Is Canadian Pacific Railway Limited on the Right Track?

Description

When it comes to Canadian railroad investments, **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) is a distant second to **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI).

Shares of CP Rail are still down over 13% from its May 2015 high, but the $200 ceiling of resistance seems to be passed, and it looks like shares are starting to pick up a fair amount of positive momentum.

Should investors give CP Rail a look? Or should they continue to stick with CN Rail, which is considered North America's most efficient railroad?

Many investors have scratched CP Rail off their radars following Hunter E. Harrison's departure. CP Rail simply isn't the high-growth company it used to be; the low-hanging fruit in the form of cost-cutting opportunities has been picked. Most of the easier cuts have already been implemented, and further operational efficiency initiatives are going to take a lot more effort from here.

Simply put, investors shouldn't expect the huge returns they received during the years before the 2015 slump, but that doesn't mean CP Rail isn't worthy of your investment dollars, especially if the price is right.

In general, the rails are places where you want to be right now; they're profitable businesses with huge moats, and as commodity prices improve, all rails will be poised to benefit.

Slowed revenue a cause for concern?

One thing that's alarming is the fact that the CP Rail's revenue growth has halted. Keith Creel, CEO of CP Rail, said that the company's focus "…is top-line growth and that's exactly what my mandate is for my team."

The management team is expanding its sales staff with the hopes that the company can attract more business and improve its relationship with customers.

CP Rail is undergoing a major transformation in the post-Harrison era. The company will still be investing to ensure operations are running smoothly, but the real upside is going to come from CP Rail's ability to retain existing customers and attract new ones.

Bottom line

Going forward, the company is expected to continue to invest in customer-satisfaction initiatives, but ultimately, it's going to be very hard to win customers from CN Rail. It has a larger network which connects all three major North American coasts.

There's a huge cloud of uncertainty following CP Rail right now, but one thing is certain: returns are going to be modest from here, and investors expecting the same magnitude of returns during the Harrison era should look elsewhere to avoid disappointment.

The stock of CP Rail trades at a 20.91 price-to-earnings multiple, which is lower than the company's five-year historical average price-to-earnings of 27.9.

Although cheaper than CN Rail's 21.96 price-to-earnings multiple, I think investors would be far better off by paying a slightly higher price for the higher-quality CN Rail, which is well positioned to deliver many consistent dividend increases in the coming years.

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Date
2025/08/29
Date Created
2017/07/14
Author
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