Why Now Is the Time to Buy Canadian National Railway Company

Description

Few people realize the overwhelming importance that railways have for our economy. **Canadian National Railway Company** (TSX:CNR)(NYSE:CNI) is not only the largest railway in Canada, but it's also an impressive investment option for investors that are contemplating a railway investment.

Here are some reasons why a railway investment is great for your portfolio and how Canadian National is innovating beyond any of its peers.

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Canadian National's moat

The first reason investors should consider a railroad investment has to do with the massive moat they command. Railroads are dependent on massive track networks that have been laid over the years and run through nearly every major metro area on the continent, allowing the railroad to haul everything from crude oil and raw materials to wheat and automotive components.

That track network typically spans tens of thousands of kilometres, making entry to the market cost prohibitive. The notion that a new competitor could emerge and challenge the supremacy of Class 1 railroads such as Canadian National is virtually impossible.

Even the idea of a merger between two smaller competitors to overcome Canadian National's network together is unlikely. The Surface Transportation Board (STB) introduced a series of rules about mergers following a series of Class 1 railroad mergers in the 90s that have all but eliminated the potential of another Class 1 merger from occurring.

Canadian National's moat has another benefit that no other railroad on the continent can boast: access to three coastlines. Canadian National's network spans from coast to coast and then down through the industrial heartland of the U.S. Midwest to the refinery-rich Gulf.

The importance of rail to the economy

The one thing that is misleading about railways is the impact they have on the overall economy. We've all seen long freight trains passing in the distance that can be over a kilometre in length, and it is an overwhelming sight. We often don't think about the sheer number of products, raw materials, and components that are on that train.

Nearly 40% of all freight in the U.S. is transported by rail, which is a significant portion of the economy. This may come as a surprise to some investors, as the stereotypical view of railroads is that they are an outdated relic of the previous century that have no place in a modern economy.

This couldn't be further from the truth.

Reinvestment and improvement

One of the things that is truly impressive about Canadian National is how it continues to strive for improvements, despite already being in a commanding position in the market.

Canadian National announced last month a massive order for 200 new locomotives, which will help it gear up for what it believes will be continued expansion and growth over the next few years.

Another advancement that Canadian National recently made was regarding bitumen — the heavy crude that is produced through the oil sands. Transporting bitumen is currently not as cost effective as sending the crude via pipeline, and it comes with risks regarding safety and the potential for spills.

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A patent filed by Canadian National may soon change that. The company worked with InnoTech to develop a method to turn bitumen into a waterproof floating substance that is more like a bar of soap.

While the technology still needs additional testing, the new technology could open a host of new opportunities.

The most efficient operator

One of the metrics of success among railways is the operating ratio, which is a measure of the company's operating expenses as a percentage of overall revenue. The lower the ratio, the more efficient and the more profitable the railroad is likely to be.

Canadian National remains the most efficient operator among Class 1 railroads, with an impressive 54.7% operating ratio as of the most recent quarter.

By way of comparison, many of Canadian National's competitors have ratios in the 60% range or higher.

In my opinion, Canadian National represents an excellent opportunity for investors looking the long term. The 1.64% yield the company offers may not initially sound attractive, but a steady string of increases and continued solid results can translate into a sizable investment over the long term.

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Date
2025/09/09
Date Created
2018/01/16
Author
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