Should You Buy Canadian Pacific Railway Limited Before its Earnings Report?

Description

Canadian Pacific Railway Limited (TSX:CP)(NYSE:CP) is reporting its second-quarter earnings results on Tuesday, right after **Canadian National Railway Company's** report, which should shed some light on Canadian Pacific's report. First, let's take a look at Canadian Pacific's business.

The business

Depending on the commodity and length of the haul, railroads are 1.9 to 5.5 times more fuel efficient than trucks. So, rail-based transportation is cost effective and environmentally friendly. Canadian Pacific also places safety as one of its highest priorities.

Canadian Pacific operates a transcontinental railway in Canada and the United States and has about 13,700 miles of tracks, providing logistics and supply chain expertise.

If you decide to invest in Canadian Pacific, then you aren't doing it for the income, but for growth since Canadian Pacific starts you off with only a 0.7% yield.

Sales growth, earnings growth, and valuation

From 2011 to 2014, Canadian Pacific's sales grew between 7-10% per year. However, that growth is showing signs of slowing, as seen in 2013 and 2014.

Year	Sales Growth
2011	
2012	10%
2013	7.7%
2014	7.9%

Then add in the fact that the company trades at a multiple of about 21 at $201 per share. If earnings estimates aren't met, Canadian Pacific's share price will likely decline.

The company’s recent normal multiple is between 21 and 23, which would indicate its shares are priced at a discount to being fairly valued. So, based on valuation, it’s not a bad idea to buy some shares now.

Since Mr. Hunter Harrison took the helm as chief executive officer in 2012, the quarterly dividend has been frozen at $0.35 per share, but the railroad company has improved efficiency, reduced costs, and grown.

Between 2012 and 2014 revenue grew from 5.7 billion to 6.6 billion, or a compounded annual growth rate of 7.8%, essentially doubling the growth rate of 3.8% between 2005 and 2012.

With the payout ratio sitting at a low of 16% compared with the past five years’ 22-48%, a dividend hike could be on the horizon.

In conclusion

I’m not encouraging the timing of the market, but around earnings report time, the market can get especially emotional about a company. Canadian Pacific could go up or down 5% in one day.

Because Canadian Pacific shares aren’t expensive, Foolish investors can act cautiously by buying half a position now and finish off the position after the earnings report.

If you plan to buy $5,000 in Canadian Pacific, you can buy $2,500 of it today and buy more after the earnings report.

If the price goes up, it means the company is doing better than expected. If not, then you might be able to spend the $2,500 and buy more shares at a lower price.

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1. Editor's Choice

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