# Do Canada's Major Railway Companies Belong in Your Portfolio?

## Description

The past few years have been very kind to Canada's major railway companies and their shareholders. Since this time in 2009, shares of **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) and **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) have gone up by 224% and 433% respectively.



So, with that in mind, is it too late to jump in? Unfortunately, the answer may very well be yes. Below we take a look at two big reasons why.

**1. Problems for crude by rail**

The crude-by-rail business has grown at breakneck speed, increasing by 4,000% since 2009. This has led to big profits (as well as growth prospects) for the railways, and helps explain why their stock prices have taken off. That said, there are some growing concerns.

Let's start with the obvious: lower oil prices. Despite a recent rally, the price of oil has decreased by about 40% in the past 12 months. And that's caused oil producers to cut the brakes on new drilling—according to **Baker Hughes**, the U.S. oil rig count has fallen for 21 straight weeks. If this leads to lower oil production, then the crude-by-rail business will take a big hit. In any case, we've already had to lower our growth forecasts for crude by rail significantly.

There's another problem with crude by rail: it can be very dangerous. On Friday regulators in the U.S. and Canada took a big step towards dealing with this problem by introducing a series of new safety regulations for the industry. This will raise costs for crude by rail, some of which must be passed on to the customer.

So, without doubt, this industry will not grow as it has in the past. That's not good news for shareholders.

**2. Expensive stocks**

By practically any standard, both CN and CP are trading at sky-high valuations.

Let’s start with CN. Its net income totaled $3.85 per share in 2014, but shareholders don’t see all of this money. Railroading is very capital intensive; lots of money gets gobbled up by upgrading the track network and replacing rail cars. For this reason, CN’s free cash flow totaled only about $2.50 per share. Yet the stock trades at roughly $80. For a company with slowing growth prospects, this is a very expensive stock. It’s no wonder the dividend yields only 1.6%.

CP is even pricier. Last year its net income and free cash flow totaled $8.46 and $3.86 respectively. Yet the stock trades at nearly $240. And to no one’s surprise, CP’s dividend yield is even lower than CN’s at 0.6%.

Don’t get me wrong, the railways are great businesses and will prosper for many years to come. But with their growth slowing, and their valuations still sky-high, I would take a pass for now.

**CATEGORY**

1. Investing

**TICKERS GLOBAL**

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



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1. Investing

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