Is Canadian Pacific Railway Limited or Canadian National Railway Company a Better Pick for 2016?

Description

Both **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) and **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) surged after the Great Recession, but 2015 has been a tough year for the two companies.

Let's take a look at Canada's top railways to see if one looks like a better choice right now.

Canadian Pacific

Canadian Pacific is down 20% this year. The company has been hit by the oil rout, and investors are wondering if CEO Hunter Harrison can find a way to drive the shares higher.

He seems to think so.

Last year Harrison said he plans to grow revenues to $10 billion by 2018 and double the company's diluted earnings per share compared with the 2014 results. The objective appears a bit ambitious given the economic headwinds facing the industry and the company's year-over-year results.

Canadian Pacific reported Q3 adjusted operating income of $685 million, up 10% from the previous year. Revenue came in at $1.71 billion, up 2%. Adjusted earnings per share came in at $2.69, a 16% increase from Q3 2014.

Strong revenues from forestry and fertilizer deliveries offset a slowdown in the oil, metals, and intermodal segments. The numbers are certainly impressive, but hitting the goals outlined for 2018 will require some big revenue gains in the next two years.

Could a takeover help?

Harrison has long said the North American rail industry needs to consolidate, and he is doing his best to put that process in motion. Canadian Pacific is trying to buy **Norfolk Southern Corp.**, but the overtures have not been well received. In fact, Norfolk Southern's board has already rejected three offers, and the situation looks like it could become ugly.

Harrison wanted to do a friendly deal but recently said, “If this is going to be a street fight, so be it.”

Even if Canadian Pacific manages to get Norfolk Southern’s investors to side with it, the deal would still have to clear a number of regulatory hurdles, and industry observers say that isn’t a slam dunk.

Canadian Pacific trades at 20 times trailing earnings and pays a quarterly dividend that yields 0.8%.

Canadian National

Canadian National’s stock has fared much better in 2015. At the time of writing the shares are down just 2% for the year.

The oil crisis has impacted the company’s energy-related revenues, but Canadian National has a built-in hedge with its wide variety of customer segments and routes that run deep into the heart of the U.S. as well as across Canada.

Canadian National delivered Q3 2015 net income of $1 billion, up 18% from Q3 2014. Operating income rose 16% and diluted earnings per share increased 21%.

The company saw strong gains in forestry and automotive revenue as well as a significant boost from U.S.-based earnings.

Canadian National trades at 18.4 times trailing earnings and pays a dividend that yields 1.6%.

Which should you buy?

Canadian National is cheaper and offers a higher dividend yield. The company also benefits heavily from a strong U.S. dollar.

Canadian Pacific is a great long-term investment, but the takeover battle for Norfolk Southern could be a long affair, and investors have to wonder if it will be a distraction for management.

I would go with Canadian National right now.

CATEGORY

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3. TSX:CNR (Canadian National Railway Company)
4. TSX:CP (Canadian Pacific Railway)

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