Canadian Pacific Railway Ltd. (TSX:CP) or Canadian National Railway (TSX:CNR) for Your TFSA?

Description

The railway companies play an important role in keeping the economy moving, and many investors prefer to hold at least one of the industry players in their portfolios.

Let's take a look at **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) and **Canadian National Railway** (TSX:CNR)(NYSE:CNI) to see if one is attractive today.

CP

CP recently signed new contracts with some of its unionized employees, avoiding a strike and shutdown of services that could have been a nightmare for investors and the economy as a whole. The new three-year deal with 1,300 signal workers, and four- to five-year agreements with 3,000 conductors and locomotive engineers should provide some stability to the entire company of 12,000 employees.

The company operates tracks across Canada and into the central United States as far as Kansas City. CP identifies its business groups as bulk, merchandise, and intermodal. Bulk represents 35% of revenue and includes grain, coal, potash, and other fertilizer shipments. Merchandise shipments account for 35% of revenue, and include forest products, energy, chemical, plastics, metals, minerals, automotive, and consumer products.

Intermodal generates 21% of revenue and refers to the container shipments transported by ships, railways, and trucks.

The company reported steady results for Q1 2018. Adjusted earnings per share rose 8% to $2.70 compared to Q1 2017. Revenue increased 4%. The Q1 operating ratio was 67.5%.

CP just raised its dividend by 15.5%. The new payout provides a yield of 1.1%.

A $10,000 investment in CP 20 years ago would be worth about $100,000 today with the dividends reinvested.

CN

CN's rail network extends much deeper into the United States, enabling the company to connect to three coasts.

Management signed a new five-year contract with its 1,800 locomotive engineers in May, and the entire company has about 25,000 employees helping the company move more than $250 billion of goods each year.

CN's business segments are similar to its competitor, but the mix is different, with merchandise shipments accounting for 49% of revenue, intermodal contributing 16%, and bulk kicking in 21%.

First-quarter revenue was pretty much flat on a year-over-year basis. Net income dropped 16%, and adjusted diluted earnings per share fell 13%, compared to 2017. A stronger Canadian dollar and bad weather conditions contributed to the weaker performance. The Q1 operating ratio was 67.8%.

The company now has a new CEO who is ramping up investment to upgrade the network infrastructure and help reduce backlogs in some of its segments. The $3.4 billion capital plan for 2018 is a record.

CN raised its dividend by 10% for 2018 and has a compound annual dividend-growth rate of better than 16% over the past two decades. The payout provides a yield of 1.7%.

Long-term investors have done well with CN stock. A $10,000 investment in the company 20 years ago would be worth more than $220,000 today with the dividends reinvested.

Is one a better bet?

Both CP and CN should continue to be reliable buy-and-hold picks for a TFSA portfolio. The two companies are trading at similar multiples, as CP has improved its efficiency to the point where the operating ratio is similar to CN. Squeezing more out of that metric will be tough, so the easy gains CP enjoyed in recent years might not be there going forward.

Despite the rough Q1 results, I would probably go with CN as the first pick today. The extensive rail network in the U.S. is an important asset, giving the company a key competitive edge. Past returns are no guarantee for future results, but CN has significantly outperformed CP over the long run.

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