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Transcript

Citi's 2022 Global Industrial Tech and Mobility Conference

February 22, 2022

Webcast

Corporate Participants:
Keith Creel – President & Chief Executive Officer, Canadian Pacific

Other Participants:
Chris Wetherbee – Analyst, Citi

QUESTION AND ANSWER SECTION

Chris Wetherbee

Analyst, Citi

Okay. Great. I'm going to go ahead and get started here with the second session on track. I'm Chris Wetherbee, the Transportation analyst at Citi. Very pleased to be joining in second track with Canadian Pacific from CP, have Keith Creel, President and CEO; and Chris De Bruyn, who runs the Investor Relations effort for the company. Thanks gentlemen. for joining us. I think we're going to start off. I'll take it over to you, Keith, maybe for a quick update. (Operator Instructions) So with that, again Keith, thanks so much for joining us. I'll turn it over to you.

Keith Creel

President and CEO, Canadian Pacific

Thanks, Chris. Obviously our pleasure to be here, not hard to come to South Florida in the middle of winter for a Canadian railroad. I can tell you though, I think about the last time I came here, I joined you two years ago. Think about 2020, it was sort of a fight for our lives with Covid. We go into 2021, Covid continued, never thought we'd have to battle, the fires that we battled, the floods that we battled -- and also the battle of our lives for a very transformational opportunity for this company.

So here we are in early 2022. We're in a -- starting the year at a pretty challenging - wouldn't expect any less - environment weather-wise in Canada. It has two major headwinds. Year-over-year, the weather in January, I called last January, sort of unicorn January. We had a record grain demand, and we had very mild weather in January. This year, we've got a drought. We've got very challenging weather from a compare standpoint. But we're coming out of that, the operational team over the last several weeks, you can see it in our numbers, RTMs are improving year-over-year.

So we're starting to reflect the demand that's in the network of the demand that's still pent up and built up in the network. So in spite of the grain, set that aside, obviously that's a huge headwind. As I said on the earnings call, this is going to be the tail of two halves. The first half, we have robust demand except for Canadian grain across the board. I'll say much -- a couple of comments about each one. Then the second half, what's so encouraging is that demand carries into a second half where from a compare standpoint and normalized demand and grain, hopefully coming back with a normal crop. We get to a very, very exciting opportunity for this company second half of the year.

So if you translate all that from an RTM basis, it's sort of down RTMs in the first half. It's double-digit RTM growth in the second half. It's positive RTMs for the year, and I realize we haven't given any official guidance, but we still see a path to positive RTMs. We still see a path to positive margin improvement. But again it will be down this first half, it will be up the second half. So the tail of two halves and what gives me that confidence and encouragement, let's talk about the market.

So we can talk about potash. We all understand the prices of potash record amounts were signed last week in contracts. We've renewed our contract for seven years with the Canpotex. It put us in a very good position with a great, strong relationship to continue to grow as they grow in the world marketplace. They've divested their dependence upon China. Now Brazil has taken over China, as their number one destination. So we think that bodes well for us.

When it comes to metallurgical coal, the cost of metallurgic coal still continues to go higher. Obviously Teck is a world player in that space. Now what's changed for us that actually you'll start to see a betterment when we get beyond the First Quarter is right now, we're up against a compare where last year, we originated and terminated 100% of the coal. Now with the new contract that

went into play Second Quarter of 2021, we originate 100%, but we only carried the destination about 1/3 of that. So 2/3 of that we handoff to the Canadian National at Kamloops.

So second half of the year, we get back to a compare standpoint, that's all just about growth in demand, which is very robust for Teck at this point. Good to International Intermodal. That's another area that has been extremely, extremely encouraging. Our story over the years, how we sort of rebalance the book of business. We've built a network, and we've sold our product and our service and our capacity to partner with those steamship lines that offer a strategic value for both Canadian Pacific as well as the steamship lines, some of that readjusting occurred last year as well.

So if I get into the second half, contract wins with Maersk, contract wins with OOCL, contract wins with COSCO, very compelling and material from a year-over-year basis. So that puts us in a very strong position on international intermodal. Then also the other thing that's creating a tailwind is the continued congestion on West Coast ports. You're seeing more discharge and demand coming to Canadian ports, which is going to benefit us well again second half into next year.

