Air Canada: Is This TSX Stock a Buy Today?

Description

Air Canada (TSX:AC) stock has fallen almost 4% in the past week. The company is due to declare its earnings this week and a question looms over potential investors- should I stay or should I go? To paraphrase The Clash: If I stay there will be trouble, if I go it might cost me double.

Why? Because Air Canada continues to remain in a precarious position right now. Travel, both business and leisure, have fallen off a cliff. Canadians are getting vaccinated but it's not at an ideal rate. The vaccine rollout has been lackluster over the last two months and has is just beginning to pick up speed. Canada has a list of people who can enter its borders. Business people and tourists aren't among them. Flights from India and Pakistan are banned until May 31.

And yet, the stock continues to attract eyeballs. Air Canada is viewed as a stock that will zoom once pandemic restrictions are lifted. Unfortunately, no one has a clear answer as to when that will be. Remember, this stock was trading at over $50 just four months before the pandemic hit the world.

Fitch downgrades Air Canada credit rating

Rating agency Fitch downgraded Air Canada's credit rating from BB- to B+ in early April, stable to negative. Fitch said, "The subdued pace of air traffic recovery, especially international travel, has pressured Air Canada's balance sheet, making it difficult to achieve credit metrics that support a 'BB-' rating before 2023. Air Canada's debt burden increased by $3.7 billion during 2020, equivalent to 1.0 turn of 2019 EBITDAR."

The rating agency states Air Canada's cash burn may continue in 2021 as well as in 2022. It means the airline company's leverage ratio might be over 5 which is high for a "BB" category rating.

What has changed between then and now? Nothing much except the travel bans. However, this is where Air Canada gets hit because trans-border and international travel make up a large part of its business. Fitch explained, “AC has accordingly reduced capacity for 1Q21 by ~85% of 1Q19 levels,and will remain at least 50% below 2019 levels through the end of 2021. Fitch expects the 1Q21 dailycash burn of $15 million-$17 million to improve throughout the year.”

Where does AC stock go from here?

Air Canada is still in its recovery stage. Extremely optimistic investors believe that the company can reclaim its pre-pandemic valuation of $50 per share in the next 12 months but they ignore the prospect of a third wave of infections hitting the world.

Air Canada has made a smart move with its refund offers. The company has already paid out refunds to the tune of $1.2 billion since February 2021. With its new refund offer, the figure will move higher. However, Air Canada has received a bailout of $5.9 billion. One of the key reasons for the bailout was that Air Canada would refund its customers. The refunds could well end up being a small trade-off, and a very smart business decision.

AC stock closed trading at $24.77 on April 30, and analysts have given it a 12-month average price target of $28.26, a gain of over 14% from current levels. It won’t be the worst idea to hold the stock. Once the world starts accelerating its vaccine roll-out, Air Canada should move up.

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