



## Does Canadian Pacific Railway Limited Belong in Your Portfolio?

### Description

**Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) has been one of Canada's top performing stocks over the past four years, but a pullback from the spring highs has investors wondering if the engine is running out of steam.

Let's take a look at the current situation to see if Canadian Pacific is a good buy right now.

### Earnings and cash flow

Canadian Pacific reported strong results for Q3 2015. Year-over-year revenue rose 2% to \$1.71 billion and adjusted earnings per share came in \$2.69, a 16% gain over the same period last year.

The results show the benefit of having revenue streams coming from a variety of economic segments.

When compared with Q3 2014, Canadian Pacific saw declines in its oil, metals and minerals, and intermodal revenues. These were offset by gains in forest products, fertilizers, coal, and chemicals.

For the first nine months of the year, Canadian Pacific generated free cash flow of \$979 million compared to \$610 million in 2014.

### Dividends and share buybacks

Canadian Pacific pays a quarterly dividend of \$0.35 per share that yields about 0.7%.

The company prefers to reward stockholders through its share-repurchase program. In the third quarter the company bought back and canceled 7.74 million shares. So far in 2015, Canadian Pacific has repurchase 13 million shares.

### Efficiency gains

Canadian Pacific used to be a very inefficient operation, but that began to change when current CEO Hunter Harrison took over in 2012.

The new leader launched a program to overhaul the business with an eye on reducing costs right across the board. The results have been nothing short of stunning. When Harrison took control, Canadian Pacific had an operating ratio of about 80%.

That meant that 80 cents out of every dollar in revenue was being used to run the railway. In the latest quarter, the operating ratio came in at just under 60%. That's a big difference and a huge reason why earnings continue to grow.

## **Outlook**

Canadian Pacific plans to grow revenues to \$10 billion by 2018 and double its diluted earnings per share compared with the 2014 results. Harrison outlined the plan last fall and is apparently sticking to it, despite the economic headwinds facing the industry. It will be interesting to see if he can pull it off given the challenges facing the oil and materials sectors.

## **Should you buy Canadian Pacific?**

The stock is a solid long-term holding, but investors might not see the same rate of price appreciation in the coming years because the big earnings gains have come from cost cuts and the huge growth in crude oil shipments. Both of those drivers are running out of steam.

The easy expense reductions have been made and getting the operating ratio down much more is going to be difficult. There's only so much cutting a company can do. As for oil, there isn't much evidence to suggest the rout has run its course.

Notwithstanding, the company is a cash machine and the stock looks reasonably priced. If you already own it, you should continue to do so. For new investors, there probably isn't a rush to buy and you might see a better entry point in the next few months.

## **CATEGORY**

1. Investing

## **TICKERS GLOBAL**

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2. TSX:CP (Canadian Pacific Railway)

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aswalker

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