Domestic Intermodal, again we have the best network in Canada. We continue to convert truck to rail. We have capacity in our terminals. We've had phenomenal growth over the last several years and year-to-date, that growth continues not only high demand for the capacity and the service but also willingness to take yield and pay price for it. So that's in a very good place for us as well.

I look at the book of merchandise. When I talk about merchandise, it's energy, it's ECP, it's chemicals, petroleum, it's lumber, it's all of those things, the singles and the doubles, not the unit trains. That has all along been a strategy of ours to diversify our book and to grow in those spaces. We continued to take market share.

So whether it's forest products demand is very robust. We've got two new facilities that are coming online that have been built on Canadian Pacific, Second Quarter IPL, the polypropylene facility that's in Edmonton that we have exclusive service into that as well as an energy company, independent energy, which is refined diesel fuel coming on the Kerrobert into the Second Quarter. If you analyze those two opportunities alone, it's just short of $100 million annual of new revenue that we'll realize full year in 2023, and obviously get a bit of a benefit in 2022.

So across the book of business, a very strong underlying demand and the ability to take fair price for our capacity and our service that are tailwinds that will carry us from the second half of '22 in a very strong position into '23.

So now let me talk about '23 and beyond. Let me give you a quick update on KCS. That's been a -- there'll be books written about it one day. I hope they'll be written in a favorable way about the way we've executed this strategy to acquire the railroad. We're extremely, extremely encouraged that we're able to get the deal closed in trust in December. And at this point, the application obviously is in the STB's hands. The STB is the regulatory authority. The STB has full plenary authority.

But the positives on our side are, number one, we've got phenomenal facts, because we do represent pro-competitive. It's extremely unique because there's not a single customer that loses competitive options. In fact, there's a multitude of customers that get new competitive options and there's zero overlap. So that being said, we're going through different steps of the timeline. The path to approval, the STB laid this out in November. I think it was in Decision 11, November 23, and it outlined a maximum regulatory process that would take us into February of '23. If you use all that time, we see that process hopefully come to fruition and being able to put the companies together with assuming a positive outcome, I'd say December of this year.

I think that's a realistic expectation. But with that being said, you've seen a lot of press as of late about applications, some of the railroads when it comes to trackage rights or divestitures. They're notice to file. The actual file date is a week away. The 28th is the next milestone everyone should look for. I can tell you, as has been the case up until now and will be the case after, there's no shortage of railroads that want to delay this combination coming together. There's no shortage of railroads that have asked for concessions obviously because they're going to have to compete against this combined network. I don't expect any less.

When the 28th comes, they've got a lot of very, very expensive stables of lawyers that are writing great narratives. They're going to write this big compelling case that this concession needs to be had or this need to be delayed. But the reality is, and I point everybody to go back to the facts. I think the facts are very compelling. I've already talked about the procompetitive nature of our transaction.

But now I think about, as I have all along, what I've chosen to do is research and understand the regulatory process. I have a lot of on-the-job experience between good experiences and bad experience in this last year. Literally, if you get to the point where you take all the rhetoric out, you understand the regulations, you take a look at not what only the precedents have been in the past with the old merger rules because there's a whole lot of jurisprudence out there or cases that you can read, not only that, but what the STB continues to say.

They continue to say that competition matters. They continue to say that as late as Friday we've laid out a procedural schedule to fairly assess and robustly assess this merger. We're not going to allow it to be unnecessarily delayed. So if you're seeking a delay to seek a delay you better have good facts. Quite frankly, I don't think there have been any, and I don't think there will be any. Number two, it speaks to competition.

Then the ruling, if you've had a chance to look at it, there was a ruling that came out on Friday. Decision 13, I believe, on the docket, February 18. If you look at Page 4, not that I read them, but I do, you'll see a very telling paragraph that speaks to not only what's happened in the past, but with the regulations say then the STB essentially in layman's term, in that paragraph the way I interpret it says that we're not going to apply concessions unless you can prove there's public harm. And public harm is defined by loss of competition.

