



Canadian National Railway Company Earnings Today: 3 Things to Watch Closely

Description

It's a crucial day for investors in **Canadian National Railway Company** ([TSX:CNR](#))([NYSE:CNI](#)) as the railroad giant will release its first-quarter numbers after market close. With the stock outperforming rival **Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) to surge nearly 20% in just the past three months, investors are wondering whether there's any more upside left. To figure that out, here are the three things you need to watch closely in today's earnings report.

Is CN's operating ratio improving?

The operating ratio, which compares a railroad's operating expenses to net sales, is a critical measure of efficiency. Expectations from Canadian National have bumped up after Canadian Pacific improved its operating ratio by nearly four percentage points to 58.9% during its first quarter.

As Canadian National has among the lowest operating ratio in the industry, it's imperative for the company to maintain this competitive edge going forward, and that's what investors need to watch for. As a reminder, Canadian National's operating ratio came in at 57.2% and 58.2% for its fourth quarter and 2015, respectively.

Will CN maintain its guidance?

Canadian National last guided its earnings per share to improve a mid-single-digit percentage point in 2016, which falls short of Canadian Pacific's outlook of a double-digit growth in EPS. With key end markets like coal, metals, and petroleum worsening in recent months, it remains to be seen if Canadian National will be able to boost its guidance.

The good news is that fuel prices declined substantially in recent months, which should boost Canadian National's bottom line. However, the company also needs to proactively reduce its administrative expenses to be able to grow its margins when fuel prices recover. In Q4, Canadian National's operating expenses dropped nearly 7% year over year. While I'm expecting the downtrend to continue, I'd like to see a good chunk of it coming off management's focus on improving efficiency and not on lower fuel prices.

Are CN's cash flows growing?

Canadian National's free cash flows need to grow in line with its plans to boost its dividend-payout ratio from 28% to 35% in the near future. The company has outlined plans to invest \$2.9 billion this year on infrastructure and equipment and needs to generate enough cash from operations to be able to pay higher dividends after accounting for capital expenditures.

While Canadian National ended 2015 with more than \$5 billion in operating cash flow, it may struggle to grow its profits and cash flows as business conditions remain weak. That could result in decelerating shareholder returns going forward.

The key takeaway is to look beyond the headlines and see if Canadian National delivers in each of the above areas today. If it does, investors can remain bullish about the stock.

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1. Investing

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1. Editor's Choice

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