Air Canada (TSX:AC) Stock Stable At $26 — the Calm Before the Storm?

**Description**

The tension is heating up as the third wave of the pandemic is deadlier and is damaging both our health and the economy in many ways. The coronavirus is getting stronger and putting younger people in intensive care units (ICU). The next few weeks are critical.

A momentum stock like **Air Canada** (TSX:AC), which falls on the slightest bad news, is holding at $26. Is it the calm before the storm?



Here are two scenarios that could sway the stock north at $30 or south at $15.

## Air Canada stock going to $30

After Michael Rousseau took the CEO role on February 15, I was hopeful AC stock would hit $30 or $32. It did come to $31 for a split second in mid-March only to fall back to its comfort level of $26-$27. What drove the stock north was the hopes of a bailout. Rousseau had been using the media to its advantage to convince the Justin Trudeau government that Air Canada is the ideal candidate for a bailout.

Air Canada agreed to refund ticket money to travelers whose flights were cancelled. It also pledged to reduce 20% carbon emission by 2030. Last month, it reiterated its plans to open routes to sun destinations in May. But till that time, the fear of the third wave was not looming.

The stock started slipping in March as there was no news around the bailout. Investors were losing patience as AC was bleeding $15-$17 million cash daily. In such a scenario, the government delays could prove to be futile. AC had $8 billion in liquidity and $7.1 billion in current liabilities at the end of 2020. Any new fund it raises is costing Air Canada 9% interest.

Fitch Ratings has downgraded Air Canada’s Long-Term Issuer Default Rating from ‘BB-‘ to ‘B+’, which incorporates expectations for a government bailout. Fitch has revised the Rating Outlook to Stable from Negative as the downside risks have decreased. It does not expect the airline to return to the BB category before 2023. Hopefully, this rating downgrade might put pressure on the government for a bailout.

## Is bailout good news for Air Canada?

While it might not look severe at present, AC's liquidity is drying up — and so are its options to raise money even at 9% interest. A $1.4 billion cash burn in the first quarter might leave AC with a little under $7 billion in liquidity. And this cash burn is after excluding any lump sum debt repayments. If the cash burn continues, it will not have sufficient liquidity to meet its current liabilities.

A bailout of more than $1 billion will help AC balance its liquidity with current liabilities and keep itself operational. The bailout can be in the form of long-term low-interest loans, grants, or an equity purchase. It will give AC much-needed liquidity to stay operational, thereby increasing its stock price to $30.

## Air Canada stock falling to $15

But the third wave of the pandemic could spill gasoline on AC's plan and aggravate its cash burn. The third wave is worse than the first wave. There is a high probability that the Canadian government might not open borders to sun destinations by April 30. If it imposes restrictions on domestic travel as well, AC stock could drop to its April 2020-level of $15.



## The culprit is over-trading

If you ask that what made AC stock rally from $15 to $30 in the first place, it was the Robinhood investors. Many zero-commission brokers opened up trading avenues to everyone. This trend of zero-commission trading paved the way for many millenials to pounce on high momentum stocks and make some quick money, leading to over-trading. Studies after studies have estimated that an average of 80% of investors lose their money in the stock market because they do active trading.

The stock market rewards those who stay invested in a quality stock with strong fundamentals or a favourable business environment for the longer term — and AC is not one of them.

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pujatayal