significant chunk of passenger aircraft grounded amid the travel restrictions, the demand for air cargo companies' services, including Cargojet, has increased. Further, Canada's e-commerce sales continue to witness robust year-over-year growth. In August, retail e-commerce sales rose 60.6%, which could increase the demand for the company's services, thus increasing its revenue.

Meanwhile, the company had also introduced scheduled routes to the U.S. and Mexico in September 2019 and two new scheduled routes to Europe in April 2020. The addition of these new routes could contribute to the company's top-line growth.

Outlook

Amid the pandemic, not only large retailers, even SMBs (small- and medium-scale businesses) have taken their shops online. In August, Canada's retail e-commerce stood at $2.8 billion, which formed just 5% of the nation's total retail sales. So, the sector still has significant scope for expansion. With a substantial market share in the air cargo sector, Cargojet is well positioned to benefit from the e-commerce sales expansion.

The air cargo sector is highly capital intensive, which provides a natural barrier for new entrants, thus preventing increased competition. So, the company's growth prospects look healthy.

Bottom line

The surge in Cargojet's stock price has increased its valuation multiples. The company currently trades at a forward price-to-earnings of 41.3 and a forward enterprise value-to-sales multiple of 6.2, which looks comparatively expensive. However, people tend to pay a premium for growth stocks. With its revenue growing at over 60%, I believe the company's high valuations are justified.

Given its impressive growth prospects, high market share, and improving margins, I am bullish on Cargojet. Of the 12 analysts that follow Cargojet, seven have given a "buy" rating, while five have given a "hold" rating. None of the analysts are in favor of a "sell" rating. Analysts' consensus price target stands at $240.27, representing a return potential of 9.8% from its current stock price.

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