Market Rally Alert: Time to Buy Canadian Pacific Railway (TSX:CP) Stock?

Description

Canadian Pacific Railway (TSX:CP)(NYSE:CP) is one of the largest stocks in Canada, with a valuation of $44 billion. Shares dipped as a result of the coronavirus pandemic, but a recent market rally has pushed the stock price towards previous highs.

There's no doubt that railroad stocks are the lifeblood of the Canadian economy. They carry raw materials and consumer products, but also crude oil and agricultural produce. If the economy does well, so do railroads like Canadian Pacific.

This is what makes the recent market rally confusing. Last month, Trudeau unveiled the worst jobs report in Canadian history. More than three million people have either lost their jobs or seen their hours reduced. Because these are lagging indicators, more pain is expected.

Why is CP stock rising alongside the market rally? Are shares really a buy?

This is a big story

Since 2006, CP stock has risen by 450%. **The S&P/TSX Composite Index**, for comparison, rose by just 22%. Those figures are *after* the recent market rally. There's clearly something special about this stock.

Railroads are terrific businesses. That's why Warren Buffett owns one of the largest rail operators in the world: Burlington Santa Fe. These companies fit Buffett's investing strategy perfectly. They have irreplaceable assets with permanent competitive advantages.

Canadian Pacific, for example, owns the shortest and fastest routes between Canada and the United States. It also operates the quickest, most consistent rail route connecting Eastern Canada and Vancouver.

The company also operates more than 100 transloading facilities across the country, giving it direct access to areas not served by its rail line. Just as important, Canadian Pacific's vast transit network allows shippers to access *both* coasts, allowing it to export and import to multiple continents with ease.

The market rally has propped up Canadian Pacific stock, as investors are anticipating higher shipping volumes as a result of renewed confidence.

What exactly is the company shipping? Nearly everything. Around 40% of revenue comes from bulk services, like grain, potash, and coal. Another 40% is merchandise like automobiles, forest products, metals, minerals, oil, chemicals, and plastics. The remaining 20% stems from intermodal transportation, which provides services to trucking companies.

No matter how you slice it, Canadian Pacific is reliant on the Canadian economy. Whether it's production or consumption, economic activity needs to keep a steady pace for the company to generate meaningful profits.

Buy the market rally?

Especially when factoring in a slowdown for the most recent quarter, Canadian Pacific stock *isn't* priced at a discount to its historical trading range. There are dozens of dirt-cheap stocks following the coronavirus crash, but this isn't one of them. That's partially why the stock hasn't popped as much as others during the recent market rally. There simply wasn't as much downside to correct for.

Due to its extreme reliance on the Canadian economy, it's hard to see how CP stock is a buy at these levels. Profits may be helped by a surge of demand from oil producers looking to offload their output in light of pipeline capacity restraints, but that's just one segment of revenue. The rest of CP's business will surely see lower volumes and weaker pricing in the quarters to come.

Make no mistake: this is still a terrific business to own for the long haul. But if you want to capitalize on the market rally, this stock has much less upside than other low-priced options.

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