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# Transcript

*Credit Suisse Industrials Conference*

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**Palm Beach, Florida**

## **Corporate Participants:**

Keith Creel, President & CEO Canadian Pacific

## **Other Participants:**

Allison Landry, Analyst Credit Suisse

## QUESTION AND ANSWER SECTION

### Allison Landry

*Analyst, Credit Suisse*

...Keith Creel, who's Chief Executive Officer. He doesn't have any prepared remarks, so we're just going to jump right into Q&A.

So, thank you. Thank you for coming. Really appreciate you participating. I guess, before I grill you maybe on – with these long list of questions, I guess, maybe could you tell us what in your view – your perspective, what the CP story is and how that may differ from at least what the investment community perception was back in 2014, for example?

### Keith Creel

*President & CEO, Canadian Pacific*

Okay. Current state, I came to CP, it's been four years now, 2013, so going on five years, coming up February. I came here, joined Hunter, obviously, with a mandate to restore the company financially. The company was in trouble financially. Company had a very capable competitor that, quite frankly, was beating in the marketplace in most all accounts. Obviously, Hunter and I had a lot to do with that transformational change. The operating model that we implemented precision scheduled railroading at the competitor, which made it a very formidable competitor, remains a very strong railway, was the mandate that we had to apply to CP.

So we came to CP and what we had thought to be some challenges became opportunities. Some of the things that I underestimated coming to CP was the willingness to change by the people, but actually we run the company day-in and day-out and as well as network strength as opposed to weaknesses. I've heard all about the challenges of operating through the mountains, which, yes, is challenging, and I never heard that it was 200 miles shorter in the key lanes that we operate in, be it coming from Toronto going to Calgary, or be it from Vancouver going to Chicago.

So those two variables were meaningful to me as an operating officer. So I come to the company. We had to take a look at business. We chased revenue. Our predecessors had chased revenue with an ability to bring it to the bottom line for a long time and we sort of right-sized the railroad. We – as Hunter used to call it a dog with fleas, some of the business we weren't making money on. We were hauling for practice. We sort of de-marketed ourselves from that. And at the same time, our competitor, who had a cost advantage, who had a service advantage, picked up some of that business. So what we walked away from some of the downturn that we had in our business demand, most specific in automotive and intermodal, drove growth for our competitor. It's not a secret; it's a fact.

But during that time, we've right-sized the railroad. We've got a very strong operating team. We've got a marketing team. We've got our cost basis so that we're not at a material disadvantage we're at; if not, very close to our competitors' strategic cost makeup, so we can compete for business now. The place we're at today, which is a very unique place in this industry, and it's not a surprise. We said this was going to happen all along. We have capacity because of the operating model, because of the investments we've made in sidings and in people and in process. We have locomotives; we have land. We're in a very unique position in a macro environment where demand is increasing, which is being multiplied by, not only with the competitors, the road on the truck side because of the shrinking capacity, the pressure on truck drivers' cost, the electronic devices. There's macroeconomics favoring demand on the truck side, and from our rail competitor, they're facing some of the same capacity challenges, because of similar growth. They have pinch points.

So what we said four years ago, we're going to repatriate the business that makes sense for this railway. So this railway, historically, was a bulk railroad. Probably 25% of the business is what we would call the business merchandise, so manifest trains. The balance was bulk, the balance was intermodal. We were very suspect to commodity prices. We're suspect to how much grain has grown. We're suspect to how big the harvest is. You're suspect to the cost of coal in the world market. You're suspect and exposed to the cost and demand for potash. So, those areas, while strengths of the franchise, could also become

weaknesses in a down market.

So we decided we're going to look at the merchandise side and we're going to sort of de-lever our risk by growing that portion of the business. To do that, you got to have service and you got to have capacity. Now we've created a reputation for having service. We have capacity. The demand is there both on merchandise, strong steady demand on bulk, and really nice demand on the domestic product on intermodal, and the next phase is going to be international intermodal. So going back again to that theory of repatriating business that makes sense for this railway based on where we have capacity, based on our service offering, based on the things that we've done since to improve our service.

Our reach to the Ohio Valley, which we've just announced back in October, in partnership with Genesee & Wyoming. If you're an international steamship company and you have product going to that market, head-haul auto parts and you have an ability to put ag product to improve your dynamics to reduce your costs, to create a backhaul move, that's a pretty compelling marketplace. Detroit, we've reopened our facility in Detroit. We de-marketed that business. We had a very service-challenged offering. We weren't making a lot of money on it. We backed away from it to focus on the core network. We fixed the core network. Now we've got an ability through our partnership with another railway to handle the business on our behalf to our facility in Detroit.

