CP NEWS

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MANAGEMENT DISCUSSION SECTION

Brandon Oglenski: Okay. Good morning, everyone. Again, Brandon Oglenski, I'm the Transport and Airline Analyst here and next up here at Barclays, we have Canadian Pacific Railway are presenting and Mr. Keith Creel, the newly – COO of the Company, but he's been at CP now since 2013, I believe.

Keith E. Creel: Yeah, that's correct.

Brandon Oglenski: Before that, he was the Chief Operating Officer of Canadian National and has worked pretty extensively with Mr. Hunter Harrison. I know that he's not in the news at all these days, so. But just to get started here, CP, I don't want to say that you are the smallest Canadian railroad, you are the second biggest up in Canada and a pretty significant player here in North America. But Keith was really involved in the transformation in the company. A lot of people in the room will know that Bill Ackman and Pershing Square got involved in late 2011, when CP had an operating ratio of north of, let's call it 80 and when Hunter Harrison came in and later Keith, you guys were pretty successful in driving operating ratio, now down below 60, I believe, and effectively double profitability in about three years time, maybe even quicker than that. And today, CP is a pretty diversified business, you guys are running in about 35% Ag and potash and grain on the revenue side, 30% industrial, chemicals, merchandised business and 20% intermodal, 10% effectively met coal, and autos making up the remainder. So, just to give folks some context here that might not know CP that well.

We're really just here to figure out what your vision is for the company, Keith and before we get started, if we could just queue the room here.

So if you currently own Canadian Pacific in the room, yes, number one will be overweight, two equally, three underweight and number four would be no ownership. A lot of potential owners in here Keith.

Question number two please. All right. Is the room is biased towards CP right now, positive, negative or neutral?

Pretty favorable skew there. And question number three please. In the room's opinion, through cycle, EPS growth for CP will be above peers, in line with peers or below peers? In line with peers? I think that might have been a different answer a couple of years ago, Keith.

So I think with that, why don't we kick it off, and just I think we have to, on the last conference call, when it wasn't out, so you'd be named officially CEO of the company this month. What is your vision now that you're at the top of CP and what's the path forward for the company?

Keith E. Creel: The vision essentially is to complete the plan that we started four years ago. So to your point, I came to CP with a mandate to change, change the operation, fix the engine. Hunter and I are in the team for the last four years, I think he’s got six months ahead of me, so I joined the party six months after Hunter, early 2013, and it's been a record transformation. At the same time though we've gotten the engine, so to speak to a point from a service level, from productivity whether you look at train links, train weights, fuel efficiencies, all sort of the levers that drive the big cost buckets in our business, as well as the service offering we're giving to the customer, it's to me, industry best, at or near industry best. We've got a very capable competitor that's east of us certainly, they're good railroaders as well. I think Canada benefits from the two best run railways in the industry, if you look at service metrics, you look at the operating metrics, you look at our cost control, but more specifically, CP now, the next part of the story is to grow the top line even more.

In the past, our franchise, we never had service, we – because I competed against when I can say this in my previous life, were disadvantaged because of that. You know we had service sensitive customers, domestic intermodal, that's an area that we’ve grown, driven some growth over the past three years. They quite frankly didn't ship with this company, because they can't trust the ship, it would get from the location in Toronto to the store shelf in Calgary or the location in Toronto, the distribution center to the store shelf in Regina, the key markets, domestic markets in Canada, you just couldn’t depend on this company to get it there, so we didn't enjoy that business.

So what we started to do and focus on, is how do we convert service to growth. Number one, you got to get reliability, you got to get credibility, and while you do that as you establish reliability and credibility to the customer, you do it by certain assets, you do it by lowering your cost, your cost structure goes down, and your credibility with the customer goes up. We are at a point now, where we're having discussions with the customers, now open the door and speak to us. So we've driven dramatic growth in domestic side. Last year at a down market, we're the only railway in North America, the only railway in North America that drove positive intermodal growth, and it was driven by domestic growth, which depends upon service.

And we're just, the tip of the iceberg with that, there is still a tremendous amount of run room, so to speak, and its more not focused on taking share from my real competitor, its focused on taking share off the road. This franchise, unlike no real competitor, you want to make some kind of comparison, an investor asked me this a while ago, they said what's the opportunity, well, it's big, but again, you got to have truck-like service offering, you got to be reliable, and you got to be transit on competitive, with the strength of our network, we are shorter in the key routes and domestic intermodal in Canada, it gives us an ability to go out and sell a product that is unique in the industry.

