2 Big Reasons to Prefer Canadian National Railway Company Over Canadian Pacific Railway Limited

Description

When searching for stocks, it's important to look for companies that are immune from new competition. And no companies in Canada are more secure than the two major railways: **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) and **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP).

For this reason, many investors have made CN or CP a long-term holding in their portfolios. But which is the better one? Well, there's a strong case to be made for CN, and below we look at two big reasons why.

1. It's all about the network

In the railroad business, having the best track network is of utmost importance. Put simply, it's what allows railways to deliver goods quickly and reliably. And CN's network is unquestionably better than CP's for a couple of reasons.

First of all, CN's track network has far more reach. The network extends from the Canadian West Coast all the way to the East Coast, and also down to the U.S. Gulf Coast. Meanwhile, the CP network only reaches one coast, the West Coast.

This has profound implications. For example, let's say you're a heavy oil producer in Alberta looking to ship your product down to refineries in Texas and Louisiana. CN can ship the product all the way on its own. CP must switch the car onto another company's network, which takes time. So, your product takes longer to ship with CP. Thus, if you're looking to ship a set amount of oil, you won't need to rent as many rail cars if you choose CN.

Secondly, CP's network passes right through the congested Chicago hub, where rail cars can face delays of up to 24 hours. But CN's network bypasses Chicago, thanks to an acquisition closed in 2009. Once again, this means CN can ship goods faster than CP.

This is why CP tried to acquire **CSX Corporation** last year. The deal fell through due to antitrust concerns. So, for the foreseeable future CP will be at a major disadvantage relative to CN.

2. The price tag is higher for CP

Despite having a worse track network, CP's shares trade at a big premium to CN's. Some numbers will help put proper perspective on this.

In 2014 CN made $3.85 per share in income and $2.53 per share in free cash flow. Based on this writing, its shares trade at 18.7 and 28.4 times these numbers.

The comparable numbers for CP are much higher: 24.2 and 53.1. Granted, CP's income has been growing much faster, but this has mainly come from ferocious cost cutting. And since CP is now the industry's most efficient railway, one has to wonder just how much more cost cutting can be done. The slowdown in crude by rail also puts a dent in CP's growth prospects.

To sum it all up, CP has less to offer investors, yet is more expensive at the same time. The choice should be clear.

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1. NYSE:CNI (Canadian National Railway Company)
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3. TSX:CNR (Canadian National Railway Company)
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bensinclair