Tightened purse strings a drag on Aeroplan rewards program

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Groupe Aeroplan Inc. would love it if Canadians forever flocked to CIBC Aerogold Visa cards, flew constantly with Air Canada and routinely collected points through retail partners such as Esso and Avis.

The popular customer loyalty program, founded in 1984 by Air Canada, has thrived for most of its history, but the recession is taking a bite out of its business, leaving investors wondering whether good times will return any time soon for Aeroplan.

There are five "buys" and four "holds" by analysts covering Aeroplan, according to Bloomberg News. For the former stock market darling, which releases its 2008 financial results today, it seems faint praise to escape with no "sell" recommendations.

Aeroplan's stock price has tumbled 47 per cent since the loyalty program converted into a corporation from an income trust last June. As a trust, Montreal-based Aeroplan enjoyed a charmed life after its initial public offering at $10 a unit in June, 2005. It soared to a record high of $25.30 on Jan. 2, 2008.

But Aeroplan shares sank to a record low of $6 in November, 2008, as the economy tanked and consumers tightened their belts.

The company's business model is based on ensuring a steady stream of revenue from its partners such as CIBC, Air Canada and American Express, which seek to enhance their services by buying Aeroplan miles and distributing them to consumers.

Neil Linsdell, an analyst at Versant Partners Inc., slapped a "sell" on Aeroplan last May, and ***Veritas Investment Research*** issued a report last August that criticized Aeroplan, contributing to negative sentiment on the stock.

Mr. Linsdell said in an interview yesterday that Air Canada's recent financial struggles also spell trouble for Aeroplan, which is now a separate firm. He currently has a "neutral" (hold) on Aeroplan, with a one-year target price of $9 - a penny below yesterday's close.

He said Aeroplan appears richly valued, noting his target price is roughly 16.5 times estimated 2009 earnings per share or 15.3 times 2010 EPS. Aeroplan has an annual dividend of 50 cents a share, or a yield of 5.5 per cent.

With Air Canada scaling back its seat capacity amid weakened travel demand, that could translate into the airline buying fewer Aeroplan miles. As well, consumers aren't spending like they used to, and that means the growth rate may slow on CIBC purchases of Aeroplan miles, Mr. Linsdell added.

Aeroplan will be hurt in 2009 by the recession, notably a 6-per-cent slide to $227-million in gross billings to Air Canada, he said. CIBC is expected to still embrace Aeroplan to promote premium Visa credit cards, but the analyst predicts a reduced growth rate of 11 per cent this year from CIBC business, compared with 12 per cent last year and 14 per cent in 2007.

Mr. Linsdell said he likes Aeroplan's business model of keeping its revenue from partners higher than the costs of consumer redemptions, though he tempered his remarks by saying the frequent-flier plan's expansion will be modest this year.

CIBC accounted for an estimated 38 per cent of Aeroplan's gross billings last year, making the bank easily the No. 1 buyer of Aeroplan miles. Air Canada accounted for 17 per cent of gross billings, while Sainsbury's supermarket outlets in Britain were also at 17 per cent.

In late 2007, Aeroplan set its sights on global expansion after making its first foreign investment with a $755-million deal for the operator of Britain's Nectar rewards program, which includes Sainsbury's. Yesterday, Aeroplan appointed Richard Baker, former chief executive officer at pharmacy chain Alliance Boots PLC, as chairman of its European advisory board in an effort to diversify in Europe.