



Why The Drop in Canadian National Railway Company Stock is the Perfect Opportunity to Buy

Description

Picture this: **Canadian National Railway Company** ([TSX:CNR](#))([NYSE:CNI](#)) reports record first-quarter sales volumes & revenues *and* upgrades outlook, but the stock drops after the announcement. That's a real head scratcher, isn't it? For investors, such situations are welcomed, as the market's irrational reactions can offer up excellent opportunities to get to know your company better and even buy the stock.

Why the markets aren't happy, but you should be

If Canadian National delivered such strong numbers, why is the stock falling?

I can see two reasons: First, the market perhaps expected even stronger numbers and outlook given the recovery in end markets. Expectations are, of course, not a valid reason to punish a stock when the company is otherwise performing well.

The second reason seems more logical: Canadian National's operating ratio increased 0.5% to 59.4%. As the operating ratio is a key measurement of management efficiency for a railroad and measures a company's operating expenses versus its net sales, a declining ratio is always better. Just days ago, Canadian National's cousin **Canadian Pacific Railway Limited** ([TSX:CP](#))([NYSE:CP](#)) reported 0.8% improvement in its Q1 operating ratio.

Or wait, that's what the headlines told you.

Canadian Pacific included a one-time gain of \$51 million for the abrupt departure of its CEO Hunter Harrison – he has now joined North American railroad giant **CSX Corp** as CEO – in its operating ratio. Excluding that, Canadian National's operating ratio increased as much as 2.4% year over year to 61.3%.

That suddenly makes Canadian National's numbers look much better, doesn't it? Wait, there's a lot more.

Here are some key numbers from Canadian National's Q1 report, all year over year:

- 9% growth in carloadings, 8% higher revenues.
- 7% jump in operating income.
- 12% jump in net income.
- 45% surge in free cash flow.
- FY 2017 adjusted EPS growth guidance improved to 8-11% from mid-single digit earlier.

Do you see any reason to be bearish about Canadian National here? Neither do I, and this is exactly why the market is horribly wrong to be punishing the stock.

Canadian National is on a strong growth trajectory, and the slight decline in its operating ratio is, by no means, a concern for two reasons.

First, it's a result of rising fuel costs, which is an uncontrollable factor and is affecting players across the industry. Second, and more importantly, Canadian National remains the most cost efficient railroad in the industry.

Management also bumped up its capital expenditure target by \$100 million to \$2.6 billion, which reflects its focus on strengthening Canadian National's infrastructure for greater efficiency.

All said, I believe investors should buy Canadian National stock at every dip, because it remains one of the best stocks to buy and hold for the long term. Now is one such opportunity.

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