Air Canada (TSX:AC) Stock at $27.5: Should You Buy, Sell, or Hold?

Description

Shares of aviation giant **Air Canada** (TSX:AC) are trading at $27.5, which is about 50% below its record high. Driven by the COVID-19 pandemic, it touched a multi-year low of $9.26 in March before gaining momentum in the last nine months.

This means Air Canada stock has almost tripled since March. It has, in fact, gained 100% since November, as investors were buoyed after pharma companies such as **Pfizer** and **Moderna** released their vaccine results for COVID-19.

But does the recent rally mean Air Canada stock remains a top pick for 2021 and beyond?

Air Canada is part of a cyclical sector

Though the vaccine results have cheered investors, it might take several more months for it to be approved, manufactured, and distributed all over the world. This means air travel is unlikely to reach pre-COVID-19 levels for at least two more years.

Airline stocks have always been high-risk investments, as a durable competitive advantage has been elusive for several decades. While airline companies experience sales growth, it is difficult to translate them into sustainable profits due to an increase in competition.

Further, aviation companies have to reinvest profits to increase passenger capacity as well as new traffic routes. Air Canada and its peers have low operating leverage due to high capital expenditures.

However, the macro landscape for Air Canada changed in the last decade, as it dominated the domestic airline market. Air Canada was one of the top-performing stocks in the 2010s and had surged an impressive 3,500% in that period before the dreaded pandemic struck.

As international and domestic borders were sealed, air traffic came to a standstill. The capital-intensive nature of the airline business means Air Canada continues to lose millions of dollars each day.

Even one of the world's most successful investors, Warren Buffett, accepted that he made a mistake by investing in this highly cyclical and competitive space and liquidated his stake in all airline stocks earlier this year.

Air Canada sales might fall close to 70% in 2020

Air Canada sales are forecast to fall by 76.6% year over year to $1.03 billion in Q4 of 2020. This suggests annual sales might decline by 68.6% to $6.01 billion in 2020, compared with sales of $19.13 billion in the prior-year period.

There is a good chance for the markets to crash once again given the high unemployment rates, low consumer spending, and a sluggish macro-economic environment. Investors can expect Air Canada stock to underperform the broader markets in a sell-off.

The second wave of COVID-19 infections will also haunt investors who will be wary and avoid public or crowded spaces like airports.

Air Canada's total debt has risen to $13 billion at the end of Q3, up from $9 billion at the end of 2019. However, its quarterly losses are close to $1 billion, which makes it a risky investment in a volatile market. Air Canada stock is expected to be rangebound in 2021 with a few dips and gains along the way.

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Author
araghunath