Should You Buy Canadian National Railway (TSX:CNR) or Canadian Pacific Railway Limited (TSX:CP) for Your Dividend Portfolio?

Description

The Canadian railways have been an investor's dream for decades. **Canadian National Railway** (TSX:CNR)(NYSE:CNI) and **Canadian Pacific Railway Limited** (TSX:CP)(NYSE:CP) are two staple holdings that almost every Canadian dividend investor would hold in their portfolios. Both of these companies have performed very well over the years, with great returns on equity and dividend growth. But should investors hold both of these companies, and if not, which should an investor hold?

Canadian National Railway

CNR is the second-largest publicly traded railroad in North America. The company is active primarily across Canada from coast to coast and in the mid to eastern United States. CNR has a very diversified shipment portfolio, although the largest portion of its shipping revenues come from petroleum and chemical shipments (18%). Of the two rails, CNR appears to have the most diversified product shipments.

The company has some of the most impressive margins in the industry, which has led to some excellent long-term results. Since 2011, CNR has experienced excellent compound annual growth. Revenue over that period grew by 6%, operating income grew by 9%, and free cash flow grew by 8%. Dividends grew by 17% compounded annually over the same time frame, but the financial growth of the company has kept the payout ratio low. Today the company only pays out around 24% of earnings.

Canadian Pacific Railway

With its railroads moving primarily from east to west, CP serves nine ports on its 12,500 miles of rail. Much of its revenues come from bulk commodity shipments (44%) of materials such as various grains and coal. As a result, CP is probably more exposed to commodity prices than CNR, so in a rising commodity price environment, it may benefit more to the upside.

CP has similarly impressive results. In the most recent quarter, the company reported that it had increased revenues by 7% over the previous year. Operating income increased by 3% and free cash flow increased by 37%. The strong financial results helped to power a 15.5% increase in the dividend. The dividend-payout ratio remains low even with that increase at about 15% of earnings, providing confidence in maintaining and increasing the dividend going forward.

What is an investor to do?

Most people who invest in these companies do so for the dividends. While the dividend at cost is currently not large with CNR or CP, coming in at 1.53% and 0.91%, respectively, the dividend growth over the decades has been excellent. Besides, a major reason for the small dividend percentage has been due to the share price appreciation over the years.

If you have the means, buying equal shares in both companies is not a bad strategy. The companies have somewhat different operating regions and strategies, so they are complementary to a degree. But if you have to, or want to, choose one, I would probably go with CNR. It has the larger current dividend, is a larger company, has a lower valuation, and has a greater geographic footprint. In reality, though, either company makes an excellent long-term dividend hold.

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