Air Canada (TSX:AC) Stock Rally: Is it Sustainable?

Description

Air Canada (TSX:AC) stock consolidated sideways since the COVID March market crash. It's hard to believe, but in the last month, it managed to rally 40%! There's reason to believe that this rally is just getting started.

The catalyst for the rally may be the recent positive news about vaccines from **Pfizer** and **BioNTech**, **Moderna**, and **AstaZeneca** with efficacy rates as high as 95% and with no adverse effects. However, there can be some challenges in terms of storage and distribution, as the vaccines need to be stored in ultra-cold temperatures.

These vaccines can start being distributed as soon as late December. And there's hope to achieve herd immunity by the second half of 2021.

As long as investors have hope of a return to normalcy, in time, Air Canada stock will recover to its previous highs and make outsized returns for shareholders.

Air Canada: All about cash and costs

For Air Canada, it's all about surviving through the pandemic. Revenue was down 86% year over year in the third quarter (Q3). As well, its net debt increased by 66% to $4.97 billion.

To survive, Air Canada has been hoarding cash and cutting costs significantly. It plans to reduce capital spending by $3 billion through 2023. This includes delaying the purchase of new aircraft. It makes perfect sense not to invest in the fleet at a time when air travel volumes are so low.

From Q1 to Q3 2020, Air Canada impressively cut capital spending by more than 50% versus the same period in 2019. Simultaneously, it was able to almost double its cash position to nearly $3.8 billion. In total, it has access to close to $8.2 billion of liquidity, including cash and short-term and long-term investments.

Air Canada stock: It's not for everyone

I will not try to undermine the risk investing in Air Canada stock. Year to date, the airline's revenues are down 66%. There's no doubt it will take a huge loss this year.

The cyclical stock is highly tied to economic boom and bust. But it's worse this year because on top of tighter travel restrictions, even people who have the money to travel are deterred from doing so because of the worry of contracting the virus.

Currently, the stock is given an S&P credit rating of B+, which is the highest-quality speculative rating. That said, as long as the company survives (and it seems to have the assets to do so), AC stock should be able to make a lucrative comeback for buyers of the stock today.

If you decide to take a position in AC stock, be cognizant of your portfolio allocation. A risky investment should stay the size of a risky allocation — perhaps no more than 1% of one's portfolio.

The Foolish takeaway

The Air Canada stock rally should be sustainable. However, expect volatility. Positive or negative news about the pandemic or vaccines is going to trigger buys or sell-offs in the stock in the short term.

Currently, AC stock is trading at the top end of its sideways channel. It needs to break above $22.50 per share before breaking through its 50-day and 200-day simple moving averages. These are major resistance to climb over.

If you have the patience, the stock should be able to recover to at least the $40-per-share level within a few years.

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