



## Air Canada (TSX:AC) Stock: Here's the \$1 Billion Question

### Description

**Air Canada** ([TSX:AC](#)) stock is doing well. Over the last 30 days, shares have spiked 50%.

Multiple positive vaccine announcements are the key catalysts. If people feel comfortable that they won't contract or become a carrier for COVID-19, it's reasonable to expect airline traffic to spike.

There's only one problem: Air Canada is running out of cash.

### Know these numbers

There's light at the end of the tunnel for airlines. That's a huge relief after a tumultuous 2020.

Just don't let the recent vaccine news overstate the situation. Passenger traffic fell to just 5% of normal volumes earlier in the year. Today, traffic is still stuck at 10% of 2019 levels. Demand is ticking up, but there's still a giant gap remaining.

That gap is important to recognize for Air Canada. It's important for all airlines. These businesses have high fixed costs. Wherever demand heads, up or down, airlines are stuck with most of their cost base. If demand drops 95%, they still need to pay to maintain 100% of their planes.

High fixed-cost businesses have a terrible time with revenue declines. Small dips can produce an outsized impact on profitability. With COVID-19, we're not talking about small changes. This year has been truly catastrophic.

"We're now living through the darkest period ever in the history of commercial aviation, significantly worse than the aftermath of 9/11, SARS, or the 2008 global financial crisis," Air Canada CEO Calin Rovinescu [stressed](#) when the downturn began. "There is little doubt that we are not yet out of the trough."

His comments weren't overly dramatic. Air Canada is losing more than \$1 billion every 90 days. This year, it could burn through nearly \$5 billion in cash. Note the current market cap is just \$7 billion.

## Can Air Canada soar?

Over the last 30 days, the market has given this stock a vote of confidence. That's important for a company losing \$1 billion each quarter. Is the end really in sight?

I expect airline traffic to improve in 2020, but analysts still [think](#) traffic will remain at least 30% below 2019 levels. If you remain cognizant that Air Canada is a high fixed-cost business, you know that this traffic improvement still isn't enough to generate profits.

That's the big mismatch. Yes, conditions could improve dramatically next year, but most airlines will still generate losses.

Right now, Air Canada has roughly \$8 billion in liquidity left. This quarter, expect another \$1 billion loss, or something within that range. If losses are cut in half next year, the business will end 2021 with around \$5 billion in liquidity.

The key will be what happens to demand in 2022. Does demand fully return to normal? Does it perhaps exceed 2019 levels? Most airline executives don't anticipate a full return to normal in 2022. One CEO in particular thinks demand will remain *permanently* lower.

In reality, Air Canada could continue to lose money for another 24 months. The bleeding will slow, but more debt and share issuances will be needed to plug the gaps. That'll dilute any potential gains.

The vaccine news is promising, but this story still has a long way left to go.

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