My 1-Year Prediction for Air Canada (TSX:AC)

Description

Air Canada (TSX:AC) stock has breached the $24 resistance and dipped to $22.87. In my previous articles, I talked about the $24-$30 range-bound series. But the airline stock has dipped below the range, leaving you in doubt about whether it's a buy. When in doubt, look at the fundamental signs and not the stock price. The stock price is about investor sentiments, which fundamentals will eventually influence.

Will history repeat itself?

Air Canada stock is currently at the same position as it was in last September. A year ago, the stock fell below its 100-day moving average of around $17. The month of September and October is seasonally slow for AC. The stock has seen a correction during this time of the year, even before the pandemic from the 2017-2019 period.

On the technicals front, AC stock's Relative Strength Index (RSI) has dipped to 35, closer to the oversold category of 30. I expect some more correction, probably to $20, which is the stock's bottom during the second wave in January. And if you remember, the stock then climbed to $29.72. It is a profit of almost $10 per share, but that is a 50% growth in less than two months.

But that was in the past, and past performance does not guarantee future growth. And the $5.89 billion government bailout has limited Air Canada's upside. In this fourth wave of the pandemic, can the airline stock repeat the 50% upside?

My 1-year prediction for Air Canada

The current market bearishness is an opportunity to buy. What makes me confident? Look at the news. Air Canada is back in the skies. It is opening all international routes, flying cargo for e-commerce, and leveraging its Aeroplan loyalty program. In other words, the airline is firing all cylinders. That doesn't mean Air Canada will miraculously turn profitable after burning $15 million cash daily.

But the airline expects to reduce the cash burn to $3 million to $5 million in the third quarter. When the airline releases its third-quarter earnings on November 2, the stock could see significant growth. At least for some time, you will have to ignore the price-to-earnings ratio. The price-to-sales (PS) ratio would be the highlight during the recovery period. Its current PS ratio of 2.29 times is way above its 2019 average of 0.6. But so is the sales growth. Its second-quarter revenue grew 59% year over year.

The next four quarters could see 50-70% revenue growth because of the weak base year. As Air Canada restarts operations, it is gradually increasing capacity and is no longer cancelling flights. This could increase its operating cost and perhaps accelerate losses for the short term. But you have to take two steps back to make a high jump.

The lifting of travel restrictions has brought some degree of certainty around future cash flows. Next year could be the recovery year. AC would also review other financing and debt restructuring options, and it will try to reduce the use of bailout money.

What is the highest Air Canada stock can go?

I have been reiterating that Air Canada stock is not a buy-and-hold for 10 years. The pandemic has permanently altered international travel, especially for business customers. That is what got Warren Buffett goosebumps, and he exited airline stocks at the dip because he had purchased them in a rally.

The stock market is all about your entry and exit price. If you buy the stock at the bottom of the hill and prepare to climb, you could win. Not all stocks will reach the top of the hill, but you don’t want them to. Even climbing to the base camp is a feat.

Air Canada stock has reached a 52-week high of $31 in March. It may not reach the $50 hilltop before seven years as it carries the weight of $7 billion net debt. But I expect the stock to reach up to $40 base camp. So buy the stock as it falls to $20-$22.

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