NEWS

www.cpr.ca (TSX:CP) (NYSE:CP)

Transcript

Scotiabank Transportation and Aerospace Conference

November 14, 2017

Toronto, Ontario

Corporate Participants:

John Brooks, CMO Canadian Pacific

Other Participants:

Turan Quettawala, Analyst Scotiabank

QUESTION AND ANSWER SECTION

Turan Quettawala

Analyst, Scotiabank

John Brooks was appointed SVP and CMO at the Canadian Pacific in February of 2017. John started his railroading career with Union Pacific and has held various senior positions in all segments including coal, intermodal, chemicals, merchandise and grain over the last 20 years. John, it's a pleasure to have you here at our conference.

John Brooks

CMO, Canadian Pacific

Thank you. Thank you for having me.

Turan Quettawala

Analyst, Scotiabank

So, it's probably been a pretty busy year for you here with lots of new products that you've put in place and certainly, we're hearing a lot of good things about service from a bunch of the stakeholders that I speak to. So, as you look into 2018, do you believe that the product suite is pretty much set up or are there a lot of changes still that are likely to come?

John Brooks

CMO, Canadian Pacific

You know what, that's a great question. So, 2017 was very busy and I'm super-excited about sort of the rebuilding we've done in our intermodal franchise in particular. We've introduced a couple of new products into Detroit, Ohio Valley. We've introduced a transload in Vancouver as we focus on building more exports for our customers. So, I'm pleased with that progression.

But I can tell you as you think forward into 2018, 2019, just having good service, transporting from A to B fast is not enough. So, we need to continue to think about how we put dots on the map, work with our partners to extend our reach. As I think about our transload franchise in particular, as you think across our network in the major hubs we have in Chicago, in the Twin Cities, in Toronto, in Calgary, in Vancouver, we've got significant footprints available to us to build our transload space, and I think that helps bring density of customers into the future for CP.

Turan Quettawala

Analyst, Scotiabank

Okay. And I guess does it give you better backhaul, too, or...

John Brooks

CMO, Canadian Pacific

Well, certainly on the intermodal side, well, and frankly on the carload side, the more export opportunities we can create, whether it'd be through transloading or extending our reach in the case of the Ohio Valley, certainly brings the economics of backhaul for our international shippers or actually as you look at growing our transloading presence for our merchandise business in the Chicago or Twin Cities market, that brings a natural opportunity to sort of partner on opportunities and potential backloads in those commodity areas, too.

Turan Quettawala

Analyst, Scotiabank

You talked about putting more dots on the map, and I think I want to talk a little bit about sort of your competitor recently announced a relationship with NS in terms of planning to move some interchange out of Chicago. I know that's not necessarily putting dots on the map right now, but it potentially could over the long-term if that becomes a bigger, fuller relationship. Are you thinking about doing something similar with another railroad? Is that a possibility? And I guess is there something that keeps you out of an NS relationship?

John Brooks

CMO, Canadian Pacific

Yeah. No, I don't think so at all. I mean, look, all the carriers are working actively together, particularly in the Chicago market. Certainly, Hunter and Keith have long been vocal around the need to sort of continue to innovate how we get traffic through Chicago. I think this was an opportunity where it made sense for CN and NS to move some of their merchandise traffic.

I can tell you we've been discussing and continue to talk with NS or CSX. Certainly, CSX, as Keith has mentioned, our largest Chicago interchange partner, so there presents a natural opportunity and obviously bring together a kind of two like operating minds, and I do, I think there is a world of possibility there too, but it's just not a CP-CSX, CN-NS story. I think that opportunity evolves by commodity type, by market reaches. So I think there's a lot of opportunity for carloads.

I'll give you an example. You look at the reinvention of us getting into the Detroit. Clearly, that was a product we put together. We looked at a number of different route options. When it ultimately developed, it made sense to work that with CSX. Now, look, we're going to start running intermodal directly into the Ohio Valley. That's with a short-line partner, Genesee & Wyoming. So I don't think there's one single recipe there. It's all about trying to figure out what makes the most operational sense and then, sort of putting those principles in place.

