Better Buy: CN Rail Stock or CP Rail?

Description

The Canadian rail stocks have been impressive performers over the past year, with **CN Rail** (TSX:CNR) and **CP Rail** (TSX:CP) shares both putting the broader TSX Index and S&P 500 to shame. Indeed, the railways have incredibly wide moats, with some of the strongest (and most durable) cash flow streams out there.

Though valuations have swollen amid the impressive rise of the rail stocks, there are reasons to believe that such hefty multiples could become even loftier in time. With rising interest rates and more emphasis placed on real fundamentals over promises or growth stories, CN and CP stocks look that much more attractive relative to the fallen tech titans that have now burst in the 2022 stock market selloff.

The tech sector is ailing, and while the profitable firms will rise from the rubble, nobody knows what the fate of the names that have imploded 80-90% will be in the new year and beyond. Profits matter, and you cannot simply rely on low interest rates for your survival. Eventually, investors will expect earnings or, at the very least, some progress on the margin front.

Now that value and fundamentals trump growth, it's the boring (and beautiful) rail plays that keep chugging along. With quarterly earnings supporting their rallies, I expect Canadian investors simply can't go wrong with having either CP or CN as one of their TFSA's core holdings for the long run, even at today's valuations.

Let's have a closer look at which name is the better buy for 2023 and beyond.

CN Rail stock

CN Rail is the $116 billion behemoth with one of the most dominant networks out there. The company is holding strong after a terrific quarterly beat that saw Canadian volumes rise impressively. Despite the beat, it was worth noting that CN Rail encountered a 15% pop in operating expenses, primarily due to higher energy prices. As energy prices cool off in the new year, and the company does its best to keep goods flowing in a potential recession year, there's a good chance that CN can improve its operational efficiency amid macro headwinds.

CN chief executive officer Tracy Robinson noted of the firm's "disciplined execution" of its operating plan to improve upon both "effectiveness and efficiency." Indeed, CN is on its way to becoming an efficient railway again after years of falling short of rivals like CP.

At 23.5 times trailing price to earnings (P/E), CNR stock is a solid buy. The 1.72% dividend yield is modest but slated to grow quickly over the next 10 years.

CP Rail stock

CP Rail is a $101 billion rail juggernaut that seems unstoppable of late. The stock is flirting with new highs in the $110-per-share range. With Kansas City Southern assets in the mix, CP makes a strong case for why it should be viewed as a more fierce competitor in the North American rail scene.

CP Rail has been firing on all cylinders, with solid grain shipments and excellent execution. Legendary investor Bill Ackman is back in the name, and I think it'll be a rewarding ride for the man as he seeks more gains in a potential recession year.

The better rail stock to buy now?

My concern with CP Rail stock is valuation. The stock is very pricey at 34.84 times trailing P/E. While CP may have more going for it post-merger with Kansas City Southern, I'd argue the price tag makes it less appealing than CN Rail stock at this juncture.

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