When you're -- a transaction that represents more competition, not less competition, that's a high hurdle rate. The second thing they said is we're not going to allow concessions to resolve long-standing issues. So if you get into some of these asks or some of these railroad positions, these are not new asks, these are historical ask in the past that have, in many cases, especially over the Laredo Gateway have been debated before, have been heard by the STB before and have been ruled on the facts and our transaction does not change those facts. We've made commitments that we're going to keep gateways open commercially and physically. We're not going to degradate the physical plant. We're going to invest $275 million to make it better.

We're going to create single-line, new market end-to-end cradle-to-grave service that's unparalleled in this industry. So if you think about all those things and you get to the facts and stick to the facts, which I tend to think are critically important and understand it. At the end of the day this leads us to a place that we are going to continue to work reasonably with our railroad partners and our railroad competitors, try to get to reasonable negotiable outcomes, and it's the same exact expectation with our shipper groups and with our customers because those concessions apply to all groups, any interested party, not just the railroads.

So if we navigate and carry our business that way, remain humble, remain engaged, remain reasonable, I think at the end of the day we're going to come to a good place. If not, if someone is unreasonable, we will not be held ransom. I'm not going to put us at a competitive disadvantage when we're spending the money that we're spending to create competition. So if it comes to that, the answer is going to be no, anything reasonable in between, I think we can come to a better solution ourselves. In the absence of that, if it has to go to the STB and the STB has to use their authority to impose a condition or a concession, I've got a good idea of the way to look at it.

I think that if people read what's written on paper, read the decisions, whether it's an investor or whether it's another railroader, maybe not through the filter of their lawyers. But if they look at the facts and just look at the plain English, I think it leads to a very highly, highly value-creating opportunity for this industry, for CP and KCS in a very unique way and for commerce between these three great nations. So with that, let me stop and I'll open it up for any questions.

<Q – Chris Wetherbee>: That's a great start. So let's pick up kind of where you left off and think about the regulatory process of approval. Maybe first, just a procedural question. When you think about the difference between your December target and maybe that February 2023 sort of max approval duration, what would be sort of the main variables to think about that? Are some of the things that we're hearing and potentially seeing about some, like you said, concessions or other dynamics going on from a competitive standpoint? Are those the type of things that could push this out? Or is it just simply the STB from a staffing perspective or a resource perspective that could end up pushing it out?

<A – Keith Creel>: I don't -- let's start with the first question. I won't know until all the comments are filed on the 28th. I haven't heard them all. I haven't heard all the cases. As I said, there's some lawyers I'm sure are going to write some compelling ones, and we'll sort through all that. But again sticking to the facts, I don't think that's going to delay the process. In fact, I believe the STB and the rulings, the STB's staffing up, and I think they have adequate staff, although they've had a full plate, obviously. But I think they're protecting their ability and their capacity through their rulings and do what they're doing to properly review.

What I can't control and what I don't know is when will the hearings to be held because once they start the hearings, the trigger is when they close the hearings. When they closed the record, that starts the 90-day clock. So the difference between December and February is 45 days, 45 or 60 days. I'm assuming and hoping that the facts will lead us to a place where hopefully the record is closed October, which puts us in a position to get a ruling into December, maybe it carries out into the first part. If it does, that's fine, ultimately, again the STB's in control of this process, and I'm going to respect the way they approach it. But I can tell you now, they've been approaching it in very respectful, diligent way to make sure it's fairly assessed. But also, I think if you really think about this, the STB's mandate is to strengthen the U.S. rail network. The STB's mandate is to create competition, create capacity.

If you're a transaction that actually allows that to happen through fact not through spin, to me, that's a pretty compelling set of facts to take a look at. And do you really want to unnecessarily delay those benefits from being delivered to the public, whether it's a shipper, whether it's the nations, whether it's commerce, I mean it's just -- I think although I can't guarantee, I think we're in a good place, and I think there's a glide path to those timelines. I think it will be the shorter version rather than the longer. But again if it is the longer, we've got to wait until February, and we'll wait until February.

<Q – Chris Wetherbee>: Got it. How much interaction have you had with KCS shippers? And what has been sort of the general reaction? Are there any specific areas or specific commodities that present either a very unique opportunity for you as a combined railroad? Or maybe some potential challenges because you need to make sure that you either get service in a better place or maybe provide some incremental gateways to those customers?

