



## 3 Things You Should Know Before Buying Air Canada (TSX:AC) Stock

### Description

**Air Canada** ([TSX:AC](#)) stock jumped more than 80% last month. Are you thinking of buying the stock now at \$27.5? Before you follow the tide, read the risk that comes with this stock. It's 80% rally is not backed by fundamentals but by sentiments around the COVID-19 vaccine.

World airlines were among the most affected by the COVID-19 pandemic. Airlines need to keep flying to make money, and the pandemic restricted air travel. While the vaccine news brings some respite to airlines, investors should consider these three things before buying AC.

### Canada has five layers of travel restriction

Canada has some of the strictest travel restrictions in the world. Its restrictions began on March 15. The government has now extended them to December 21 for U.S. borders and January 21 for foreign nationals from non-U.S. countries.

In an interview with [BNN Bloomberg](#), AC CEO Calin Rovinescu stated that the airline faces five layers of restrictions:

- A blanket prohibition on foreign travelers coming to Canada;
- U.S. border closure for non-essential travel;
- Mandatory 14-day quarantine requirement for Canadians and residents returning to Canada;
- Prohibition, even on Canadians traveling to the Atlantic provinces; and
- Travel advisories that are nullifying insurance policies for non-essential travel.

The result was 90% of AC's planes remained grounded. It is now retiring 75 aircraft and has canceled orders for 22 new aircraft. It has also discontinued 30 domestic regional routes and closed eight stations in Canada.

The COVID-19 vaccine will gradually relieve AC from these restrictions. But this could take another six months to one year. Even when the vaccine comes, it remains to be seen when people return to flying again. Rovinescu believes it could take air travel at least three years to return to pre-pandemic levels. Until then, AC is doing everything it can to generate cash.

## Air Canada focuses on cargo planes

As passengers stay grounded, the next best source of cash is cargo. **Cargojet** reported 65% and over 30% revenue growth in the second and third quarters. Hence, AC shifted its focus to cargo. For the first time, AC's cargo revenue (\$269 million) surpassed passenger revenue (\$207 million) in the second quarter.

Rovinescu saw an opportunity and, in the third-quarter earnings call, said, "Cargo will become an increasingly important part of our business as we plan to expand to dedicated freighter business." Air Canada intends to convert its retired Boeing 767-300ER aircraft into freighters and tap the global air cargo opportunity. AC will also play an active role in transmitting COVID-19 vaccines from around the world to Canada.

AC plans to actively pursue the cargo strategy, even in the long term, when passenger revenue recovers. If it succeeds in pulling this cargo strategy profitably, it will emerge stronger from the pandemic. But that will only happen if it survives the pandemic with not too much debt. And for that, it needs a government bailout.

## How long until Air Canada gets a bailout?

Airlines worldwide have received a sector-specific bailout. But AC has remained isolated from the bailout. It availed of wage subsidies to pay salaries to its employees. But now, the Canadian government is considering a bailout for airlines under two conditions:

- AC should provide cash refunds for canceled flights; and
- AC should resume the routes it discontinued during the pandemic.

The [bailout can be in the form](#) of grants, low-interest loans for the long term, and buying an equity stake in AC.

Rovinescu agreed to fulfill the first condition of refunding ticket money for canceled flights provided the bailout is sizeable. He also expressed his opposition to a bailout option where the government takes an equity stake in AC. In the *BNN Bloomberg* interview, he said, "State ownership of airlines has been a colossal failure elsewhere around the world, and we're certainly not advocating for it."

If AC succeeds in getting the desired bailout, it could ease the airline's biggest challenge of high-interest debt and increase its chance to become profitable earlier than expected. It will enter the post-pandemic economy more competitive. Until profits show up, AC stock will have difficulty sustaining its rally.

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