A Great Defensive Moat Your Portfolio Needs

Description

Since the COVID-19 pandemic began, the need to insulate portfolios with a wide defensive moat has grown. In short, extreme volatility coupled with large swaths of the businesses operating at reduced capacity has wreaked havoc on markets. Adding to this is the fact that a viable vaccine could be more than a year away could make this volatile environment the norm for some time.

So, what exactly can investors do? Is there an investment that can provide both a defensive moat and a source of income? Fortunately, the answer to that is a resounding yes!

Now boarding: Your defensive moat

Canadian National Railway (TSX:CNR)(NYSE:CNI) is the largest railroad in Canada. I realize that railroads don't exactly come off as stellar investments for 2020, at least at first glance. The stereotype often attributed to railroads is that they are antiquated relics, with no place in our modern world. In reality, that couldn't be further from the truth.

First, let's talk about the tracks that railroads require. Canadian National boasts a track network that is over 31,000 km in length. That network was built around and through communities stretching across the entirety of Canada and through the U.S. to the Gulf coast. In fact, Canadian National is the only railroad in North America that is connected to three coastlines. That fact alone is a defensive moat worthy of any portfolio, but there's still more.

In other words, Canadian National's impressive network provides a competitive advantage over its peers that is nearly impossible to challenge. The same could be said for new market entrants. The costs and construction necessary to build a new railroad to compete with Canadian National are immeasurable.

Even a merger among Canadian National's peers seems unlikely. Following a series of railroad mega-mergers in the 90s, the Surface Transportation Board imposed strict criteria on how large Class I railroads can merge.

In summary, Canadian National has a massive defensive moat. But is a defensive railroad a *good* investment?

CN is a diversified, profitable investment

Canadian National hauls $250 billion worth of freight each year. That freight can be anything from automotive parts and chemicals to crude oil and wheat. In terms of results, Canadian National reported revenue of $3,545 million in the most recent quarter.

The results, which were inclusive to the end of March were flat over the same period last year. From an earnings standpoint, Canadian National reported $1.42 per diluted share, reflecting an impressive 31% improvement over the prior year. The operating ratio, which is a key indicator among railroads, came in at 65.8%, reflecting an improvement of 3.8 points.

The railroad's strong and diversified business provides another benefit to investors. Currently, Canadian National offers a quarterly dividend, which currently provides a yield of 1.97%. That might not resonate for income-focused investors, but keep in mind that defensive moat I mentioned above. CN's payout ratio, which stands at 35% only adds to that view.

It's also worth noting that Canadian National has continued to provide handsome upticks to that dividend on an annual basis that goes back over two decades.

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Date

2025/09/29
Date Created
2020/06/27
Author
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