<A – Keith Creel>: Yes. Chris, I would say we've had quite a bit of engagement. If you know me, I'm not one that likes to let things sit too much. So obviously we have to allow KCS to run KCS and we are. We're not going to interfere, they're in trust. Pat and his team are doing a great job running the railway and getting better every day. So I'm tickled to death about that. But when it comes to preparing for the consolidated companies, we have a responsibility as well, because it's not just to talk about these synergies. You have to have capital that match it, you had to have a playbook, a business plan, systems. There's a lot of work that has to be done between saying it and realizing it.

So with that said, we've hit the ground running. We spent probably November, December over 100 customer contacts. That list of customer contacts, that's myself, that's John Brooks, that's our senior team going out and sitting with current CP customers, current KCS customers, future CPKC customers and talking about the art of the possible, what would this network look like? And what role do we think you can play? And what role do you think we can play?

So those discussions are in earnest. They're deep, getting deep. We're getting to a point now where several customers talking about pro forma company, assuming we get the deal approved, it's all contingent upon that, of course nondisclosure agreements with real business opportunities that are extremely exciting. I can tell you as much as we talked about the synergies, they don't just come, you've got to earn them, you've got to work through them, but there are real opportunities.

And the more and more we interact with customers, the more I sat down with my counterparts at large customers that have an ability to move the needle. There's a lot of pent-up opportunity. Maybe they've never had the opportunity to create the market or maybe they've been held back. But it's extremely, extremely compelling. In those cases, it's happening in grain; it's happening in the ag products; it's happening in the intermodal; it's happening on the automotive side. I'll give you a case in point. Just last week, we did our first pilot ship, an Interline move, intermodal, domestic intermodal move from Chicago Laredo. Of course we obviously it's an interline move, we connect and interchange with KCS at Kansas City.

Our transit time, even when we don't have the infrastructure is matching the competitor on a single line move. Once we invest in the infrastructure and create and we operate and execute the way we do at our company, we're going to have a very compelling product in the marketplace. So we're testing the concept, sharing those success stories. We're literally on the verge if not next week, the week after, we've got a shipper -- third-party shipper that is literally contracted their own ship, a small steamship, steamship's en route now coming to Lazaros with a discharge for Texas with discharge for Kansas, with discharge from Mexico.

So we're going to start testing the market, so to speak, from an interline basis to go and prove the concept, obviously it's got to scale up, and we've got to have an investment in the infrastructure, but just to be able to speak to and show the way this can work today. Again it's compelling. And the other thing I think about, and I just went through this, this weekend, I got super excited about it. If you go back and look at our strategy over the years, I told our investors back in 2018 as the new CEO, we're pivoting to growth. And part of that strategy was to take our surplus land assets and to create customer solutions that create stickiness that allows them to win and create markets and we win with them, right?

So that whole strategy, think about that playbook on the KCS property. We still have about 1,000 acres at CP to develop. KCS, when we just purchased in this transaction, there's over 6,200 acres, and about 2,500 of those are contiguous to very strategic locations. I'm talking about Houston. I'm talking about Dallas. I'm talking about Kansas City. There is an opportunity to create the right customer solutions and to create mousetraps that perhaps a trucker operates and provides today when you connect the dots with our shippers and what the future looks like, it's extremely, extremely exciting.

<Q – Chris Wetherbee>: So when you think about the synergies that you originally gave us when you were involved in pursuing the transaction and where you sit today it sounds like there's not a concern about the revenue synergy opportunity there maybe, in fact, sounds like it could be better over the long run?

<A – Keith Creel>: Yes. It's understated. I believe it's our responsibility to be responsible, call it a bit conservative. So are we guilty of maybe underestimating a little bit? Yes. But again that said, we have to create these markets. We have to go out and do our work. So the last thing I'm going to tell my team is take your foot off the gas. We're going to keep and maintain construct tension. We're hitting the ground running now. We're laying out the playbook. We're having the meetings that we need to have. You've got to imagine as much as we're creating this momentum, our competitors are trying to lock customers up to try to extend contracts. They're trying to protect their business.

