Is CN Rail (TSX:CNR) Stock a Buy Before Earnings?

Description

The earnings season is about to ramp up. This week, there are several high-profile TSX-listed companies scheduled to report earnings. Among them, **Canadian National Railway** (TSX:CNR)(NYSE:CNI) is on deck to report second-quarter results after the close on Tuesday.

This quarter will be among the most watched in recent history. Investors will finally get insights into the impacts of COVID-19 mitigation efforts and the subsequent economic shutdown.

Is CN Rail a buy before earnings? Let's take a look.

Q2 expectations

Analysts are expecting CN Rail to post earnings of $1.26 per share and revenue of $3.25 billion. This represents drops of 27.17% and 17.90% over the second quarter of 2019.

Looking forward, Canada's largest railway is expected to see full-year earnings drop by 20.1% and 13.3% in 2020 and 2021, respectively. Revenue is expected to drop by 7% in 2020 before rebounding by 1.9% in 2020.

Given this, it is somewhat surprising to see that the stock is hitting 52-week highs. On Friday, CN Rail closed at $129.50, which is an all-time high, and at a 7.6% premium to analysts' one-year average price target of $118 per share. The company is a long way from March's 52-week low of $92.09, and one must question whether the big bounce is justifiable.

This is especially true when one considers that the Bank of Canada expects GDP to drop by 7.8% in 2020. In fact, analysts don't expect the economy to reach pre-pandemic levels until at least 2022.

As railways are a bellwether of the economy, CN Rail's second-quarter results will be closely analyzed.

Historical performance

Although CN Rail's stock price looks pricey given estimates, it has a history of delivering. Over the past 12 quarters, earnings have either beat, or been in line with analysts' estimates.

That being said, revenue is less consistent. Over the past 12 quarters it has beat seven times and missed on five occasions.

It is also worth noting that revisions have been trending downwards. Over the past 90 days, 15 analysts have revised downwards, and earnings estimates now sit 26% lower than where they were only 90 days ago.

Given these downwards revisions, even an earnings beat may not be enough to push its CN Rail stock upwards. In fact, it will likely require a meaningful beat along with a better-than-expected outlook to drive any meaningful share price appreciation.

Is CN Rail a buy?

On the basis of earnings alone, CN Rail stock is not one I'd aggressively accumulate. The stock price is hitting all-time highs, despite the fact that earnings and revenue will drop in a meaningful way.

This also means that the company is trading at pretty expensive valuations. It is now trading at 24 times earnings, which is quite pricey for a stock that will not grow earnings for another two years.

Need another reason to avoid CN Rail's stock before earnings? Last week, the company entered overbought territory with a 14-day RSI of 72. This means that it is likely due for a short-term dip — a dip that may come along with second-quarter earnings.

All things considered, investors should pay close attention to management's commentary on the outlook for the second half. As a CN Rail shareholder myself, I'd choose to wait for a meaningful pullback before adding to my position.

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