Is Canadian Pacific Railway Limited (TSX:CP) Stock a Buy After its Q2 Earnings?

Description

Canadian Pacific Railway Limited (TSX:CP)(NYSE:CP), Canada's second-largest railroad operator, reported its second-quarter results at the close of markets on Wednesday, which topped estimates.

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Shares soared almost 3% on Thursday and are now trading very near their 52-week high of $257.95. However, while revenue rose for the railway in the second quarter, its net income fell, hurt by labour disruptions.

Is Canadian Pacific Railway a buy after its earnings release? Let's have a closer look at the results to see if the company is a good buy going forward.

Strong revenue growth offset by higher costs

Canadian Pacific Railway's quarterly profit fell 9% in the second quarter from $480 million to $436 million. This drop in profit was caused by an increase in expenses due to service interruptions related to a labour strife as well as to a rise in fuel costs.

Per share, profit was $3.04 in the second quarter of 2018, down from $3.27 in the same quarter in 2017.

Excluding one-time items, adjusted profit rose 11% to $453 million, or $3.16 per share, beating analysts' average estimate of $3.12 per share.

Due to the increased expenses, CP Rail's operating ratio worsened and rose from 62.8% to 64.2%.

The Calgary-based railway earned revenue 7% higher in the second quarter from $1.64 billion to $1.75 billion, slightly topping the average estimate of $1.73 billion. Volumes as measured by revenue tonne miles increased 4%, and carloads are up 2% as compared to 2017.

A surge in CP's crude-by-rail business amid rising oil production and tightening pipeline capacity contributed to the company's rise in revenues in the second quarter. About 20,000 carloads of crude was moved in the quarter, which represents about 60 trains a month. The company believes it can grow that number during the third quarter. Higher shipments of commodities like grains and potash also helped to increase revenues.

CP Rail's labour situation has improved after a strike by 3,000 conductors and engineers temporarily shut down the railroad in May. CP has reached long-term agreements with both the Teamsters Canada Rail Conference and the International Brotherhood of Electrical Workers. CP now has 12,800 employees, up 5% compared with last year.

"It is an exciting time to be at CP as we are well-positioned for a strong second half of the year," CEO Keith Creel said on a conference call after the earnings release.

CP Rail should be able to raise prices throughout the year due to strong demand and capacity constraints in both the U.S. trucking market and at its main Canadian competitor, **Canadian National Railway**.

Is Canadian Pacific Railway a buy?

It looks like CP Rail's worst days are behind it. With labour stability now in place, we can expect that CP Rail will have a better second half year. However, the stock is becoming a little pricey, with a forward P/E of 17.

CP's share price is up by 9% this year, outpacing the TSX by about 6%. CP's earnings are expected to grow at an average annual rate of 12.4% over the next five years, while the TSX is expected to grow by 11.4% over the same period. Considering all the above, I consider CP Rail's stock to be a moderate buy at the moment.

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