Air Canada Stock: Price Holding Steady Despite Bad News

Description

Air Canada (TSX:AC) just announced more route cuts and layoffs as new travel restrictions put added pressure on cash flow. Despite the pain, Air Canada stock continues to trade at an elevated level.

Air Canada's troubles mount

Air Canada traded near $45 per share a year ago. Today the share price is down about 50% from that level. When you look at the size of the business and the outlook for the coming months and years, it would seem that the current price is simply too high, or the stock was extremely cheap 12 months ago.

In early February 2020, before the pandemic, Air Canada was very profitable. The company enjoyed strong demand for its business class and economy seats and had figured out that charging passengers for checked bags, as well as the right to choose their spots padded margins.

Oil prices traded slightly below current market levels, so fuel costs weren't bad a year ago and economic growth prospects in Canada and abroad suggested strong ongoing demand for Air Canada's passenger and cargo services.

A year later, Air Canada is a smaller company than it was in the 1970s, according to a CBC article citing a comment from the CEO of the Air Canada Pilots Association.

Profitability has evaporated. In fact, Air Canada anticipated net cash burn of more than $1 billion for Q4 2020 when it released the Q3 results. Investors should brace for rough Q4 numbers and a dismal outlook for the first half of 2021.

Route cancellations continue to mount and more staff positions are being cut. Air Canada grounded its Rouge subsidiary and just put another 1,500 staff on layoff notice due to the cancellation of 17 additional routes, including flights to the United States and overseas.

Why isn’t Air Canada stock falling on bad news?

Things can’t much worse and there is no end in sight for the new travel restrictions. Nonetheless, Air Canada stock trades close to where it did in early January before the government announced the first batch of new travel rules and restrictions.

One theory is that investors hope the government will step up with a big bailout package that keeps Air Canada solvent through the rest of the pandemic. The company entered 2021 with sufficient liquidity to keep it alive for several months thanks to quick decisions made by management last spring.

Based on the $8 billion in liquidity at the end of Q3 and the anticipated Q4 cash burn, Air Canada likely started the year with something close to $7 billion. It will be interesting to see where things sat at the end of December when the Q4 results come out February 12.

Betting on a generous rescue package is risky. Investor interests might be low on the government’s priority list. Comments from the government indicate a bailout deal would need to include an agreement to refund cancelled flights. That would put a large dent in the cash position at a critical time.

Commitments to restart cancelled routes to smaller Canadian cities would likely be part of any agreement. As Air Canada’s situation worsens, its options to find funds shrink and the ability to push back on government requirements decreases.

While nationalizing Air Canada probably won’t happen, investors shouldn’t expect a gift from the government when terms of an agreement emerge.

Should you buy Air Canada stock now?

Air Canada will survive and travel demand will slowly return post-pandemic, but it could take years before Air Canada gets back to its pre-pandemic condition. With that thought in mind and all the uncertainty ahead for the coming weeks and months, it might be best to look for other opportunities in the market today.

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