



Why Did Bombardier (TSX:BBD.B) Stock Surge Over 75% in a Month?

Description

Bombardier ([TSX:BBD.B](#)) stock has surged more than 75% in the last 30 days after falling 28% in June and mid-July. This stock did a 25-for-1 share consolidation in June to stay on the TSX Composite Index, as the rising interest rates and inflation slowed its recovery. But when this debt-heavy business jet maker reported its second-quarter earnings, it revived investor confidence. Four factors pushed the stock up 75% in a month: industry demand, free cash flow guidance, debt reduction, and investor optimism.

Let's see how these factors affect you as a Bombardier investor.

Industry demand for business jets

There is a growing demand for business jets. Bombardier reported a 37% year-over-year increase in the order backlog to US\$14.7 billion, as demand increased. Its new Challenger 3500 business jets found a [new client](#), Air Corporate SRL. Even though demand is high, supply chain constraints kept aircraft deliveries in check. However, the company maintained its guidance to deliver more than 120 aircrafts this year and generate revenue of over US\$6.5 billion.

The lifting of COVID restrictions increased flying hours, thereby increasing Bombardier's aftermarket revenue. The company is on track to achieve its 2025 revenue target.

Bombardier increases its free cash flow guidance for 2022

The strong revenue growth helped Bombardier turn net cash positive. Strategic priorities and restructuring expanded its adjusted EBITDA (earnings before interest, taxes, depreciation, and amortization) margin to 12.9% in the second quarter from 9.4% in the prior year's quarter. Margin expansion and better working capital performance increased its free cash flow. But the main contributing factor was interest cost savings from accelerated deleveraging.

Bombardier's debt reduction

Bombardier's biggest bottleneck is its long-term debt of over US\$7 billion. Although the next debt maturity is in 2024, it aims to reduce debt as fast as possible. It has repaid US\$773 million in debt year to date by making partial repayments of 2024 and 2025 senior notes. This brought savings in interest costs to such an extent that Bombardier increased its 2022 free cash flow guidance 10-fold from over US\$50 million to over US\$515 million.

Even Moody's upgraded Bombardier's corporate family and senior unsecured notes rating to B3 and maintained a stable outlook. That is a big move for a company that has nearly escaped bankruptcy due to debt. So, investors are buying this stock during a dip.

Overall market optimism

Bombardier's debt levels are high, and it is a risky stock. Its customers are not significantly affected by inflation, but they are affected by restrictions on flying. The overall stock market witnessed a downturn, as rising inflation and interest rate hikes created fear of a recession. The overall stock market saw a recovery from mid-July as signs of inflation easing surfaced. The market believes the worst is over, and the easing of inflation will slow interest rate hikes.

The TSX Composite Index has grown 10.6% since mid-July, pushing all economically sensitive stocks towards recovery. Stocks like Bombardier and **Descartes Systems** surged 75% and 12%, respectively.

Is Bombardier stock a buy?

Although Bombardier stock has surged 75%, you have to look at the risk-return balance. Firstly, the stock is highly volatile, with a beta of 2.57. Beta is a measure of [volatility](#), where market beta is one; the more the stock goes above one, the higher its volatility is. On average, if the market jumps 10%, Bombardier stock could jump 2.5 times the market and vice versa. Secondly, the stock is a small-cap stock and has a debt cost attached to it.

The above risk is mitigated by its US\$1.8 billion liquidity, rising cash flows, and reducing debt. Any news around the three factors will move the stock significantly in the direction where the market is moving. It is not a stock for your core portfolio. But you can buy it to take advantage of the volatility. But invest a small portion of your portfolio.

At present, the stock is overbought. If you own the stock, it is time to book a profit, as it could drop on the slightest negative sentiment. You can buy the stock when it falls 25-30% to below \$23.

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