But the reality is, and my message to the customer is, this is compelling. Don't lock yourself out of an opportunity. Some of it is going to take time anyway. Some of the stuff is already locked up in contracts. But the other part that's exciting, too, is it's the truck. There's a big chunk of this that's going to come off the truck. It's a conversion from truck to rail. It's creating a product much like we have in the Canadian space, reefers, for instance. We move reefers door-to-door in Canada. In the U.S., the reefers are controlled by the truckers. If you can create a single line move and create an ecosystem, a supply chain that's going to take perhaps it's proteins in a refrigerated container that's in Middle America to Mexico on return with produce that goes back to Middle America into Canada. That's very compelling.

And maybe when you get to Canada, you put French fries in it, that are produced in Canada and take them back into the Midwest. So there's an ecosystem. There's a supply chain that create markets here. We just got to get the right infrastructure, get the right service setup, layered on top of the investments that we're making over this 3-year period, and that's '25 and beyond, it's extremely compelling. I think it's going to be unparalleled, an opportunity. We're not going to be the biggest railroad, but I think we're going to be the most relevant, when it comes to connecting these nations with a growth platform and a growth outlook that's unparalleled by any other rail.

<Q – Chris Wetherbee>: Yes. A question that came in on the webcast that I was thinking about as well as you're going through some of these test runs from an interline basis with the KCS today how does that work in the voting trust? Do you just sort of operate it as you normally would, where there's just simply a handoff where that interchange occurs? I just want to make sure we understand how that dynamic has to play out as you go through the voting trust?

<A – Keith Creel>: So that -- it has to play out where there's two separate commercial processes, obviously. The customer gets their rate from KCS on the KCS network, they get our rate from CP on the CP network. It's a interline move. Operationally, we connect already in the same facility, right? So it's -- there's nothing new. We co-own the agency in Kansas City, where we connect where the physical interchange occurs. So we built the train in Chicago, block the train, hand it off to our partners in Kansas City, and then we expect them to take it to destination.

Obviously we're all motivated to succeed. We're in this thing, together, we want to create the service that's compelling, a compelling alternative because the competition, if you're going to take an interline move and compete with a single-line move, that's 300 miles shorter, you've got to execute. But 300 miles seems like a lot, and I've heard a lot of people talked about 300 miles of disadvantaging customers. Well I think about it as transit times. I think about 300 miles, if you've got a 40-mile an hour railroad, you're talking about 10, 11 hours of transit time.

If that could be consistent and create an ecosystem that has capacity and reliability, single-line move, I could overcome 10 hours. It happens. It's a non-event. It's not going to keep me from winning market share. That simplicity of a single-line move, the equipment turns. If you're -- again I point people back if you understand the industry, when the railroads only own 50% of the cars, the customer owns the other 50%. From a value standpoint, when you can help customers save their assets, they don't have to own as many cars.

You can create a reliable ecosystem. You can eliminate the complexities of handoffs and the delays from interchanges, all those things and hold one person accountable cradle to grave from a service experience that's unparalleled. From a cost ability experience that's unparalleled. That's the reason this is so compelling, being able to create something that's never been created before. With these two networks can never be replicated. Never as a long time. I just don't -- I can't imagine in my life and your life in three of our lives, that you're ever going to be able to build a railroad connecting all these three countries again. I think it's one and done.

<Q – Chris Wetherbee>: Yes. It certainly is a unique opportunity. Let's talk a little big picture then I want to come back ultimately to this year and sort of the 2022 outlook. But when we're thinking bigger picture about the combined company out beyond STB approval, you've talked a lot about the opportunities on the revenue side. There are some cost opportunities as well. But we've talked a lot about the incremental margin sort of opportunities of this. If you run it over time, it does put you guys in a sort of industry-leading position from an operating ratio standpoint. So just conceptually, is that something that the industry can achieve where you get both very good top line growth and also an operating ratio that could look like a 50 or something in that ballpark?

<A – Keith Creel>: Chris, I'm not going to speak about the industry. I'm going to talk about us. To me, the operating ratio has always been an outcome of running the railway the right way. It's controlling their costs, it's investing in infrastructure. This isn't cut your way to success. Again we've never spent as much capital in CP's history as we have since the way implemented PSR. We never bought more ties, rails and ballast than we have since. You've got to have a reliable, safe railroad to create the reliability, the safety and the capacity to be able to convert this growth. That's what led us to industry-leading growth. It's a combination of the two.

