Air Canada (TSX:AC) Q2 Earnings: A Big Recovery in the Making

Description

Canada's biggest passenger airline **Air Canada** (TSX:AC) reported its second-quarter 2021 earnings today. The numbers indicate that the worst is behind and highlight a big recovery is in the making. This should help AC stock that has been trading subdued for the last few months.

Air Canada: Q2 revenues jump 60%

Air Canada's revenues jumped 60% year over year to $837 million during the second quarter. Vaccinations and partial re-openings uplifted its top-line. Notably, Air Canada's net loss also narrowed from $1.75 billion in Q2 2020 to $1.16 billion in Q2 this year.

The flag carrier's effective cost management and increased bookings improved its cash burn. During the second quarter, Air Canada's net cash burn came in at $8 million per day from the average of $15 million per day in the last few quarters.

Its cash burn rate was comparatively lower against global peers almost throughout the pandemic. In addition, a steep fall this quarter highlight a smooth recovery and a road to profitability.

Interestingly, Air Canada's second-quarter earnings have set up a strong foundation for the Q3 and Q4 earnings. Q2 saw a decent air travel demand growth, as the top-line indicates. So, the second half of 2021 will likely see even steeper growth driven by loosening restrictions and more vaccinations. And that's exactly why Air Canada expects its net cash burn rate to fall further to $3 million to $5 million per day in the third quarter.

Air Canada increased its operating capacity by 78% during the second quarter against Q2 2020. It plans to increase the same in the third quarter to cater to the recovering air travel demand.

Notably, Air Canada has a strong liquidity position with a cash of $9.8 billion as of June 30, 2021. After burning billions of dollars amid the pandemic, AC still bodes a strong balance sheet thanks to the Canadian government's generous bailout package.

Importantly, air travel demand seems to recover at a fast pace than earlier expected. Passenger carriers south of the border **American Airlines** and **Southwest Airlines** returned to profits in Q2 2021. Air Canada, too, could follow in the next few quarters, given Canada's slackening travel restrictions.

Risks

I expect the COVID-19 Delta variant to be a very short-term risk for re-openings. Vaccines have been largely effective on virus mutations, so that might not significantly delay recovery.

Another thorn — a serious one — is going to be the rising crude oil prices. Fuel cost makes up around one-third or more of an operating expense of a commercial airline. Air Canada's fuel cost per litre increased by 32% during the second quarter year over year. If energy prices continue to increase, Air Canada's operating expenses will notably increase, which could dawdle its profitability.

Should you buy AC stock?

AC stock is up almost 50% since last year. However, it is still trading 52% lower than its last year's record-high levels. I think it could unlock significant value for shareholders driven by higher demand and improving financials.

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