



## Canadian Pacific Railway Limited or Canadian National Railway Company: Which Belongs in Your Portfolio?

### Description

As far as investments go, railroads can be some of the best investment decisions you can make. The two largest railroads in Canada are **Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) and **Canadian National Railway Company** ([TSX:CNR](#))([NYSE:CNI](#)).

Railroads are often seen as defensive stocks, because of the sheer size of the networks they operate in which make it virtually impossible for new competitors to emerge.

As far as selecting the better investment, let's take a close look at both.

### The case for Canadian National

One of the things that truly impresses me about Canadian National is how the railroad is the only one in north America with access to three different coastlines. This is a major competitive advantage over other railroads, which need to stop at one terminal, reconfigure to another train line, and then proceed to the coast, often at the cost of significant delays.

In the most recent quarter, Canadian National posted net income of \$972 million, or \$1.25 per diluted share. This came in only just slightly lower than the same quarter last year, whereby \$1,007 million was reported. Revenues decreased by 6% in the quarter, coming in at \$3.01 billion.

Much of the lower than expected figures can be attributed to the weaker economy seen throughout North America in the quarter. Indeed, company executives reiterated that weakness during the most recent earnings call, citing pressure on volumes and pricing.

Impressively, the one area where Canadian National did improve during the quarter was in terms of the operating ratio, which came in at a record-setting 53.3%.

Canadian National recently announced a share-repurchase program. Announced earlier this month, the program and calls for nearly five million shares to be repurchased on a daily basis by the railroad through March of next year.

In terms of providing shareholder value, Canadian National pays a quarterly dividend of \$0.375 per share, or \$1.50 per year. Given the current stock price of just below \$92, Canadian National provides investors with a 1.64% yield and a P/E of 20.13. Year-to-date, the stock has appreciated by 18%.

### **The case for Canadian Pacific**

While Canadian Pacific may lack access to the third port that Canadian National offers, the railroad does offer a compelling network of its own that sprawls from one end of the country to the other.

Canadian Pacific is a vastly different company than it was just three years ago. As recently as 2012, Canadian Pacific was a largely inefficient operation that desperately needed to be whipped into shape. Thanks to a significant investment by billionaire investor Bill Ackman, Canadian Pacific, under the leadership of CEO Hunter Harrison (who was brought in by Ackman), embarked on a period of significant changes.

In just three years, Canadian Pacific's operating ratio went from an industry worst of 81.3% to a very impressive 57%.

This past fall, Ackman sold his stake in the company, and Harrison has announced his retirement and successor—Keith Creel, the current COO and president, who will assume CEO duties on July 1 next year.

In the most recent quarter, Canadian Pacific saw revenues drop by 9% to \$1.55 billion, while diluted earnings per share increased 15% to \$2.34, although much of that can be attributed to ongoing cost cuts at the company. Canadian Pacific also recorded an operating ratio of 57.7%—the lowest yet based on previous quarterly results.

Canadian Pacific pays a quarterly dividend of \$0.50 per share, which results in a yield of 1.02% at the current stock price. Year-to-date, the railroad is trading up 10%.

### **The better investment**

In my opinion, Canadian National is a better pick between the two. What swayed me towards Canadian National were two specific factors: Canadian Pacific's results, which highlight significant cost-cutting efforts but no real growth, and, further to those results and cost cuts, the fact that it seems overvalued. Even Ackman has cut his stake in the railroad.

### **CATEGORY**

1. Investing

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2. NYSE:CP (Canadian Pacific Railway)

3. TSX:CNR (Canadian National Railway Company)
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