



Should You Buy Canadian National Railway Company or Canadian Pacific Railway Limited?

Description

Over the past five years, investors in Canada's rail providers have done extremely well. During this time, **Canadian National Railway Company** ([TSX:CNR](#))([NYSE:CNI](#)) shares have nearly tripled, while **Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) shares have more than quadrupled.

There are certainly concerns for each of the carriers. Most notably, the crude-by-rail business faces slowing growth and increasing regulation. There are concerns about regulations in other areas, such as grain shipments. Finally, the shares for these companies are not exactly cheap.

That said, this is a very stable industry, one characterized by steady demand, limited competition, and high barriers to entry. So, in a well-diversified portfolio, you should strongly consider holding at least one of these names. Which one should you choose? Well, below we take a look.

The case for CN Rail

At first glance, CN Rail looks like an expensive stock. As of this writing, the stock trades for about 22 times earnings, and the dividend yields only 1.5%. That said, there's a reason why this stock trades at a premium.

CN has been known as the best-in-class carrier for a long time, sporting lower expense ratios than its competitors. So, as the company grows, it's able to add more value to shareholders. Just as important, CN easily has the best track network of any rail carrier. It's the only railroad with access to all three coasts—the West Coast, the East Coast, and the Gulf Coast. The network also bypasses the congested Chicago area, allowing CN to deliver cargo to customers more quickly.

Newspapers have focused a lot on the slowing crude-by-rail business (and we at The Motley Fool have as well). However, CN is still in growth mode—the company hopes to increase earnings by 10%+ this year, and if history is any guide, this target will be reached.

So, if you're looking for a stock to hold for 50 years, this may be the one for you.

The case for CP

Over the past five years, CP has been on a tear, and CEO Hunter Harrison deserves much of the credit. When he took over, the company was easily the least efficient operator in North America, and now it is one of the leaders.

Last quarter, CP's operating ratio (which measures operating expenses as a percentage of revenue) came in at 59.8%. When Mr. Harrison took over, that number went over 80%. This has allowed CP to grow very quickly. Just last year, adjusted earnings per share climbed by 32%, even though revenue climbed by only 8%. So, CP has plenty of momentum on its side, and also has arguably the best leadership of any railroad. Still, I think it's a worse option than CN. The reason is quite simple: valuation.

Based on adjusted numbers, CP trades for over 27 times earnings, a big number for any company in any industry. As a result, its dividend yields a tiny 0.6%, even less than CN. To be fair, the company hopes to grow earnings by 25% this year, but this stock is still too expensive.

At this point, I would certainly choose Canadian National Railway over Canadian Pacific Railway.

CATEGORY

1. Investing

TICKERS GLOBAL

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2. NYSE:CP (Canadian Pacific Railway)
3. TSX:CNR (Canadian National Railway Company)
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