So, now, we're repatriating all of the business in that market, and we've got a service offering and transit time that's reliable, and it's fast and it can't be touched. The western carriers can't touch it, Canadian counterpart can't touch it. So, again, those things are making our service offering as we go into this next round of opportunity to repatriate is these contracts come up in 2018 puts us in a very unique position, a very positive position to realize some market wins which are going to emulate some of the wins we've been getting on the merchandise side in 2017. So it's a very good position to be in right now.

## **Allison Landry**

*Analyst, Credit Suisse*

Great. And the contracts that are coming up in 2018. Are those international intermodal specifically, or does that also include some merchandise?

## **Keith Creel**

*President & CEO, Canadian Pacific*

There's some merchandise, some large chemical customers. There's some business that we're actively competing for now, and then the big piece is, obviously, on the international intermodal side. ONE, which is the consortium – consolidation of the three Japanese carriers, the NYK, K Line, and MOL, goes into play April 1 operating as ONE. We only have about a third of that business now with K Line. We don't move MOL. We don't move NYK. So, obviously, when that business gets awarded, I personally believe based on value of our service offering and the capacity and the reliability we have in the network, we're going to see a shift. But how much it is, I don't know, obviously. Our competitors are going to compete, but our product is in a good place.

## **Allison Landry**

*Analyst, Credit Suisse*

Okay. Is there any way to without – of course, you just said you don't know how to size what you would be awarded, but what's the total size of that business?

## **Keith Creel**

*President & CEO, Canadian Pacific*

If you were to win 100% of the business, it's about CAD 160 million. But we've already got about CAD 60 million. So the net is about CAD 100 million. But again, something I'm proponent of. I think balance matters. And I think, and I've said this all along, there's enough business in Canada. We've got two very capable railroads. We should win in the marketplaces where our network has strengths, because it's all about service and turning assets, and controlling costs, the same operating model. So the lanes that we're shortest in and we have reliable service in, we should win in. We should play to our network strengths, and if the

other railroad plays at their network strengths, then there's balance and there's enough opportunity for both railroads to do well.

So I take that theory, and I think about if I'm a customer, giving away 100% of the business, do I want to put all of my eggs in one basket? No. If they do, will I handle the business. If I look at it, it fits our network and we commit to it, we will. I'm not going to promise the moon and the stars and disappoint them. But I would be surprised and I think the service piece is what keeps that level. As we go forward, to me, if I'm a supplier I want two healthy suppliers. I would think for shippers, they want two very capable shippers and if they get problematic service to put all their eggs in one basket, I don't know if that's always the best answer.

So, again, what fits us well, we're going to handle well. We'll commit to it. I think we're in a good place to win business.

I just don't want to – that balance, you have to be thoughtful about that, you got to be very respectful, because if you lose the service piece, not only do you lose credibility and lose your stickiness to the customer, you jeopardize the operating model, because the operating model, again, to control the cost, which is what creates the service, you have to turn assets. Once you slow those assets down and you start sticking your locomotives and the locomotive dwell goes out, the terminals get congested, you're affecting not only the revenue side, you're affecting the cost side. And it's a recipe for not sustaining long-term success.

## **Allison Landry**

*Analyst, Credit Suisse*

Right. Do you think that that's what's happening at your competitor with the service issues in the last several months?

## **Keith Creel**

*President & CEO, Canadian Pacific*

You know what, I'm not – I'm on the outside looking in. I see they've got pinch points. I see the same metrics everybody else sees. They're best to answer that. I know this. If I think about international intermodal, if you increase capacity 50% on the West Coast and you don't match that in inland capacity, that traffic has got to go somewhere. It's about a fluid supply chain. So you can take it off the ship put it on the railcar, but you got to get to destination, that railcar has got to turn back. If you can't do that, you've got some challenges.

But again, that's a very capable railroad. They've got a great franchise. I'm not going to talk bad about them, because I worked with a lot of them, and they certainly understand how to run the business. Are they having some growing pains? Yes. But again, I think it just – that theory of repatriating business, I think it just accelerates it. We're going to make conscious, thoughtful, responsible decisions to sustain growth, and provide and maintain service on this railroad. We're not going to just go chase business because we can chase business.