So now that we've got the reliability, now we can go to the customers, other than some of the big box retail customers we've had in the past, we're partnering with wholesale, we're partnering with trucking companies. They're an extension of our railway and extension of our sales force and that's what's driving growth. So that's a key area of growth force as we go forward.

And if you look at intermodal, and there has been a lot of questions about intermodal. To really understand the intermodal business, international intermodal, the margins are low. Domestic, it's much more service sensitive, so the customers are willing to pay for it. Rule of thumb, you got to move three international boxes to get the same revenue for one domestic box. So when you take a footprint, and the Canadian model is different than the U.S. model, because of length of haul, that's a key piece that's different.

When you say a domestic move in the states, it's going to be somewhere on average probably 500 miles, 500 to 600 miles would be a domestic move. Comparison for our Canadian Railway, because the larger metropolitan centers are so far apart, our average domestic move is 1,500 miles. So it's hard, it's a whole different dynamic that have occurs once you start to create that truck like service and transit and reliability, you can grow the top-line quite a bit. And again, compared to domestic versus international, the margins and the sustainability is a lot more attractive than the international businesses and we control the terminals. We control the product from picking it up to delivery and which is positive.

The other piece that's super positive for this franchise and our story is now that we got service reliability and low cost, we're going to grow merchandise business. So you said the mix a minute ago, right now, we're about a – actually 40% based on last year's revenue, 45% bulk which is coal, which is potash, which is grain predominantly. Then you got 35% merchandise and then 20% intermodal. That 35% merchandise, we're in a position now again think about what drives strength, the franchising service offering on domestic intermodal is our franchise footprint. Now, our predecessors at this railroad use our franchise footprint as an explanation to why we couldn't perform.

So we were disadvantaged, because we went to the Canadian Rockies. I heard, I competed this company a long time that was always how we explained our CP's operating ratio, would always be worse than my competitor, because of these big mountains we go through. While, they fail to tell everybody that it was 220 miles shorter to go through those mountains.

So straight-line is always going to be shorter and faster than a curved line. So when those markets again, if you've got customers, that never could depend upon on your service, merchandise customers that run similar lines in Canada, that might take a product say from Edmonton to Vancouver, or Edmonton to Toronto to run that facility, they couldn't trust us in the past because we had shut the similar lines down now that we've established trust, we can go out and say, listen and I'll give you a real for instance. We just recently submitted a pretty large bid for a customer and I was at our sales, call it a sales meeting, it was actually sales training session two weeks ago with our new Chief Marketing Officer and the team, and there was an account they put up on the board. So if you look at this account, they were enamored with our low cost, now we can compete, we can't be beat, we can give a comparable competitive way to make money. In the past, we couldn't, and well yes you can, but the reality is selling services, what do you do with your franchise, and in this particular customer that we've been on, effectively in this particular lane, it's an eight-day transit.

With our service, with our shorter route and the simplicity and you take out interchanges, where it's direct or it's in the destination instead of switching between two railways, we can get them there two days faster. So you get a 25% faster transit time, they own their own cars, I remember the numbers, 4,160, I did the math. You do the math 25% faster, if you get on 25% less cars, it's over $100 million of capital. If you can't go and tell a customer, how you can save them money and they still give you a fair rate for your transportation by selling service, then you are in the wrong business, that's compelling.

Those stories were just starting to be able to happen, because again we have to establish that credibility, but that's what gets me so excited. On the growth and the top line I'm focused on this railroad, we've said this numerous times, there's $200 million to $300 million of that kind of business, as these contracts come open, and as these doors get open, and as the sales force gets more discipline, and they have the same kind of culture and the sales force that we have in the operating side, it's extremely powerful that will allow us to repatriate that business and grow the top line and drive very meaningful earnings, earnings growth as we go forward.

Brandon Oglenski: Well, I don't want to deviate from the top line because I think that's very interesting for your stock. But I'm going to ask one that might be a bit critical, and I'm sure this room wants to know. M&A was a big piece of the CP story last two years. Obviously, you guys went public with an offer for Norfolk, now that was more – I think, maybe tied to the vision with Hunter. But how does consolidation factor in? Is that still something that you see CP being involved in the future, and is that just not a priority at the moment?