So if you can be the railroad and we can, that can maintain the discipline on the cost control side, it can run a disciplined scheduled railroad that gives you truck-like service to convert the growth because you've got to earn the customers' trust. Then at the end of the day the margins, the outcome of all that work is they're going to be favorable. They're going to be industry best. The path to getting there is obvious, but I'm not enamored with having the lowest operating ratio. I'm enamored with earnings growth. I just think that by running the railway the way we run it, the natural output is it's going to be a very favorable low margin that drives earnings growth. But again earnings growth is the golden star to be. It's not OR.

<Q – Chris Wetherbee>: Got it. Makes sense. So let's talk about 2022 a little bit more now. Obviously as you highlighted at the top, there are some challenges that we're seeing. Weather is difficult and volumes look certainly more back half weighted than they do first half weighted. So

maybe honing in on CP or sort of above the line as I would think about from operating ratio up, which is kind of going to be the core CP this year. We talked about RTMs sort of ramping as we get, go further into the year. Can you get -- is it really 3Q when you think our RTMs kind of turned positive. It's going to be difficult because of grain to do it before that. Is that fair?

<A – Keith Creel>: Yes. It is. I think 3Q, what we expect is some of the choppiness from the chip manufacturers. We think that's going to be resolved. We're in a very good position with high-demand vehicles. So from a compare standpoint, that's going to be wind at our back. We're going to have strong -- continued strong domestic intermodal growth, continued all-in international growth with the contract wins that I've talked about. Then the other thing that's ramping up is crude. We don't talk a lot about crude because crude from a carload standpoint, is down from an RTM standpoint, it's going to be favorable because the length of haul, it extended with the DRU.

The DRU came online end of last year. We're going to be at nameplate run rate this month. So the product was classified, I think it was in December, is a nonhazardous DRU, it's a pure bitumen. It's moving in the car, all the diluent is going to remove with the DR unit, that's in Hardisty. So full all out, you're talking about 25, 30 trains a month. But from a linehaul standpoint, they're not going to one Emerson, they're going other way Kansas City, where we're interchanging the KCS. So second half of the year, you're going to have a full run rate on that, which is going to be very encouraging for us.

Then continued demand on forest products. The potash piece. Last year, we had some choppiness in the potash numbers. Second half should be huge demand, railroad operating well. I think we're going to be in a really good place. But yes, Third Quarter, you'll see it Fourth Quarter, those two should be very, very big quarters.

The other thing I'll draw into is a compare standpoint. Last year in the third and Fourth Quarter, we had the fires, the railroad was shut down for two weeks. That was in July. Then, of course we had the floods for the railroad we shut down. We were shut down for eight days. Our competitor was shut down for an additional two weeks and I'll remind everyone in both of those corridors, that's directional running. So when CP's shut down, CN's shutdown, nobody is moving. When CP's open but CN's shutdown, 100% of their traffic is on our railroad going both ways. So it's not the same throughput, it's a strain and it restrains capacity. So knock on wood, mother nature is good to us, and we don't have 100-year fires this year and 100-year floods. We're setting ourselves up for a very strong back half.

<Q – Chris Wetherbee>: Got it. You said you can get improvement on the operating ratio for CP over the course of the year. How do we think roughly speaking about -- obviously the comps do help in the back half of the year. There's no doubt about that. Although some of that cost, particularly in the Fourth Quarter, was largely capitalized, I think around the floods. But how do we think about OR?

<A – Keith Creel>: So Nadeem told me I could not give you guidance, but I'll tell you it's -- it will be -- we will have margin improvement. It won't be 100 basis points, but it would be an improvement.

<Q – Chris Wetherbee>: Okay. That's more back half weighted is -- reasonable weighted –

<A – Keith Creel>: Yes. Absolutely, right.

<Q – Chris Wetherbee>: Okay. Got it. That's very helpful. Then when you think about KCS, and I know you can't give guidance for KCS. But when you think about the contribution for KCS to the business this year, I think there are some things to think about. There is a step-up in depreciation

that has to be captured within that below-the-line income. Anything else that we should be thinking about? They seem to be operating well. Fourth quarter results were actually good.