I'm not going to jeopardize my existing customers and ruin my reputation, which ultimately will hurt my long-term value. I'm just not going to do that. Not when I'm running this company. It's not going to happen.

## **Allison Landry**

*Analyst, Credit Suisse*

That makes perfect sense. I think back in 2014, you sized the merchandise repatriation opportunity at maybe CAD 200 million to CAD 300 million. Is that still the right way to think about it? And have you been – obviously, two years of a freight recession, so that obviously makes it difficult. But have you made a dent in any of that?

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yeah, absolutely. We probably gained, I'd say, about half of that. And then maybe upside of that. I mean, as demand

increases, obviously, at least over the short term, this crude by rail piece, I described this in the meeting I just had with investors, we were married to the ramp up. This company was connected to it. Our value was driven by it. We thought, like everybody else, that it was real and it was staying. We went through a very painful divorce. We took some hits in the marketplace rightfully so. We made a decision after that. We're not going to chase the peaks.

Long term, I don't think the dynamic for the demand that's in crude by rail is going to exist when you get to pipelines. The economics favor the pipeline. Is there going to be a niche market, is there going to be a certain percentage of the business, 2% or 3% of the revenue, that's always going to be there? Yes. But the demand is there now. Long term, I just don't think it all stays there. So we're being very strategic over the next two to three years, and I don't know if it's a two-year deal before the pipelines or a three-year. I think it's somewhere in between. It could be longer. But again, I don't think it's long term.

We're talking about 30-year asset decisions. I'm not going to be making 30-year decision based on two or three years of demand. But in the interim period, I think there's an opportunity, especially if we manage this properly, to win business, to win business based on the value of the service offering, to do it in a controlled manner, so that we bring it to the bottom line. We maintain our cost advantage. We have superior service. That's the recipe for success for this company.

## **Allison Landry**

*Analyst, Credit Suisse*

So if you were to take on some of the heavy Canadian crude business, what would you – or how would you structure contracts differently if it was under contract as far as a spot move, knowing what you know now after what we saw in the end of 2014 and 2015, what do you guys do differently now to protect yourself?

## **Keith Creel**

*President & CEO, Canadian Pacific*

They're going to be short-term contracts, not long in duration. There's going to be minimum volume commitments.

It's going to have to be accretive and make sense. For us, where we're at, we've got capacity on the rail; we've got capacity with locomotives. It's about hiring people. Hiring and training people. Number one, I want to do right by people. I don't want to ramp up a lot of people, and then lay them off. That's not fair to folks and their families. And number two, it's a significant investment to hire, train, and retain and employ. So that's what we need. I can make a two-year decision when it comes to people, and I can attrit out and manage it through attrition to a point.

I've got to be careful in how we do it. But certainly there's some room to play with it. But again, if I've got a minimum volume commitment, I know what to plan to at a minimum. And as we go look forward now, it's not talking about just minimums. We'll do minimums and maximums, if we're going to do contracts.

Or we stay in a tariff world. So, we'll probably do a little bit of both. We're going to have some tariff business with spot moves, contracts we get into. If we extend contracts, they're going to be short in duration. There's going to be a floor and there's going to be a ceiling. And to me, that's the only way you can manage the demand, which is pretty robust right now.

## **Allison Landry**

*Analyst, Credit Suisse*

Sure. So, in other words, pricing is one lever for spot opportunities, and then sort of the collar on volumes, if you do... a short-term contract.

## **Keith Creel**

*President & CEO, Canadian Pacific*

That's correct. That's exactly correct. You just don't want to get to a place where to protect all the other business you put in

these corridors, that I'm going to congest a railroad, I'm going to spend millions of dollars to add sidings that, if that, goes away in two years. I'm just eating the depreciated cost, I don't really need them. So there's a fine balance that we're trying to maintain.

## **Allison Landry**

*Analyst, Credit Suisse*

Sure. Okay. So going back to the 2014 Analyst Day and speaking about those three pillars of revenue growth, one which was largely driven by crude by rail, and there was a merchandise piece, and intermodal. So if we just sort of think about two of those drivers going forward, how do you think about the top line growth potential at CP over the next few years, assuming the economy cooperates?

## **Keith Creel**

*President & CEO, Canadian Pacific*

I see it – from an RTM standpoint, from a volume standpoint, depends on how the contracts fall, but mid-single-digit growth is possible. I would say low double-digit EPS growth is possible. So barring some kind of economic catastrophe based on the value of our network, doing it in a controlled fashion, I think that's – it's not easy, but I think that's certainly within the realm of possibility.

