Forget Air Canada (TSX:AC): This Is a Much Better Buy Today!

Description

Air Canada (TSX:AC) stock is tempting. The airline stock trades at half of where it stood from its pre-pandemic levels. This means that if the volatile stock were to return to its previous levels, it would *double investors' money* from current levels!

Air Canada stock is depressed for multiple reasons.

Profitability

Air Canada had no profit at all last year. In fact, revenues dropped 70% year over year to $5.8 billion with a whopping operating loss of $3.8 billion (versus 2019's operating income of $1.6 billion). The company has taken a massive hit from the novel coronavirus pandemic impacts. Flight restrictions and a lack of interest in air travel (business or leisure) were the cause.

In short, in 2020, Air Canada burned close to $4.7 billion of cash, which equated to roughly $13 million a day on average! The situation worsened in Q4, in which the cash burn was *$15 million per day* on average.

The airline further projected that the cash burn could be $15-17 million a day in Q1. The exact amount will be revealed soon, as the company will report its Q1 earnings results this Friday.

In comparison, **Cargojet** (TSX:CJT) is in a much better situation. Its revenue is much more secured, as there's surer demand for air cargo services versus air traveling in the near and medium term.

During the pandemic, Cargojet found that a big part of normal shipping of flowers, food, computer, and automobile parts turned into personal protective equipment and medical supplies.

Cargojet's revenue climbed 37% in 2020. It also posted adjusted EBITDA of $291 million (up 87% year over year) and adjusted free cash flow of nearly $197 million. The growth stock's performance poses a stark contrast to AC stock's performance. Specifically, Cargojet stock is 50% higher from pre-pandemic levels.

Balance sheet

Air Canada stock's balance sheet has turned for the worse. No surprise there, given that it has been burning cash every day. In 2020, it raised net proceeds of approximately $7.6 billion from equity and debt financings. At year end, its net debt was almost $5 billion, which more than doubled (specifically rose 133%) from the end of 2019.

The airline's long-term debt-to-equity ratio (D/E) rose to 653% versus 182% at the end of 2019. Its D/E is high versus its five-year average of about 350%. As scary as its debt levels are, investors don't need to worry that AC stock is going away because of the government bailout. That said, there's no question its balance sheet has been damaged.

In comparison, Cargojet managed to reduce its net debt by $63 million last it. The air cargo service provider's long-term D/E rose to 268% versus 208% at the end of 2019. Its D/E is relatively low against its five-year average of about 302%.

Valuation

Both stocks have experienced pullbacks lately. At $24.77 per share at writing, AC stock trades at a 12% discount from the near-term analyst consensus price target. Cargojet stock's correction of roughly 27% from its recent high represents a discount of about 30%.

The Foolish takeaway

Although Air Canada and Cargojet both fly planes, there's no competition between the two businesses. Cargojet's business is more predictable over the near to medium term, while Air Canada stock is more of a contrarian play. That is, there's a chance that analysts will upgrade their ratings on AC stock should there be positive news about the pandemic.

With Cargojet having a more defensive business, a better balance sheet, and with the stock trading at a bigger discount with greater upside potential, I'm choosing it over AC stock today. What about you?

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