<A – Keith Creel>: Yes. Correct me if I'm wrong, Chris, but I think on the step-up on the depreciation, it's going to be $125 million offset from the earnings that they –

<Q – Chris Wetherbee>: Yes. That's noncash?

<A – Keith Creel>: Correct.

<Q – Chris Wetherbee>: Okay. Got it. That's helpful. Then I guess when you think about the competitive landscape in Canada, there's been some changes at the competitor there. You guys obviously have had -- they've had similar challenges from a weather perspective as you have. Anything materially changing there you think as you look out over the course of this year. You guys obviously always compete with them quite fiercely in Canada. That's always the way it's been. So how do you think about it going forward?

<A – Keith Creel>: I think more about optimism, Chris, in all honesty. I've always said this. Both railroads, when they run well, create a great service with a great opportunity for growth, and I think that's a better place for us both to be as much as CP can run well, but we're connected in some locations, like talking about going to the West Coast, that's vital part of our network, on to Vancouver, we don't go to Prince Rupert. We go to Vancouver. So we need those corridors to work.

So I'm encouraged with the change. I'm hoping that, obviously they make commitments. They're focused on yield. They're focused on running the railway better operationally. Both those environments, I think that's favorable for the industry. It's favorable for the customers and it's favorable for CP. So again I'm very optimistic, and I'm hopeful that the meet and exceed every one of those goals because if they do, I think we both do well.

<Q – Chris Wetherbee>: Got it. Where are we with price? That's obviously been something that we've seen some meaningful improvements with pricing on the back of obviously a very tight transportation market in North America in general. So when you think about the 2022 outlook around price, where are the best opportunities for you?

<A – Keith Creel>: Across the book, it's been strong. Probably the most robust pricing environment I've ever been in. But again a Canadian company, we're conservative by nature. We've always said the 2% to 3% on the down cycle, the 3% to 4% in the up cycle. We're exceeding that, obviously. But our book of business, I think we're going to turn over 40% this year in 2022. So rough numbers, to me, somewhere between 4% and 5%, I think is a good number. We'll see how things come out. The one piece I don't know yet about is what's going to happen with our regulated grain that VRCPI number is going to come out, telling us what we can charge on the rate, that will be the Fourth Quarter when the harvest comes back in.

We'll know that in April, I think. We're assuming 3% there. So if it's more than that, there's some upside. So again we're in a good place. And as long as we provide great service, we have capacity, which we do. We've got a very compelling value proposition for our customer compared to the truck and even compared to our competitor. So again we'll continue to play to our strengths and do what we do well, executing a railroad, keep constructive tension on pricing, on service, on cost, and I think everybody is going to be happy.

<Q – Chris Wetherbee>: Got it. Then I guess we talked a lot about inflation in the markets over the course of the last couple of months, couple of quarters here. How are you guys planning for that sort of what's embedded in the outlook for 2022 in terms of cost inflation?

<A – Keith Creel>: Yes. We're obviously that's -- the inflation discussion is what's driving a very solid case to have discussions with the customers on price. We're not just charging on that price because we have to cover our costs, too. Fortunately, from a labor standpoint, overall, our contracts are tied to -- they were very progressive contracts, and this isn't all, but this is probably 80-90%. There was a base wage increase, which was 2%, and then the kickers that were there that could earn up to 3% were tied to RTM growth. Well in a world where last year, we contracted a little bit, we haven't triggered that yet. I'd love to get there, and we will. But at this point, in these recessionary times, fortunately, we're not facing huge wage inflation. We're still able to hire employees, I heard Alan and some of the challenges they're having in the U.S., and Canada it's not as challenging. But at the same time, if I get to the U.S. markets, I think we have a different value proposition. Our collective agreements are different than the other roads. CN has a like collective agreement where they pay by the hour. The other roads, all the other Class Is, itself for CN, they're traditional. There's a yard rate. There's a road. Road takes seniority. It takes a while to build your wages up at our railroad you hire at the full rate.