Turan Quettawala

Analyst, Scotiabank

Sounds good. What about the team? It would be great if you could talk a little bit about the team that's working with you on the sales and marketing side right now. Is it pretty much complete? Are there still sort of few positions that you may like to fill?

John Brooks

CMO, Canadian Pacific

Yeah. It's interesting. It's certainly the sales and marketing team has been an evolution similar to the operating team went through. We've had a lot of change. Now that being said, if I looked at the sales side of the house, I'd say we're in the late innings of the ball game. We're pretty well set. I feel good about it. We've got a, what we call, high-performance sales culture. Our sales people are partially based on commission. They're aggressive. Maybe the old CP, you saw, you walk in the office, a lot of salespeople sitting behind desks. There's not many salespeople sitting behind desks anymore at CP. They're out in the field. So I feel good about that. We're probably in the mid-innings as I think about our marketing team.

So we've got a little work to do there yet. I tell you I spent the first eight months of being the CMO, probably 80% of my time sitting down with my individual marketing managers. And the reason being is we want to grow CP at a disciplined level. But to do that, you got to surgically have strategies in place, commodity-by-commodity, customer-by-customer, on how you want to grow this to maximize our franchise and our value versus sort of just selling and shotgun blasting out there. So middle innings in the marketing side. We're going to do some things to add some people yet in sales and marketing and look for more to come on that in the coming months.

I think just on the people side that's worth mentioning also, we recently are going to beef up our presence in Asia. We're putting a person in Shanghai. We're also looking at putting a person in Singapore and a critical piece of that is how we do a better job of linking our total supply chain into those end users. So we're excited about that.

And then, I'd say the last thing on the people front, it's critically important to our CEO Keith, and myself that we have a very tight knit group with our operating team. To me, it's the special recipe that we have at CP that's going to enable growth. So I can tell you whether it'd be myself or my leaders in the commodity groups, we work close with Keith and the operating team daily on how we sell into our franchise.

Turan Quettawala

Analyst, Scotiabank

So you mentioned a great word there, discipline. You know, CP is obviously looking to gain market share over the next one to two years. I don't think that's a surprise to anybody. I understand there's – not all of it is going to come from your primary real competitor, but can you talk a little bit about pricing? There's a lot of investor concern I'd say about potential for weaker pricing in Canada because of some of these, let's call it, market share gains.

John Brooks

CMO, Canadian Pacific

Yeah, I think first of all, I'd say if all the indicators continue to move in the right direction, which we're hopeful they will, I think there's a lot of growth opportunity for both CN and CP. Over the prior few years that we haven't bound ourselves to a lot of long-term contracts.

Now certainly, we've got strategic partnerships and where there's capital involved, we've done longer term commitments. But we've tried to keep ourselves fairly flexible in our contracts and then also moving more into tariff where we can. And I think that's going to bode us well as we look into 2018 and if we get the tailwind on pricing that we think could happen, then we've got a fair amount of our book that rolls over and we'll take advantage of that.

Turan Quettawala

Analyst, Scotiabank

Can you give us a percentage of the book roughly?

John Brooks

CMO, Canadian Pacific

There's certainly some big chunks as you think about potash and coal that are bound to longer term agreements. But we look at close to 50% of our book rolling over.

Turan Quettawala

Analyst, Scotiabank

Okay. Excluding those contracts?

John Brooks

CMO, Canadian Pacific

Yeah, excluding them.

Turan Quettawala

Analyst, Scotiabank

I guess as we think about 2018 volume growth, I think you've kind of alluded to mid-single-digit RTM growth in 2018. I was wondering if you can touch upon maybe some of the segments where you think the growth mainly comes from and then maybe even some areas that you worry about a little bit.