## **Allison Landry**

*Analyst, Credit Suisse*

And maybe I'll just go to the audience. Are there any questions out there? In the back.

## **Unverified participant**

[indiscernible]

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yeah. So I'm looking at raw numbers more so than percentages. I look at by basic capital, and the basic for the railroad, ties, tracks, ballast, the basic for our IT systems to keep the lights on kind of expense. It's probably around CAD 1 billion, CAD 1.1 billion. So anything else is incremental. It's productivity capital. It's growth capital. So what we're doing this year, we're going to see us come in just a little – around CAD 1.3 billion number, a little bit less than CAD 1.3 billion. What I see going forward, we've got this thing going on in Canada Bill C-49 that's, we hope, is about to come to fruition and become law.

Within those provisions, there is an MRE bifurcation index, a cost index, which, if it's written the way we think it's going to be written, the way the government has led us to believe in initial meetings it's going to be written, it's going to create an environment where we can spend, ramp-up on capital, and invest in hopper cars.

Our profile and our fleet of grain cars in Canada, which they're 40-year-old cars, we've got a disproportionate number of our fleet, they're old Canadian-owned grain hoppers, they're 263's, so they're lightweight, they're high cost, they're not reliable. They're old. Customers don't like them. The gates don't work that great. You don't have a lot of product. So we've got an opportunity with this change with the law and this is in our capital plans.

Assuming it comes out the way we think it's going to be, we're going to ramp up to about CAD 1.5 billion probably. We're talking about a CAD 500 million spend, about 5,000 railcars over the next three years, and we're staged ready to do that.

And what that does for us, not only is it a contribution to margin opportunity, a productivity opportunity. If I look at the profile of the fleet, once we get that fully converted, because I run trains hauling more grain, they're shorter cars, they're lower cost,

they're more reliable, there's about 30% productivity improvement in that investment alone. So the customer gets a better service. The country gets more reliable movement to the port. And then on the revenue side, the grain we compete for out of the U.S., our main competitor is the BNSF Railway. They've got a great fleet of cars now; in fact, similar cars. Our grain gets discounted, because our cars are in such poor shape coming from the same competitive draw area. We have to make up the difference in that in discount. So that revenue, quality of the revenue, once we get this new fleet, not only does it help us on the margin side, on the productivity side. It also helps us on the revenue side. So we'll ramp up to do that. It makes great sense to invest internally for the growth.

And then once we get that done, as you said, PTC is going to fall off. So I think you'll see the high watermark around CAD 1.5 billion, maybe CAD 1.55 billion in 2018 and to tail off a little in 2019, a little bit in 2020, and then we'll probably be back down to about a CAD 1.3 billion. And percentage-wise, maybe that's 16%, 17% based on what the revenue is going to be in 2020. So that's sort of the range we're talking about. We're not talking about a lot of swing, but it makes good sense, it's strategic for us. It's going to help drive growth. It's a good call on cash, and that's the way we're going to do it.

## Unverified participant

[indiscernible]

### Keith Creel

*President & CEO, Canadian Pacific*

Yeah. No, PTC is probably going to go a little bit into 2020. The heavy years, though – we're in the heavy years. So we were talking about CAD 45 million, CAD 50 million a year right now. That's what starts to tail out.

But as far as it being completed, I think we're probably sometime in 2021. I don't know the exact number. It depends on how things progress. But as far as the big spend, the big spend years are going to be 2018, 2019, and then it sort of tails off in 2020, and very little in 2021.

### Allison Landry

*Analyst, Credit Suisse*

How are you thinking about the maintenance expense on PTC going forward? And I think your competitor has put some numbers out there, but I'm not sure that they were net of any productivity benefits that are derived from PTC. How do you think about that?

### Keith Creel

*President & CEO, Canadian Pacific*

You just got the equation. I think it's a wash. There's going to be a little bit more maintenance expense, but the productivity I get from it, it's never going to pay for, but as far the ongoing maintenance expense, I think they eliminate each other. It's not material.

### Allison Landry

*Analyst, Credit Suisse*

Okay. Okay. That makes sense. Maybe high level, how do you – is there anything that you're doing differently than Hunter did or would do, whether it's top line related? Is there anything that you would say that you think you're sort of – have a little bit of a different vision?

