Canadian National Railway (CNI)

Updated October 26th, 2023 by Nathan Parsh

Key Metrics

Current Price:	$106	**5 Year CAGR Estimate:**	6.7%	**Market Cap:**	$68 B
Fair Value Price:	$94	**5 Year Growth Estimate:**	7.0%	**Ex-Dividend Date:**	12/06/23
% Fair Value:	112%	**5 Year Valuation Multiple Estimate:**	-2.3%	**Dividend Payment Date:**	12/28/23
Dividend Yield:	2.2%	**5 Year Price Target**	$132	**Years Of Dividend Growth:**	28
Dividend Risk Score:	B	**Retirement Suitability Score:**	B	**Rating:**	Hold

Overview & Current Events

Canadian National Railway is the largest railway operator in Canada. The company has a network of approximately 20,000 route miles and connects three coasts: the Atlantic, the Pacific and the Gulf of Mexico. It handles over $200 billion worth of goods annually and carries over 300 million tons of cargo. The company is cross-listed on the New York Stock Exchange, where it trades under the ticker CNI. Although the company reports financial results in Canadian Dollars, all figures in this report are in USD, as the railroad's NYSE-listed shares have been used for the purpose of valuation analysis.

On January 24th, 2023, Canadian National Railway increased its dividend 3.1% for the March 31st, 2023 payment date.

On October 24th, 2023, Canadian National Railway reported third quarter results for the period ending September 30th, 2023. For the quarter, revenue fell 12.5% to $2.9 billion, which was $50 million less than expected. Adjusted earnings-per-share of $1.23 compared unfavorably to $1.57 in the prior year and was $0.02 below estimates.

For the quarter, Canadian National Railway's operating ratio was higher by 480 basis points to 62.0%. Revenue ton miles (RTM) decreased 5.0%. Revenue results amongst individual product categories were mostly down for the year, though grain and fertilizers (+16%) and automotive (+14%) remained strong. Intermodal (-34%) was the worst performer, but Forest Products (-15%) and Petroleum and Chemicals (-11%) were both down double-digits. Car velocity and terminal dwell both fell 1% and train length declined 3% while fuel efficiency improved 1%. Finally, the company increased its share repurchase authorization $500 million to $4.5 billion, or 6.5% of its current market capitalization.

Canadian National Railway continues to project adjusted earnings-per-share will be flat to slightly negative for the year, down from a prior outlook of up mid-single-digit percentage. We now expect that the company will earn $5.24 in 2023, down from $5.67 previously. updated our forecast accordingly.

Growth on a Per-Share Basis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
EPS	$2.88	$3.23	$3.20	$3.44	$3.82	$4.31	$4.41	$4.00	$4.75	$5.67	*$5.24*	*$7.35*
DPS	$0.81	$0.86	$0.90	$1.12	$1.25	$1.39	$1.62	$1.64	$1.96	$2.25	*$2.36*	*$3.31*
Shares[1]	831	809	787	762	743	735	717	711	701	677	*656*	*630*

Canadian National Railway has grown its earnings at an approximately 8% average annual rate during the last decade, but it has slowed to a 6.5% annual growth rate in the last five years. Still, we believe that the company is capable of delivering more than 6% growth moving forward. More specifically, we are forecasting 7% long-term growth in per-share earnings for company due to increased revenues and share repurchases. Applying a 7% growth rate to our 2023 earnings-per-share estimate of $5.24 allows us to compute a 2028 per-share-earnings estimate of $7.35. The company has been an aggressive repurchaser of its own shares over the last decade, reducing the share count by more than 2% annually over this period.

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[1] Share count in millions

Disclosure: This analyst has no position in the security discussed in this research report, and no plans to initiate one in the next 72 hours.

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Valuation Analysis

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	Now	2028
Avg. P/E	17.6	19.6	19.2	17.8	20.1	19.1	20.0	23.6	25.9	21.0	*20.2*	*18.0*
Avg. Yld.	1.6%	1.4%	1.5%	1.8%	1.6%	1.7%	1.8%	1.8%	1.6%	1.9%	*2.2%*	*2.5%*

Shares of Canadian National Railway are down $12, or 10.2%, since our July 28th, 2023 report. The stock has traded at an average price-to-earnings ratio of 19.8 over the last decade and is currently trading at near this level today. We are reaffirming our target price-to-earnings ratio of 18. If Canadian National Railway's price-to-earnings ratio contracts to this target then annual returns would be reduced by 2.3% over this period. We see the stock as slightly overvalued today at 112% of fair value.

