With the C Series officially dead, Bombardier in a holding pattern

Eric Reguly, Globe & Mail Report on Business
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A year ago, Credit Suisse First Boston published a Bombardier report that slammed the ruling Beaudoin family in *l'estomac*. The "realistic addressable market" for the new C Series jet, then touted as the company's angel of salvation, was a mere 1,500 planes over 20 years, the Wall Street firm concluded. The Bomber's own estimate was almost twice as big.

It turns out CSFB and Bombardier were both wrong, though the former was less wrong than the latter. The market for the C Series, in fact, is precisely zero. The company this week killed the $2-billion (U.S.) project, which would have launched a transcontinental jet with 110 to 130 seats.

With the C Series gone, is the stock gone with it? Certainly, the potential growth story has been eliminated. Still, there could be a surprise in the form of a revival of Bombardier's workhorse regional jets. But pleasant news on that front could be years away. "It comes down to a waiting game that might test investors' patience," says **Anthony Scilipoti** of Toronto's **Veritas Investment Research.**

Hold on. Aren't Bombardier's regional jets, known as CRJs, going the way of the C Series?

Sure looks that way on paper. The CRJs have been aloft since the early 1990s and created a whole new market. Imagine the flying equivalent of the minivan. By the end of 2005, Bombardier had delivered 1,321 CRJs, in models ranging from 50 to 86 seats, to dozens of airlines. The party, though, is over. Brazil's Embraer is proving to be a fierce competitor in the regional jet market, especially at the suddenly popular large end of the spectrum. Airlines now want jumbo shrimp.

At the end of 2004, Bombardier had 233 CRJs of various types in the order backlog. By the end of September, the number had fallen to 136. Only three months later, it was 107.

The fall-off is so extreme, Bombardier will cease production of the 50-seater in a few weeks. The 70-seaters are still selling, though sales are softening, and 29 of them are owed to USAirways, which has propelled itself into the bankruptcy courts twice this decade. In Bombardier's aerospace division, the bright spot is business jets.

Given the trend, it's conceivable that Bombardier could wind down regional jet production and emerge largely as a maker of business jets and trains. What might that cost? Not as much as you might think. After a series of layoffs, the direct employment in the CRJ division, largely in Montreal, is only about 2,000 (the turboprop division in Toronto, where orders are picking up, employs 2,300). It costs Bombardier about $20,000 (Canadian) a head to get rid of an employee. Based on that figure, ending CRJ production would cost Bombardier a relatively insignificant $40-million or so.

But it may not come to that. Orders for all the Big Three commercial aircraft makers -- Boeing, Airbus and Bombardier -- can come and go in waves. In the early 1990s, Boeing looked like a goner in commercial aviation. It came back. The market got roughed up after the 9/11 terrorist attacks and came back again. Last year, Boeing and Airbus together nailed a healthy 2,000 orders, with Asian airlines doing most of the buying.

The Asian airlines have not shown great enthusiasm for regional jets. But that could change as their air travel markets become more developed, more airports are built and the wealth effect creates more flyers. Orders could come rushing in. At that point, all Bombardier would have to do is pray Embraer doesn't emerge as the front runner.

The same thing could happen in United States. The better part of the American airline industry went into bankruptcy protection after 9/11. Eventually, the wing-to-wing restructuring will create stronger, leaner airlines which, eventually, are likely to buy new jets.

All of this is theoretical, of course. What Bombardier investors know is that the company will stop squandering money on the C Series fairy tale. That's a plus. They know that business jet sales are booming. They know that reducing or even suspending regional jet production will not kill Bombardier on the cost front, and that the company faces no immediate liquidity crisis in spite of an underfunded pension plan. They also know that CRJ orders could come roaring back.

So hang on to the stock? That depends almost entirely on your view of the timing of a potential CRJ bounce-back. Months? Years? Never? At a share price of just under $3, the stock seems fully valued, based on the fiscal 2007 profit estimate of about 16 cents a share -- Versant Partners' figure -- and an earnings multiple of 15 (Versant has a $2.75 target on the stock).

What seems certain is that Bombardier will not be an exciting stock in the near term. As **Veritas Research** noted, this is an investment for gamblers with a rare quality -- patience.