### Keith Creel

*President & CEO, Canadian Pacific*

Yeah. No, the vision is very similar. I mean, he was my mentor. He taught me how to make money in this business and how to

run a successful business. I'm not going to change that. It's a formula that works. Precision scheduled railroading it's what got us here and it's what's going to keep us here.

If he were here today, the only thing probably that I'd do differently that he wouldn't be doing differently, I'd go to Ottawa, I get involved in that process, I go to D.C. You could argue the value and all that, I think it's important. I'm spending quite a bit of time with customers. We're talking about big accounts. We're talking about credibility is on the line. We're talking about if they're going to make modal shift in share and they're going to jeopardize their reputation based on service, I think I can add a whole lot of value explaining not only how it works and what our value proposition is, but also commitment. I'm an operating CEO. That's never going to change.

So there's not a lot – my style is different than Hunter, but philosophically, not a lot of changes. It's just where we are in the chapters of the story. Just like when Hunter left CN, we fixed the engine, we got it running extremely well, then went into growth mode. It's sort of the same thing here.

I'm just going to be very careful in how we do it to make sure that we sustain it. So there's not a lot of difference. Just style, I'd say maybe I've got a little bit more patience than Hunter might.

## **Allison Landry**

*Analyst, Credit Suisse*

Okay. Makes sense. So going back to my original question, what is the CP story? It sounds like it's still, okay, there's some incremental margin improvement. But obviously, the heavy lifting has been done and we're sort of on or at the precipice of where the top line growth should really start to kick in. Is that how you would describe it?

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yeah. Exactly it is. It's maintaining our focus on service, our cost advantage. It's all about the operating model, making sure we don't lose sight of that because if you do, you're going to lose it all, and it's bringing on growth that makes sense for the company.

And there's growth out there. There's opportunity out there. So as long as the economy grows, we're going to win in the marketplace. We should be doing a little bit better in the economy. The quality of the service, the capacity has given us pricing strength. We haven't had in the past from a macro level and a micro level. So, I mean, overall, we're in a pretty good place, pretty good place.

## **Allison Landry**

*Analyst, Credit Suisse*

In terms of pricing, given the changes in the cost structure and your service products, do you think with the broader acceleration in rail pricing, plus tight truck capacity, could CP see stronger pricing than it has historically?

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yes, CP will. I mean, the Canadian roads – and we've got to keep this in perspective – the regulatory environment with FOAs, historically what the Canadian roads have done, you've never seen us take in 6%, 7% price.

It just isn't going to happen. You can't sustain it. You jeopardize too much trying to do it. But that 2% to 4% has always been a pretty good barometer over the long term. So in a weak market, where the shippers have had opportunity and excess capacity, then it's closer to 2%. In an environment which we transitioned to and we're still transitioning in, it's more on the higher side, the 3% to 4%, so we did 2.5%. Third quarter, we'll come in at 3%. This quarter at 2018, it's going to be 3% plus.

And the key to that, and this is an important point, you can't enjoy the opportunity to realize the value in your service if you lock yourself in a long term contract and you lock yourself out of the economic environment. It's not good for the customers. It's not good for the railroad. So that discipline about long-term contracts, there is going to be exceptions to the rule, but we didn't lock ourselves up in the downturn. We knew this was going to bounce back. We knew the economic cycle was going to come back. And when it does, if you've got great service low cost, you're in a pretty good position to benefit from it. But if you've locked yourself in to five, six-year deals at some index that's much less than the cost of inflation, not only you miss the quality of the revenue on the cost side, you're going to get hit both sides.

So that pricing that's something Hunter taught me a long time ago, that's fundamental. That's one of the foundational rocks of this precision scheduled operating model. It's something that we benefited from that discipline. We got hit pretty hard and we got criticized. Our multiple took a little bit of a hit during sort of the rightsizing of the railroad and some of the revenue that left for the right reasons. And rest assured when it comes back, it's going to come back for the right seasons and it's going to go to the bottom line, which to me long term value, that's the right way to run the business.

## **Allison Landry**

*Analyst, Credit Suisse*

Right. If you think about your comments about not wanting to be in sort of multiyear contracts, can you – is there a way to frame what percentage of the business was under multiyear contracts maybe when you joined and what it is today and what's the annual?

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yeah. It's chunks. I mean, the big contracts, there are some long-term deals, big, big customers. Teck's a long-term deal. It's a 10-year deal that we're about half way through. Canpotex is a long-term deal. It's a 10-year deal that we're half way through. There are one or two more, I'm trying to think about, Mosaic. Mosaic's longer than the average. It would be like a five-year deal. But that's probably, I'd say, 25% to 30% of the business is long term like that because they're big chunks.