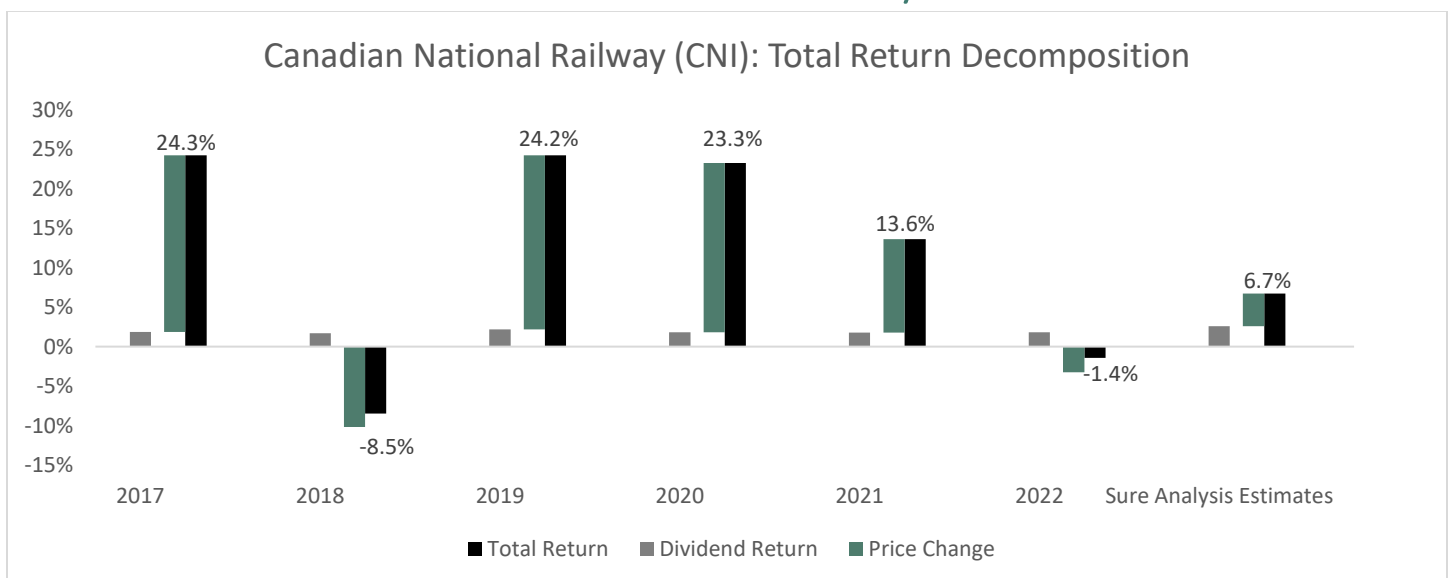## Safety, Quality, Competitive Advantage, & Recession Resiliency

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2028
Payout	28%	27%	28%	33%	33%	32%	37%	41%	41%	40%	*45%*	*45%*

Canadian National Railway benefits from operating in the railway industry, one of the sectors with the highest barriers to entry. The capital and expertise required to build new railways is tremendous. Moreover, the railway industry is saturated and is structured as an oligopoly, which results in virtually no new entrants and minimal competition. Canadian National Railway is also quite shareholder-friendly, as the company has increased its dividend payment (in Canadian dollars) for 28 consecutive years.

Final Thoughts & Recommendation

After third quarter results, Canadian National Railway is now expected to offer a total annual return of 6.7% through 2028, up from our previous estimate of 6.0%. This projection stems from a 7% earnings growth rate and starting yield of 2.2%, offset by a low single-digit headwind from multiple contraction. Canadian National Railway has now turned in several mixed quarters. The company also expects to see an EPS decline in 2023 as most product categories are seeing decreases in revenue. We have lowered our 2028 price target $11 to $132 due to EPS estimates for the year, but maintain our hold rating on Canadian National Railway due to projected returns.

Total Return Breakdown by Year

Canadian National Railway (CNI): Total Return Decomposition

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Income Statement Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Revenue	10270	10991	9881	9089	10063	11051	11239	10314	11547	13149
Gross Profit	4048	4522	4435	4074	4379	4601	4585	4307	4841	5685
Gross Margin	39.4%	41.1%	44.9%	44.8%	43.5%	41.6%	40.8%	41.8%	41.9%	43.2%
D&A Exp.	952	951	907	925	988	1026	1177	1186	1275	1329
Operating Profit	4048	4522	4435	4074	4379	-2212	-2440	-2441	4841	5685
Operating Margin	39.4%	41.1%	44.9%	44.8%	43.5%	-20.0%	-21.7%	-23.7%	41.9%	43.2%
Net Profit	2537	2869	2772	2749	4231	3340	3177	2659	3902	3934
Net Margin	24.7%	26.1%	28.1%	30.2%	42.1%	30.2%	28.3%	25.8%	33.8%	29.9%
Free Cash Flow	1530	1888	1907	1893	2194	1842	1551	2464	3254	3011
Income Tax	949	1081	1047	972	(305)	1045	914	733	1149	1264

Balance Sheet Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Total Assets	28328	27296	26232	27485	29924	30259	33518	35136	38068	37328
Cash & Equivalents	201	45	110	131	56	195	49	446	657	242
Acc. Receivable	765	799	633	649	783	858	929	827	842	1010
Inventories	257	289	256	269	337	409	468	457	462	510
Goodwill & Int.	55	53	51	50	49	54	175	169	164	298
Total Liabilities	16163	15693	15459	16478	16678	17307	19707	19725	20230	21572
Accounts Payable	383	400	282	359	587	721	663	612	708	2052
Long-Term Debt	7363	7212	7514	8112	8611	9228	10561	10121	9792	11368
Total Equity	12165	11603	10773	11008	13245	12952	13811	15411	17838	15756
LTD/E Ratio	0.61	0.62	0.70	0.74	0.65	0.71	0.76	0.66	0.55	0.72

Profitability & Per Share Metrics

Year	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022
Return on Assets	9.2%	10.3%	10.4%	10.2%	14.7%	11.1%	10.0%	7.7%	10.7%	10.4%
Return on Equity	21.8%	24.1%	24.8%	25.2%	34.9%	25.5%	23.7%	18.2%	23.5%	23.4%
ROIC	13.5%	15.0%	14.9%	14.7%	20.7%	15.2%	13.6%	10.7%	14.7%	14.4%
Shares Out.	831	809	787	762	743	735	717	711	701	677
Revenue/Share	12.14	13.35	12.27	11.67	13.29	14.98	15.55	14.47	16.26	19.10
FCF/Share	1.81	2.29	2.37	2.43	2.90	2.50	2.15	3.46	4.58	4.37

Note: All figures in millions of U.S. Dollars unless per share or indicated otherwise.