Which Railroad Should You Invest In?

Description

Railroad investments are some of the most misunderstood investments on the market. The general view of railroads is that they are slow-moving, inefficient and dated relics from the last century with little to no role to play in a modern, increasingly connected society.

Fortunately, investors who have already added a railroad to their portfolio know much better. Railroads continue to play an important role in transporting raw materials and finished goods to storage terminals, ports, and warehouses across the continent, utilizing massive rail networks that were laid in many cases well before the communities around them even formed. In fact, between the amount of freight transported by rail and the extensive rail networks in place, the existing complement of railroads have established an impressive moat over the economy.

The two biggest railroads in Canada are **Canadian National Railway** (TSX:CNR)(NYSE:CNI) and **Canadian Pacific Railway** (TSX:CP)(NYSE:CP), both of which offer advantages to investors.

Let's determine which of the two is a better investment.

The case for Canadian Pacific

Canadian Pacific is the second-largest of the two railroads, with a network that hauls everything from automotive components to wheat from the west coast and through the U.S. Midwest to an eastern terminus in Montreal.

In terms of results, Canadian Pacific recently announced results for the fourth quarter that saw revenues surge 17% over the same period last year to $1.7 billion, and the railroad's operating ratio improved to 56.5%.

In short, the results were record-breaking and showcase the incredible strides the company has made over the years to improve across a variety of fronts.

For income-seeking investors contemplating Canadian Pacific, the company's more conservative yield of just 0.97% may come off as lacking, but in reality, the company's dividend growth over the years has more than matched its peers.

Canadian Pacific currently trades at over $267 with a P/E of 19.64.

The case for Canadian National

Canadian National is the larger of the two railroads, with an extensive network that not only extends from coast-to-coast but also cuts straight down the U.S. Midwest reaching the Gulf region. Access to the Gulf also means that Canadian National has access to three different coastlines in North America, something that no other railroad can attest to.

Another interesting factor relating to Canadian National is what can only be described as the company's grit. It was one year ago this month that an exceptionally long and harsh winter caused a backlog of delays along Canadian National's network, with the end result being that most of Canadian National's deliveries were missed and the company's earnings took a significant dip.

Apart from apologizing, which it did, Canadian National stepped up and invested heavily into upgrading its infrastructure in the impacted areas, and even staffed up and added more locomotives to clear that backlog.

In terms of results, in the most recent quarter, Canadian National reported revenue of $3,808 million, reflecting a 16% gain over the same period last year. Canadian National's operating ratio for the quarter came in at 61.9%

Canadian National's quarterly dividend provides a solid and growing 1.96% yield, and the company currently trades at just shy of $110 with a P/E of 18.63.

Which is the better railroad investment for your portfolio?

Both railroads offer investors a viable path to long-term growth, with their own set of advantages, but in my opinion, Canadian National remains the better of the two options for the following two reasons.

First, while both railroads are experiencing a surge in freight recently due to the ongoing pipeline crisis, Canadian National's' larger network and access to the U.S. Gulf coast and its refineries place the company at a distinct advantage.

Second, there's Canadian National's dividend. Besides providing a higher yield than Canadian Pacific, double-digit growth of that dividend has been a common theme over the past few years that is likely to continue for the foreseeable future.

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