The balance, I would say, 25%, 30% would be two- to three-year deals and then there's a percentage that's one year. A lot of the things we've done in the last two years have been one-year deals.

Two years. I just wouldn't sign anything longer than two years for all the reasons I've explained. So it's coming up for renewal, but there's no big chunky contracts coming up renewal. So there's no big, big-ticket items that are out there. It's more – the domestic intermodal is an opportunity for us, the international, the big contracts which we're covered in 2018, we have no exposure in 2018. It's all upside for us. There's not downside. So we're just in a good place overall to win in the marketplace.

## **Allison Landry**

*Analyst, Credit Suisse*

All right. Are there any questions? I wanted to ask about the partnership with Genesee & Wyoming in Ohio. It's I think a unique and obviously mutually beneficial agreement, especially with the backhaul opportunity. Is there anything else we should be thinking of that is a potential opportunity in a similar vein that you see out there, whether it's with Genesee or another short line? It seems like CP and Genesee have sort of created this synergistic relationship, starting with the sale of the Western DM&E. I'm just curious, it seems like in that sort of Ohio region, there's a lot of interchange points that might make sense.

## **Keith Creel**

*President & CEO, Canadian Pacific*

Yeah, I think in the Ohio region, that's the only strategic one I see where there's demand and where there could be enough volume to sustain service. But if I go elsewhere and I look at like the Genesee & Wyoming, Jack and his team, they're always looking for accretive expansion. Other short lines have now become available that stand-alone may not be worth a lot. But

when you connect it to their network, it starts opening up lanes on the East Coast. There's some stuff we're looking at that we're talking about down- the-line automotive. You think about automotives coming from Europe. Right now, there's – if it's coming into Canada, there's one port and one option.

If there's a competitive option out there, if we had to do it in partnership with a short line or with an Eastern carrier for Canadian-destined automobiles coming in off tidewater, that's an opportunity we haven't explored yet. We're exploring it. We're looking at it. We have converted it. But it's an opportunity still left, and that goes to the story about adding to the merchandise portfolio.

So, those are new thoughts and new ideas that, in all honestly, when I talk about upsides, that wasn't in the CAD 200 million to CAD 300 million.

So, a lot of work. It's competitive business. We got to compete to win it. But I think we're in a good place to be able to compete for it.

## **Allison Landry**

*Analyst, Credit Suisse*

Okay. So, it sounds like there's ongoing discussions in terms of thinking a little bit differently about working with your peers and sort of creating these opportunities that would benefit both parties.

## **Keith Creel**

*President & CEO, Canadian Pacific*

Absolutely. And I think as demand increases again in for freight railroads and it is and it will, and as population grows, the pinch points are still the same. Chicago's still not been fixed. It hasn't been the problem because it hasn't had the volume. But when the volume comes back and you have the same challenges, you've going to have potentially a similar outcome. If that happens, the railroad, they can partner with other railroads to work around Chicago to create velocity and reliable service, both controlling cost as well as providing service and revenues, is going to win in the marketplace. And we have that kind of mind. So we'll look at all the gateways. We'll look at both Eastern carriers. If there's things that we can do shorter transactions to extend our reach to provide better service for our joint customers to grow revenue, we're going to do it. That's just the way we're wired.

And if you have like-minded leaders on the Eastern roads that are willing to do the same thing, that can be pretty compelling. So that's something. Again, that's an area that we haven't even reached yet. It's an area that's on my horizon. It's in my thought process and rest assured, it's something we'll explore.

## **Allison Landry**

*Analyst, Credit Suisse*

So probably fair to say you would favor one Eastern Rail over another at this point?

## **Keith Creel**

*President & CEO, Canadian Pacific*

You tell me. Yeah, there's definitely one like-minded leader for sure

## **Allison Landry**

*Analyst, Credit Suisse*

Any thoughts on what's happening with NAFTA, how you think about the various scenarios and what the risks to the franchise could be?

## Keith Creel

*President & CEO, Canadian Pacific*

Yeah. I think it's a choppy process. I think it's a frustrating process. I've tried to stay close. I've dealt with the Canadian Ambassador to the U.S. I attended dinner with Canadian CEOs, with the U.S. Ambassador to Canada. We understand between the two countries how critically important trade is. There's a larger concern with this tri- party deal that the U.S. obviously is trying to improve. What's being proposed at this point if I put my Canadian hat on is not acceptable to Canada.

