Is CN Rail (TSX:CNR) Stock in Trouble?

Description

Canadian National Railway (TSX:CNR)(NYSE:CNI) released its third-quarter results this past week. And while the railway operator continued to do well with sales up 4% year over year and earnings per share also rising by 8%, the big concern for investors may be what lies ahead for not just the company, but the country as a whole.

CN Rail adjusts outlook for 2019

In the company's earnings release, CN Rail said that rather than the double-digit growth it had previously been anticipating in earnings per share for 2019, it was adjusting that figure down, and it will now be in the single digits.

While moving from low double digits to high single digits might amount to a minor change in actual percentage points, it's still a noticeable development, as it highlights the uncertainty ahead for the company.

But it's not just the next quarter that CN Rail is worried about. It also notes that the first half of next year could provide some challenges as well. And while expectations are that the latter half of 2020 should be an improvement, there's no guarantee that will happen as well.

Volumes down from a year ago

As to why CN Rail is adjusting down its estimates, the company blamed "the deterioration in North American rail demand, as the economy continues to weaken." One of the company's key metrics, revenue tonne miles (RTM), is also expected to be weak, as volumes are expected to be down for the year.

Rather than volumes, it's been rate increases that have played more of a factor behind the company's revenue growth in Q3 as well as an increase in intermodal revenue.

RTM saw some big, unfavourable changes across metals and minerals as well as forest products, dropping 13% and 14%, respectively. While the intermodal category was up a modest 2% from the prior year, total RTM was still down 1% overall.

Should investors be concerned?

Even though CN Rail didn't have a bad quarter in Q3, there are clearly many warning signs ahead for investors that shouldn't be ignored. Railway operators are dependent on the strength of the economy, and if CN Rail is already starting to see signs of weakness, it could be an indication that a slowdown could be happening sooner rather than later. And if that's the case, investors may want to consider selling their shares of CN Rail.

Heading into its earnings release, the stock was trading at 19 times earnings and more than four times its book value. Those are some relatively high multiples given that the company isn't generating a lot of growth. Through the first nine months of the year, CN Rail's stock had rallied more than 18%. However, a correction could be in store for the stock in light of its outlook for the next several months.

Bottom line

Without a strong economy, there may be little reason to buy shares of CN Rail today. The stock is a little pricey, and with a dividend yield of just 1.8%, it's not that attractive an option for dividend investors , either.

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