



Billionaire Diaries: Will Warren Buffett Invest in Air Canada (TSX:AC) in 2021?

Description

This year saw the takeoff and crash of airline stocks. Warren Buffett took the emergency parachute and jumped off the airline stocks in April. Do you think Buffett will invest in airline stocks in 2021? If yes, will he invest in **Air Canada** ([TSX:AC](#))? Let's find out.

What does Buffett think of airlines?

Buffett is a value hunter. He buys shares of companies that are distressed but have the potential to make money. In the 2009 financial crisis, he bought preference shares of **Goldman Sachs** and made money on his investment.

But not all his distress purchases were successful. He made a mistake buying the dying [textile business](#) of **Berkshire Hathaway** in 1962. He also just managed to profit out of his **U.S. Air** preferred stock that he bought in 1989. Since then, he despised airlines and even called investing in airlines as funding their losses.

Buffett on airlines in 2017

After 28 years, he bought shares of top four U.S. airlines. Sharing his views in an [interview](#) with **CNBC** in 2017, his tone was of caution. He said, "I think there have been almost 100 airline bankruptcies. I mean, that is a lot." He added, "It's been a disaster for capital."

Buffett explained the airline economics of demand and supply, saying that people are flying more. Once airlines manage to fill a certain number of seats, any additional seats they sell have no cost and only profit. Airlines have got the bad century out of the way and are now making steady profits. He added, "The hope is they will keep orders in reasonable relationship to potential demand."

What did he mean by the above statement? Commercial airlines operate like a commodity. Most travelers buy tickets based on the price and availability of seats for their preferred destination and timing. The airline that sells the cheapest tickets to a route has a higher possibility of filling its seats

faster. Airlines order more planes and expand their routes to attract more travelers. But this increase in capacity can only become profitable if there is demand.

Until 2019, there was a lot of demand because airlines' capacity increase was paying off with higher cash flow and profits.

Buffett on airlines in 2020

The world changed for airlines in 2020 when the pandemic confined people to their homes. The very reason for which Buffett put his hand in the airlines (demand-supply dynamics) collapsed. The demand for commercial air travel vanished because governments worldwide imposed travel restrictions.

Before the pandemic, these planes were printing money when in the skies. After the pandemic, they were burning money lying idle on the ground. Buffett sold \$6 billion worth of his stocks in four airlines saying, "You've got too many planes."

The weight of all these planes is becoming difficult for airlines to handle. Hence, it comes as no surprise that Air Canada has retired one-third of its fleet and canceled orders for 22 aircraft. It is doing every possible thing to help the government ease travel restrictions. It has done COVID-19 test trials and is working with the government to supply COVID-19 vaccines.

AC and **Southwest Airlines** are better off than other North American airlines as they entered the pandemic with a strong balance sheet. Both airlines have contained losses, but rising oil prices could shatter their cost-cutting and optimization efforts.

Will Buffett invest in Air Canada in 2021?

It's not like Buffett doesn't buy distressed stocks, but he needs to see the value. Looking at the demand-supply economics of airlines there is a lot of pent-up demand from leisure travelers. AC is well equipped to handle that with the acquisition of international tour operator **Transat A.T.** and its Aeroplan loyalty program. The problem is business travel, which might not return to the pre-pandemic level soon. AC is reducing its supply of planes and routes.

If AC manages to achieve the demand-supply equilibrium, it will be another three years until profit. It took Buffett 28 years and over five years of the airline's positive cash flow to return to buying airline stocks. His mind won't change about AC in 2021, at least.

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