Canadian Pacific Railway Limited Reports Record Q2 Profit: Is Now the Time to Buy?

Description

Canadian Pacific Railway Limited (TSX:CP)(NYSE:CP), one of North America's largest rail network operators , announced second-quarter earnings results on the morning of July 21, and its stock has responded by making a slight move to the upside. Let's take a closer look at the result to determine if this could be the start of a sustained rally higher and if we should consider initiating positions today.

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The results that sent its shares higher

Here's a breakdown of Canadian Pacific's second-quarter earnings results compared with its results in the same period a year ago.

Metric	Q2 2015	Q2 2014
Adjusted Earnings Per Share	$2.45	$2.11
Revenue	$1.65 billion	$1.68 billion

Source: Canadian Pacific Railway Limited

Canadian Pacific's adjusted earnings per share increased 16.1% and its revenue decreased 1.8% compared with the second quarter of fiscal 2014. The company's double-digit percentage increase in earnings per share can be attributed to its net income increasing 5.1% to a second-quarter record $390 million and its average number of diluted shares outstanding decreasing 6.2% to 165 million. Its slight decline in revenue can be attributed to its total carloads decreasing 3% to 668,000, which more than offset the positive impact of its revenue per carload increasing 1.1% to $2,409.

Here's a quick breakdown of eight other notable statistics from the report compared with the year-ago period:

1. Freight revenues decreased 1.9% to $1.61 billion
2. Other revenues increased 5.1% to $41 million

3. Freight gross ton-miles decreased 6.1% to 66.44 million
4. Revenue ton-miles decreased 5.6% to 36.28 million
5. Operating income increased 10.1% to $646 million
6. Operating margin improved 420 basis points to a second-quarter record 60.9%
7. Free cash flow decreased 66.7% to $173 million
8. Repurchased 3.06 million shares of its common stock during the quarter for a total cost of approximately $590 million

Canadian Pacific also updated its full-year outlook on fiscal 2015, calling for revenue growth of 2-3% from the $6.62 billion reported in fiscal 2014 and adjusted earnings per share in the range of $10.00-10.40, which would result in growth of 17.6-22.4% from the $8.50 earned in fiscal 2014.

This outlook is down from its previous outlook, which called for revenue growth in the range of 7-8% and adjusted earnings-per-share growth of 25% or more. However, the company continues to anticipate an operating ratio below 62%.

Should you buy Canadian Pacific today?

Canadian Pacific held its own in the second quarter despite economic headwinds, so I think its stock has responded correctly by moving higher. I also think this could be the start of a sustained rally higher because the stock still trades at inexpensive forward valuations and because the company has shown a strong dedication to maximizing shareholder value.

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First, Canadian Pacific trades at 20.3 times its median earnings-per-share outlook of $10.20 for fiscal 2015 and 16.8 times fiscal 2016's estimated earnings per share of $12.38, both of which are inexpensive compared with the five-year average price-to-earnings multiple of 25.7 and the industry average multiple of 26.3.

Second, Canadian Pacific pays a quarterly dividend of $0.35 per share, or $1.40 per share annually, which gives its stock a 0.7% yield at current levels. A 0.7% yield is not high by any means, but it is very important to note that the company has increased its dividend three times in the last five years, and its consistent free cash flow could allow for another increase in the near future. Also, the company has been actively repurchasing its shares, including $1.08 billion in repurchases in the first half of the year, and this will help drive earnings higher in the second half.

With all of the information above in mind, I think Canadian Pacific represents one of the best long-term investment opportunities in the market today. Foolish investors should strongly consider making it a core holding.

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