Put my American hat on, I know what their demands are. Is there a deal to be made? I don't know where the pin's going to fall. So far, they haven't made a lot of progress. So, I think about in the absence of the deal what happens, number one is the sixth-month cancellation process. They haven't gotten there yet. If it goes away, we fall back to a bi-party agreement that exists between Canada and the U.S.

And looking by business mix, the most exposed, the most material would be automotive industry and that's only 3% of our book. So, does it keep me up at night? Do I want it to happen and do I think there's some risk? Yes. But is it end of the day going to be hugely material to this company? No. But again, I think cooler heads will prevail.

Once they get through the negotiation, those are tough, tough challenges. And obviously, Mr. Trump and his team, they pride themselves in negotiation. But there are like-minded capable people on the Canadian side too, and I think we come to a place that make sense for trade between both countries because we're both heavily- dependent upon the other.

So again, we're staying very close to it, we're paying attention to it. But right now, I'm not losing sleep over it now, that's for sure.

## Allison Landry

*Analyst, Credit Suisse*

Okay. Let's see, so thinking about – maybe getting back to the share gains on intermodal, do you think that with the tight capacity – I guess what's the addressable market for domestic intermodal in terms of the number of truckloads that you think would have the potential to convert annually. Like, for example, the Eastern Rails have talked about 9 million truckloads a year, that's addressable. Do you have something like that?

## Keith Creel

*President & CEO, Canadian Pacific*

I like more of the overall demand, I haven't looked at the exact number of truckload. There's a lot of truckloads still going across the border back and forth between Montreal, Toronto and Chicago. That's a key lane. We have a great service offering in.

Domestically in the country, I think about the modal shifts. I think about the macro environment. I think about Amazon. I think about if Amazon is going to become more present in Canada, which they are, they're going to develop that market. What are those boxes going to be shipped on? Well those boxes are going to be shipped on UPSs of the world, Purolators of the world? Who are they going to ship with? They're going to ship with the railroad that's got great service, reliable service, speedy service. That favors my railway in the domestic markets.

So I see an environment – I think quarter-to-date, overall intermodal, this is everything. This is intermodal international as well as domestic. We're up about 5% quarter-to-date. If not for Yang Ming, which is the international contract that we're covering those losses now, we'd be up 10%. And that's being driven by strong, strong demand in domestic.

We're doing things to improve our service offering. We're investing in reefers. So everything that's temperature- controlled, be it heat, be it cold, that's a value-add. On top of the value of the network we're going to have the best-in-class technology that

exists with the investment decision that we made this year. We're developing and spending money on our transload facilities. So we've got a facility we've opened that's in Vancouver that you can't replicate. We've got 80-something acres of land, co-located by our intermodal facility that we can grow into, that we own. We don't need permitting. We just need bricks-and-mortar and a business case to do it, which we're developing.

We've got the same land in our facility in Toronto. We're not trying to develop a new facility. Our footprint for the existing facility has enough land to double it in size and capacity. It's just a matter of doing the contracts to build the facility. We've got similar capacity in Bensenville. We've shut the hump down there. We've got a lot of yard that's not developed. We've got a hump yard where intermodal facility in Montreal that can expand. We've got land outside of Montreal which is playing into our automotive strategy.

We talked about that on the last call where one of these automotive customers which we lost last year because of price, we weren't going to chase the business we weren't making any money on it. It wasn't even earning its cost of capital. I was not about the cut the rate to keep one-third of the business, we lost all of it. Well, now, because of service and the value of service, we're taking a piece of land, their money, their investment. They're going to spend to put the asphalt down. They're going to operate the facility. It's going to be hook-and-haul for me. It's using a piece of land creating value.

It's not congesting my existing automotive facilities, so I don't have the risk. Now they came back and signed a contract with us. In 2020 we take 100% of the business, and it's better than our average book of business on profitability. So there are a lot of those unique opportunities that are coupled to this railroad that are being developed that from a revenue standpoint, from a value standpoint, and from a cost control standpoint that are unique in our space, very unique in our space.

## **Allison Landry**

*Analyst, Credit Suisse*

Sounds like it's just a matter of timing.

