Is Canadian National Railway Company a Smart Income Play?

Description

Dividend investments are one of the greatest ways to grow your portfolio. Taking the cash flow and then reinvesting it in more shares of the company, or in other assets, allows for significantly compounded growth. At first glance, **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) doesn't appear to be a great dividend stock, primarily because it only pays a 1.72% yield; however, if we look a little deeper, the possibilities become more clear.

Part of the reason a company is able to pay a dividend is because of its economic moat. The wider the moat, the more difficult it is for competing firms to take over market share. Railroads have incredibly wide moats because of the costs associated with launching a new line. Because it doesn't have to be too concerned with competition, it can reallocate those funds to expansion, optimization, or rewarding investors.

But that's only the start for Canadian National Railway.

Back in January, Canadian National Railway released its full-year financial results. Results were consistent and, in some cases, quite surprising. Revenues for the year dropped by 5% to $12 billion, which would leave any investor concerned if that wasn't coupled with a 3% increase to net income to $3.64 billion. The company brought in less business, but simultaneously, it became more profitable. And along with that, its free cash flow grew from $2.37 billion to $2.52 billion.

A big reason for this increase in net income, despite a drop in revenue, is because of the 2.3% improvement to the operating ratio. I have remained bullish on Canadian National Railway because of the operating ratio, which, at the end of 2016, was at a record 55.9%. For those that aren't aware, the operating ratio is the amount of money that must be spent for every one dollar of revenue. The lower this goes, the higher the margin.

What's significant is that of all the major railroads in North America, Canadian National Railway has the best operating ratio. It improved its gross tonne miles per train mile, increased the number of cars per yard-switching hour, and increased the speed of the train by an entire mile per hour. It might not seem significant, but these add up.

To reward investors for its growth, management increased the divided by 10%. For 17 straight years, management has increased the dividend, which goes to show that management's interests are aligned with investors'. Between 2015 and 2016, management bought back shares, reducing the number from 805.1 million to 779.2 million. And management has authorized an additional share-buyback program, which will reduce those numbers even further.

My problem with Canadian National Railway is that it's expensive, trading at a 20.56 price-to-earnings ratio. This is part of the reason that the yield is as low as it is; however, with cash flow increasing lucratively, I see little reason why the dividend won't increase in future years, especially if it can keep its operating ratio strong. Perhaps don't back up the truck, but having a sizeable position here will increase your portfolio strength.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:CNI (Canadian National Railway Company)
2. TSX:CNR (Canadian National Railway Company)

PARTNER-FEEDS

1. Msn
2. Newscred
3. Yahoo CA

Category

1. Dividend Stocks
2. Investing

Date
2025/08/18
Date Created
2017/03/21
Author
jaycodon