



## Can Canadian Pacific Railway Limited Really Double its Earnings by 2018?

### Description

In October of last year, **Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) excited both shareholders and analysts alike by announcing an ambitious series of goals for 2018. These goals included, most notably, a \$10 billion revenue target and a doubling of earnings per share from 2014 levels.

Full-year 2014 results indicated that CP Rail is indeed on track, as it reported record revenues of \$6.62 billion (up 8% from 2013), and earnings per share of \$8.46 (up 71% from 2013). This strong performance is on the back of an impressive 200% growth in earnings since 2012.

The question is, can CP Rail keep it up? Whereas CP grew its earnings by 200% since 2012, its revenue only grew by a conservative 9%. This is because the earnings growth was largely due to CEO Hunter Harrison's extensive cost-cutting and efficiency improvement efforts.

In order to double earnings by 2018, CP will need to focus attention away from cutting and towards boosting its top line, an area of concern for analysts and investors. Fortunately, CP Rail has some extremely viable growth avenues to produce the kind of revenue it needs to meet its targets.

### **CP Rail has opportunity to capture intermodal market share**

One of CP's main revenue growth avenues is through expanding its market share in the intermodal space. CP is expecting to grow revenue from intermodal by increasing total carloads by 50%, which in turn represents a 12% compound annual growth rate (CAGR).

This may seem ambitious, but several trends are in place that will continue to grow revenues from this franchise. Intermodal transportation refers to combining train and truck to deliver goods from point A to point B in a single container. Intermodal transportation traditionally competes with straight trucking, but was often seen as a poor alternative due to much slower transit times.

Things have been changing rapidly, however. First, intermodal transportation is able to offer services at a much cheaper cost than traditional trucking. CP Rail estimates that even with the fall in fuel prices—a boon to truckers—rail still enjoys a 20-25% cost advantage.

But what about timing? This is rapidly changing to favour rail as well. CP Rail currently offers the shortest point-to-point Toronto-Calgary route, and has been able to reduce transit time by 20 hours to 61 hours total. This is competitive with trucking, but at a huge 30% discount in price.

In addition, CP has added more double-stacked rail cars to routes, which can transport double the cargo of a standard long-haul truck, at half the cost. With a severe truck driver shortage, CP is well poised to steal market share from trucking and hit its growth targets, especially as CP plans to dramatically improve its velocity over the next several years, which leads us to the next major growth avenue CP possesses.

### **CP plans to further boost its network velocity**

Speed and efficiency are everything for rail, and CP has plans to improve dramatically in this regard. CP plans to boost train speeds by 20% for 2018, a viable objective considering CP Rail trains travel at only 19.3 mph on average, compared to 25.1 mph for its main competitor, **Canadian National Railway Company**.

CP will accomplish this by making key investments in its terminals and corridors. CP has plans to upgrade infrastructure to its key North Line route, which should increase train speed, and add 15% to trainload capacity. CP is also making upgrades to its Vancouver-Calgary lane, which should increase train lengths and lower maintenance costs.

These investments, combined with a \$300 million investment in better Centralized Traffic Control—which should improve communication and increase speed—will collectively improve CP's speed, train weight, and productivity.

### **CP's growth objectives seem reasonable**

Not only does CP plan on gaining intermodal market share from trucking and improving velocity, but it also has ambitious plans to dramatically increase the amount of crude-by-rail it transports.

These avenues combined leave CP with numerous opportunities to double its earnings before 2018. With top notch leadership in CEO Hunter Harrison—who activist investor Bill Ackman described the greatest railroader of all time—investors should be confident in CP's ability to hit its targets.

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1. Investing

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1. Editor's Choice

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1. NYSE:CNI (Canadian National Railway Company)
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