When you hire out on an hourly deal, depending on what part of the property you're on, but the ranges are around $40, $40-something for a conductor an hour and 50, $50-something for an engineer. When you're offering those kind of wages, it's pretty compelling from a competitive standpoint, competing for talent. Then the other thing that's really helping us, I think attract more employees and hire employees is just our future. There are a lot of people that are extremely excited about CPKC's future, both in the U.S. as well as in Canada, that quite frankly, pride in these two companies. Canadian Pacific, uniquely in Canada. We're the railroad that connected the country literally connect to British Columbia with the Federation as Canada is known today.

So the people that work at CP take great pride in that. That's a 140-year-old history, where we're partnering with the other small Class I that has -- they're six years younger than us. So they're 134 years old. There were 1887, we're 1881. So like pride, like commitment, you've got the two smallest we're humble, we're hungry. We want to work hard and create success, and we're getting a level playing field once we get to the process assuming that the STB approves this as we expect the facts support with a lot bigger playing field to execute and deliver on. So all those things said, success breeds success and people want to be a part of that, and it's something that's helping us attract future employees.

<Q – Chris Wetherbee>: Then maybe the last question is on supply chain and understanding sort of how you fit into that. As you noted, West Coast ports in the U.S. certainly have been more congested than we've seen in Vancouver and in Canada. So I want to get a sense of is this an opportunity for you? And I guess have you seen any improvement in what you can look at?

<A – Keith Creel>: It's an undeniable opportunity. If you think about the potential of this new network, if you think about the connectivity that gives us down the line when you're having discussions with shippers that quite frankly are they're pulling their hair out, like everybody else is trying to get containers discharged in LA Long Beach or on the U.S. West Coast. Some of that congestion has occurred in Canada as well, not anywhere remotely close, but because of the weather. There have been a few hiccups in Canada. They're getting themselves worked out. But long term, you think about the growth, you think about nearshoring, you think about the products, you still have to come into North America to be consumed. There's plenty of business to go around.

So when you have an opportunity, because of those real pains, people's eyes open, and you can explain to him just take a look at Lazaros. Lazaros to Houston, to Texas markets, it's -- I don't know, 300-some-odd miles shorter by rail than coming from LA Long Beach. Now then you think about, well, what's the total transit time. Well they'll sell you [ph] if you're going to LA Long Beach from Shanghai, it's -- what is it, a 13-day or 14-day transit time versus right now, Lazaro they would advertise 17, but the reality is that ships stopping along the way. If you create destination density and you have a steam ship coming from Shanghai, going to LA Long Beach and one racing to Lazaros. Lazaros will get there three days later because it's an additional 1,400 nautical miles.

But once you get the land, the on dock dwell time with the capacity that's available at Lazaros is, two days on customs, two days on getting loading on a train. You're at the border in another two days. You're in Dallas markets, Houston markets, from landing to destination in five days, you've got a shorter transit time, and you can convert that opportunity going into the Midwest as well. If you take it all and you combine it all, piece by piece. I'm going to speak to this next week when I'm at the TPM conference in LA Long Beach. You've got an opportunity, a lot of these lanes to cut for a ship to cut transit time in half. So a 20-day opportunity versus a 40-day in a world where there's not enough capacity going around and a lot of ships are in line in queue for 20 days trying to get offloaded in LA Long Beach.

If I can pull one of those ships and create a rotation at Lazaros to create additional capacity with the assets that I have. It's a very compelling value proposition to sell. So there's never been a better time to have those discussions, not only for relieving congestion today but most importantly, creating a marketplace that will be there, not go away when all the congestion goes away but we'll uniquely complement and provide opportunity for LA Long Beach to still thrive and grow Lazaros to grow much like in Canada with the Canadian experience we've had with Rupert and Vancouver. There's a place for both to do well. In all honesty, with the demand that consumers are requiring, we need both.

<Q – Chris Wetherbee>: Yes. I'd imagine your customers would probably like to have that full service today.

<A – Keith Creel>: In diversity, option -- optionality.

<Q – Chris Wetherbee>: Absolutely. That sounds great. Well listen. We're at the end of our time. Keith, thanks so much. Really appreciate the time.

<A – Keith Creel>: Thank you.

<Q – Chris Wetherbee>: Thank you.