## **Keith Creel**

*President & CEO, Canadian Pacific*

It's also timing. It's making sure we don't – and I said this a minute ago. It's something I was thinking about. This team, we've been in a rightsizing. Number one, we never had service. We never had reputation for service. To get it, we had to create the right culture and to create the right operating model. So we've shrank, shrank, shrank. We've got it created now where it's running like a sewing machine. We've got a lot of capacity. We've got a macro demand environment both from rail as well as economy as well as truck, macro and micro, everything is turning our way.

Now, the thing you've got to be careful about is you do it in a controlled sustainable way. I cannot and will not be everything to everyone. I've got to make sure I tell the marketing team every day, listen, I'm not going to sit there and say bring on 20% more business in this lane if I'm going to deteriorate the service for my existing customers. I'm just not going to do that. I'm going to do it in a controlled fashion.

So I'll give you – for instance, we've got an international steamship – not customer – company that wants us to help them today. So I've looked at it and I've said, you know what, let's look at the lanes where we have capacity on existing trains. I'm not going to adversely affect my existing customers. I'm not going to add train starts. I'm not going to constrain the network. It can come on – I mean the margins in the business is pretty compelling. I said, so fill those trains out. You can sell that on short term. But if you want to do it long term, they're going to commit. Otherwise, I'm not going to jeopardize.

So being thoughtful like that to me is critically important because the reputation we've created for service was hard to get. We had to work really hard to do it, blood, sweat, and tears for the last four years. I'm not going to forget that, and I'm not going to allow our desire to bring top line money to the company to affect our ability to take it to the bottom line, because if I do, I jeopardize the entire thing. So we're going to be very disciplined, very thoughtful, very strategic, and figuring out what that

right mix is in a macro environment where in just about every lane and every commodity, we've got opportunity and demand. There's a science to that. We're going to make sure we get it right. We're going to take our time and do that thoughtful strategically and make sure it represents and reflects the principles that are creating our success in the down market as well as we'll continue to maintain it in the up market.

## **Allison Landry**

*Analyst, Credit Suisse*

What you said reminded me of a rail that is private, that operates in the West, obviously had some major service disruptions a few years ago, spent a lot of capital from at least appearances stake, has been using price to fill up their network. Is that – I think if you look at that sort of holistically and just sort of from a philosophical standpoint with what you were just talking about, is it fair to say you would disagree with the way that they handled that or are handling it?

## **Keith Creel**

*President & CEO, Canadian Pacific*

I wouldn't criticize them. I mean they had a very unique challenge in the winter of 2013 and 2014. I sat at the same table, in the same firing line with the STB hearings as they sat. They had to spend some capital. Obviously, some of the business they spent the capital for has gone away, some of the crude that we all enjoyed. We thought the same thing they thought. They were just caught up in a cycle where they've spent the money to handle it. They didn't have the surplus capacity. I happen to have surplus capacity. So it affected them in a different way than it affected us. But once you've got the rail on the ground, you've got the costs, the fixed costs, to cover your fixed costs to create cash and to pay the light bills, you've got to try to fill it up.

To me the right thing to do though is the best you can in a very disciplined fashion is to be very strategic on how you spend that capital. We're very conservative, we're very thoughtful, we're very disciplined on our capital allocation. It's something that were even in our compensation side return on invested capital becomes a large portion of our annual STIP and long-term compensation on a go-forward basis. I'm not going to destroy value from officers either or for my shareholders. So it's something we'll be very thoughtful about and not get ourselves in that kind of situation. But sometimes you get yourself in that position. If you commit a lot of business and you have a lot of growth you can't control and you throw a lot of money at it, if the service is bad, while you're doing it, trying to play catch up, you might wake up after you spend all that capital not have the business there that you thought you had in the first place. And that's a terrible position to put yourself in as well. So I'm mindful of all those things. We're not perfect. We're going to make mistakes.

But those disciplines will keep you out of trouble or at least in less trouble and help you manage the down cycle and the up cycle with a much better outcome for your shareholders, in railroads we don't do it. That's probably the best way to say it. It's a high capital intensive business. You're making 30-year decisions. It's easy to go chase short-term revenue, but if it's not the best long-term value creating decision, you're going to pay for it or your predecessor is going to pay for it. Your successors will pay for it. Not the legacy I want to leave.

## **Allison Landry**

*Analyst, Credit Suisse*

Got it. That makes sense.

All right. Any last questions? All right. Thank you, Keith.

## **Keith Creel**

*President & CEO, Canadian Pacific*

Thank you. Appreciate the time. Take care.