



## CN Railway's (TSX:CNR) Earnings Beat Is Good News for the Economy

### Description

On Tuesday, **Canadian National Railway** ([TSX:CNR](#))([NYSE:CNI](#)) released a quarterly report that surpassed analyst expectations and sent the stock soaring. On Tuesday and Wednesday, CNR shares rose 3.3% on the news, allaying investor concerns that **CSX Corp's** dismal earnings report spelled bad news for railroads as a whole.

However, it's not just railway investors who should be pleased about CN's results.

In addition to being good news for CN, these results also spell good news for the broader economy — and other industries that are tied to overall macro conditions, like banking and real estate. As you're about to see, railroads are a pretty good proxy for overall economic performance, and their results can indicate the direction that the economy is heading in.

First, let's take a look at what analysts were expecting from CN and how it outperformed.

### What analysts expected

Prior to CN's Q2 earnings release, analysts had been expecting adjusted diluted EPS of \$1.65 per share — a significant improvement over \$1.51 the prior year. However, CN actually delivered earnings of \$1.73, beating expectations. The earnings beat was a fairly big surprise to most market watchers, as CSX's earnings miss the previous week had cast a cloud of pessimism over the rail industry in general.

### CN's performance

In addition to growing adjusted EPS by 15%, CN outperformed by a number of other relevant metrics. The company's operating ratio of 57.5 was a 70-basis-point improvement over the same quarter a year before. Operating income grew by 11%, while revenue shot up by \$328 million. Free cash flow suffered, falling from \$900 million to \$500 million, but that was easily explained by an enormous jump in investing activities. All in all, it was a solid quarter for the company.

## How railways correlate with the broader economy

Railways [correlate with the broader economy](#) because their revenue is tied to overall demand for goods. Shipping essential commodities like crude, grain, and coal, CN's business is a proxy for North American economic conditions. The fact that both CN and **Canadian Pacific** [posted good Q2 earnings](#) is therefore a positive sign for the North American economy.

However, it should be mentioned that because CN and CP do significant business with the U.S., their earnings jump isn't necessarily a good omen for the Canadian economy *specifically*. In fact, during the same quarter when CN and CP were both posting record earnings, Canadian GDP growth crawled at 0.4%.

## Foolish takeaway

It's no secret that railroads do well when the economy is doing well and vice versa. However, you needn't be a railway shareholder to feel justifiably optimistic about the good news coming out of CN. Many other Canadian industries, like banking and energy, are strongly correlated with broader economic conditions, so if you own a broad cross section of Canadian industry, you can take CN's earnings news as a bullish signal.

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