Is Now the Time to Buy Canadian Pacific Railway Limited?

Description

Ever since Hunter Harrison took over as CEO, it has been a fabulous ride for **Canadian Pacific Railway Limited** (TSX: CP)(NYSE: CP). The shares, which traded below $50 in September of 2011, have skyrocketed since then, and currently trade at $225.

The real key to the company's success has been Mr. Harrison, who has aggressively cut costs and made the railway more efficient. This morning offered a perfect example, when CP reported its results for the third quarter of this year.

More strong results

In Q3 of 2014, CP reported a net income of $2.31 per diluted share, up 26% from a year earlier. This was partly driven by the top line; revenue increased 8.7% year-over-year. But the real key, once again, was lower costs – CP's operating ratio, which measures operating expenses as a percentage of revenue, fell to a record low 62.8%, a decline of 3.1 percentage points. Despite softening commodity prices, CP is firing on all cylinders.

Still some problems

Despite these impressive results, the week may still have been a sombre one for CP. On Monday, the company confirmed that merger talks with Florida-based **CSX Corporation** (NYSE: CSX) had gone nowhere, denying CP the chance to expand its network.

If the merger had gone through, it could have been very advantageous for CP, whose track network is inferior to that of rival **Canadian National Railway Company** (TSX: CNR)(NYSE: CNI). Two problems stand out. One is a lack of access to the East Coast and Gulf Coast. The other problem is CP's reliance on the Chicago hub, where delays can be very lengthy. Thus CP loses critical market share, especially in the growing crude-by-rail business. Adding the CSX network could have fixed those problems.

Is now the time to invest in CP?

Despite these disadvantages, CP has very high expectations. To illustrate, its impressive quarterly results actually fell short of estimates. If expectations were met, then revenue and earnings per share would have grown by 10% and 28%, respectively.

These expectations are why CP trades at such high multiples. More specifically, the stock trades at roughly $225 per share, despite making less than $6 per share so far this year. This is partly why the company has a dividend yield under 0.7%.

The verdict

Today's results were very solid, and Mr. Harrison deserves much credit, even if CP didn't meet its expectations. That being said, the company is far too expensive given its track network deficiencies. If you are insistent on owning a railway stock, CN Rail is the much better bet.

But there are better options than either of the rails. One of them is The Motley Fool's top stock pick for 2014. You can read all about it in the free report below.

CATEGORY

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bensinclair