John Brooks

CMO, Canadian Pacific

Sure. Yeah. So I think low-to-mid feels about right to me. We continue on sort of the run rate as how things have been in Q3, Q4, get some tougher comps in some areas next year. As I think about our intermodal franchise, we've had quite a bit of success in our domestic space the last couple of years. I think a fair amount of that has been rebalanced with our competition, but I think we can sustain that success in our domestic space.

It's going to be more working closely with our customers, take advantage of converting over the road. As I look at our international space, I think we've worked hard over the last year to better our product, to prepare ourselves for some of those contracts that are coming available. So we feel pretty good about again our ability to rebalance some of those contracts.

As I looked across some of our other sectors, the energy sector is really getting interesting. Certainly, the frac sand, I think, we expect to continue at a strong run rate, how it's been. We're working hard to put ourselves into other markets to diversify there a little bit. The crude space is – certainly crude by rail is coming alive a little bit. So we'll watch that. But the energy side outside of those two spaces really looks interesting, too: LPGs, chemicals, plastics, refined products, biodiesel. We've seen some pretty good tailwind in all those areas.

I continue to be optimistic on our merchandise. I think potash remains fairly robust as we look to next year. Teck, our largest customer, remains pretty optimistic on what they think 2018 looks like. So those all feel pretty good.

On maybe the other side of the ledger, our U.S. grain franchise continues to be a little bit of a headwind. I don't foresee – we're very reliant in that Northern territory on the P&W export market. And I just – it feels like to me U.S. grain exports are going to remain challenged. So that one keeps me up a little at night.

On the Canadian grain front, we're running at a pretty good clip so far this year. We set records in September and October. Given where the crop's at and the size, I think you have a pretty good run in Canadian grain into early next year. But then, you probably see that tail off midyear Q2, Q3 timing and up against some tough comps there.

And then, as I think about the auto sector, it's an area where we've been pretty choosy in how we partner and play in that market space. There's not a lot of availability for contract rollover in 2018. I think you couple that with some uncertainty in the auto space, just around production consumption, maybe NAFTA, so it looks to me to be a little bit of a headwind in that area too.

Turan Quettawala

Analyst, Scotiabank

Okay. That's a great detailed answer there. I guess maybe I'll just ask you about Teck. Maybe I'm wrong in my thinking, but do you expect a lot of growth on the Teck next year?

John Brooks

CMO, Canadian Pacific

No, I wouldn't say growth, but steady to slight uptick maybe is what we're forecasting. As I look at our major contracts with Canpotex and Teck, I spent just recently a couple of weeks in Japan, South Korea, China meeting with a number of the end users of those customers, and the fact that how happy they are with our reliability of our supply chain makes the difference.

And it's what we've really focused on with both of those players in terms of enabling growth, how do we drive down the cost for both of those, run their product to export more efficiently, and then give that certainty to that end user that their products are going to get there.

Turan Quettawala

Analyst, Scotiabank

Okay. Thank you. Anything from the audience? There's a question in the back there.

<Unverified participant>

When you talk about frac sand related traffic, what geographic areas or basins are you thinking about in terms of origins and destinations?

John Brooks

CMO, Canadian Pacific

Yeah. So currently, 2017, we've been very strong into the Permian. I would say that is – it's frankly been our primary supplier region that our minds have been attracted to. Now, as that evolves with – I think there's close to 16 brown sand projects in the works down there. As that sort of evolves, I think we expect to continue to be a player up there but we focused hard frankly into the Bakken. It's a single-line haul for us. It's direct. We have a number of crude terminals that are no longer shipping crude up in that part of the world. So, we're working with those customers to convert those into sand terminals.

I think we see quite a bit of opportunity up there. I think there's also a fair amount of potential to grow our presence up into Alberta. And so we're, again, looking at opportunities where we have existing infrastructure up there in Northern Alberta that we can reach potentially with our sand out of Wisconsin.

Turan Quettawala

Analyst, Scotiabank

I guess maybe I'll go back to the two large long-term contracts that you talked about on the commodity side. I think they're both up for renewal sort of in 2021, 2022. CP was a very different company when those were signed. Can you throw some light on what your thinking would be for those contracts?

John Brooks

CMO, Canadian Pacific

Frankly, I think it's hard to tell right now. We're halfway through those contracts. As a policy, as I said, I think we've tried to keep ourselves more nimble in terms of term and how we set up those contracts. Obviously, those are very big, important supply chain partners for us.

Our focus, I would say, in those areas are specifically with how we ensure that getting their product to export the most efficient, low cost way is our driving model. And I can tell you, the collaboration with both those partners is as good as I've seen it. So, I'm pleased directionally with where we're going. And, look, as those contracts come up, we'll get into those down the road here a little bit.

Turan Quettawala

Analyst, Scotiabank

Okay. Fair enough. On your last conference call, it was pretty clear that CP has capacity here to accommodate more volume on the network. I know capacity is kind of a little bit tricky with the railroad sector because you can do a lot to add capacity if you needed to, but as you plan for 2018 and maybe beyond and given your forecast for growth, how soon do you think you

can soak up some of that excess capacity?

John Brooks

CMO, Canadian Pacific

Yeah. So, I mean, I feel good in terms of where our network sits today on the capacity front, right. And I wouldn't characterize it as soaking it up. It's how we go out and strategically sell to maximize the value of that capacity. And I think that's different, right. That is selling in a strategic way to maximize the value to us on every single opportunity, how we fill trains out in specific lanes and corridors.

I'd say the other piece, though, and this is, I think unique to Canadian Pacific. If you look across our network starting in Vancouver, Edmonton, Calgary, really Chicago, Toronto, Montreal, we have a unique footprint in each one of those locations. And I say unique in terms of we've got excess land and capacity, particularly just in the form of land that we own and control. And in each one of these spaces, it gives us the ability to be innovative, to add customers, like a GLOVIS up in Montreal. We got 60-plus acres available right outside of our terminal in Vancouver. We all know what the land value is in Vancouver. For us to have that infrastructure and the flexibility to – if the right partner comes along, to expand that capacity is valuable.

But if you look across our network, we've got that luxury or that opportunity in a number of key locations, including Chicago. We had an intermodal, a secondary intermodal facility at a location called Schiller Park that's been mothballed and set aside for the last few years. We're looking at with really low capital expenditure, we could bring a facility like that back into production and get big – massive efficiency and capacity gains not overnight, but in a pretty short period.

Turan Quettawala

Analyst, Scotiabank

So needless to say capacity is not really...

John Brooks

CMO, Canadian Pacific

You know what and we've got locomotives, we feel pretty good on the capacity front.

Turan Quettawala

Analyst, Scotiabank

Okay. Okay. I'll move on to grain. There's been a little bit of discussion here around this with regard to share shift and so on and so forth. Can you talk a little bit about what CP is doing to its – sort of on the grain plan and how do you plan to maintain our gain share on the grain side? And I'm specifically talking about Canada here obviously.

John Brooks

CMO, Canadian Pacific

Sure. Sure. I'll first start by saying CP's grain franchise, in my belief, is the best in North America. Maybe you could argue Burlington Northern is better, but the proximity, the growing diversity we have of our commodities, how our customers can leverage our freight and transportation on both sides of the border I think is unique and second to none.

Currently, we're running close to 53% share. We set records in September. We set a record in October with our grain franchise. We feel good about where we sit today, but for us, looking forward, it's about how we drive more efficiency into that model. Think about this, we've got a strategy where you say, look, 25% of our revenues is linked to grain and if I can increase on that 25% railroads at 20% productivity share, which I think I can improve, that's big dollars. That's a lot of opportunity for us. And how we're going to do it is we're going to work with our existing and new entrants in Canada. We're

going to drive what we coined as our 8,500-foot train model, and it's really taking the old grain system of Canada of 56 cars and 112 cars and driving it up to 134 cars and look to reinvest in the new hoppers. They're shorter. Suddenly, that train is capable of handling 148 cars.

The productivity lift that we get, the share gain that we can work with our customers to earn gets pretty compelling. And really as I look in the next few years, it's not only about – look, we'll probably add 10 to 13 greenfield elevators across our network. But it's really about the development of the existing franchise, the 112s and the 56s, development of the ports that I think really bring the next step function in gain – in the grain franchise.

Turan Quettawala

Analyst, Scotiabank

What type of timeframe are we thinking about here?

John Brooks

CMO, Canadian Pacific

It's going to take some time to build it all out. It's probably anywhere from a three-to-five-year total build-out. But I can tell you, we're active in the marketplace right now, taking that next step.

Turan Quettawala

Analyst, Scotiabank

I want to talk a little bit about e-commerce as well. It's obviously been a massive growth area here and it really is changing the way which people are buying stuff. And this is a lot of people focused on the last mile, which obviously isn't really your business. But I was just hoping you could talk just more broadly about how rails fit into the changing retail landscape. Do rails win or lose in that sort of more or larger e-commerce environment?

John Brooks

CMO, Canadian Pacific

Yeah. So, it's certainly a rapidly evolving area. We've prided ourselves at CP, I think, for a long time, particularly in the domestic space, of being a leader in terms of working with the retail partners. But it is changing. I do think it presents more of an opportunity than risk as it evolves. I think what I hang my head on as I think about our franchise, at the end of the day, to go transcon across Canada, there's no faster, shorter route than Canadian Pacific. So, it lends itself well to e-commerce, courier business. It's reliable, fast, and it's the shortest.

And as you think about the next evolution of how we do business, we talk a lot about Trip Plan at CP, and Trip Plan is a system really designed, as you look at a single car or a manifest boxcar, what is it designed to run from Edmonton to Chicago, how fast, and it allows the customer to sort of plan, and we measure ourselves against that.

To me, the next evolution is overlaying that into our intermodal, particularly as you think about e-commerce. Imagine the power that a rail company could provide to a shipper if we could track and provide that transparency from the ramp, the intermodal box, starting at the origin and ending up ultimately maybe even at the consumer. So, you can measure and report out on ramp-to-ramp. I think we do that today door-to-door.

But the next evolution of it is, how can we provide that consumer the ability to maybe look into our network and see where the TV they bought or the shirt they bought moving transcon across Canada on their mobile device. You can see it starts to get powerful.

Turan Quettawala

Analyst, Scotiabank

For sure. And how much are you already up that kind of path?

John Brooks

CMO, Canadian Pacific

You know what, we're certainly up the path on Trip Plan and we are overlaying it actively today into our intermodal franchise. I would say we're just sort of on the tip of the iceberg and working with sort of our key e-commerce potential partners on what that next evolution could look like.

Turan Quettawala

Analyst, Scotiabank

Anything from the audience? Maybe one last more on the driverless truck side because that's something that's I guess fast becoming interesting as well and changing pretty quickly. How do you see that potentially impacting your business or does not really impact?

John Brooks

CMO, Canadian Pacific

Yeah. Again disruptive technologies in that are something that we are trying to stay as close as we can to that to understand. I think a lot needs to evolve, particularly in Canada in that space with driverless trucks. I would say two things come to mind. One is, we're one of the largest truckers in Canada. We provide a ton – our partners provide a huge level of dray services for our intermodal facilities and the power of potential driverless trucks on our dray services could provide huge costs savings and opportunity for us.

The flip side is, as I think about the one-man crew in railroading and compare it to a driverless truck across Canada, I think there's going to be some time before this evolves. You've got – it's not like driverless trucks maybe in the U.S. and intermodal in the U.S. where you've got shorter hauls typically. You're talking 1,000-plus mile hauls across Canada. And I think it's something we're going to watch. I think it's more of a longer term sort of evolution if in fact that comes to roost in Canada.

Turan Quettawala

Analyst, Scotiabank

Okay. Anything else? Thank you very much, John. Thanks for your time.

John Brooks

CMO, Canadian Pacific

All right. Thanks for having me.