Keith E. Creel: Yeah. I would say, number one, it's not a priority at the moment. We've got plenty of opportunities that we're focused on to drive earnings growth by doing the things that we talked about within our story. Long-term though, our thesis remains the same. I've always said this and I will always say this, there is only so many railroads that are going to be built, you're not going to build new ones. If you believe that we're going to have the population growth and if you believe that they're going to consume goods, then you have to believe that more freight is going to go the railway because the public highways can't handle it all.

So if you're going to have growth, consolidation will have to occur, because you're not going to be able to create the capacity without consolidation again and I don't want to get into the weeds too much. Every time, you handoff cars between railways, it's an opportunity for somebody to make a mistake, it's an opportunity to miss the connection, the cars dwell, it drives up cost, service is not reliable. So if you can eliminate those handoffs that occur in this industry, and create a longer, simpler, more efficient franchise, that's how you create capacity. So eventually it will happen.

So my focus is, number one, short-term. Let's do what we have to do with, then we've got a lot we can still convert and a lot of opportunity to drive earnings. Be the best run railway, and if you are the best run railway, when there is an opportunity for that consolidation, who would someone want to consolidate with and who would they want to partner with. I fully believe that again, it will happen, and when it does happen, if it's right for this company, we're going to be at a position, where we're going to be run well, low cost, it's going to be good for our customers and it will be something I think will be involved here.

Brandon Oglenski: Okay. And obviously your shareholder base has changed a little bit since then...

Keith E. Creel: Yes, yes, that's correct.

Brandon Oglenski: And by the way, everyone knows that you can an email questions, my team will read them anonymously that addresses or addresses up here or just want, raise your hand, we'll get a mic around there, we have one appear. While we bring the mic up, Keith, so coming back to the top-line opportunity. I recall in the Analyst Meeting, I think September 2014, it was right in front of the arguably energy depression in North America and sorry if it pains and I bring this up, but we did have an outlook for CP to have a 10% top-line CAGR for four years, it's pretty aggressive, but I do think your predecessor company actually achieved that in the prior four years leading up to it. So definitely proven attainable by railroad, but not easily attainable.

Why should skeptical investors say that, all right, now CP can convert that top-line and keep in mind, so – I think you did have a 11% crude oil revenue at the time and that's down to about 3% or 4% today, so you have had significant headwinds in the business.

Keith E. Creel: Yeah, so let me speak to the crude piece. Crude was about 5%, 6% of our business and it was a big piece back in 2014. I remember correctly, it was a third, a third, a third, of the growth that we were going to drive. A third in intermodal, a third in price and a third in crude and energy. So now crude has came back towards only about 1% of our business. So we don't have that anymore, but if you look at our growth last year, effectively, if you took crude out, we were driving about 5% growth, 5% revenue share growth taken it from truck, taken it from our competitor.

If you look at our business right now, our RTMs, on an RTM basis, number one, we had a record year, last year. First quarter was the best ever, first quarter for CP grain movement in our history. We had no weather and the assets turned fast as a result of it, and we did a phenomenal job. We got pretty tough comps this year and then in crude last year, we only moved 38,000 car loads, 39,000 car loads over the year and we moved 17 of those in the first quarter. So we've got two extremely meaningful headwinds this year. From an RTM basis, we're just slightly below flat, which is what we expected against those huge comps and if you take crude out alone, we are about 4% RTM growth. So in the – the opportunity for this company from an earnings potential this year is more second quarter and third quarter because if I look at second quarter last year, we ran out of grain.

Second quarter last year, I think we didn't move hardly any crude at all. So from a comp standpoint, you'll start to see the strength of this franchise and you'll start to see the things that I'm talking about play out as we move into the second quarter and third quarter. And that should give you the confidence to drive the kind of the growth we're talking about on the top line and our guidance we're at high, single digit EPS and in all honesty and complete transparency, that's driven primarily by margin improvement, by running the railway better, by some tailwind from pensions, offset a little bit from that headwinds from land sales, but overall it's about operating the railway better and it's about productivity synergies.

So if we get a favorable volume environment from an earnings potential, then it could become even more exciting than it has been. I mean if you look at our peers, we drove a meaningful difference and our earnings potential doing the transformation, but even last year, I think there are only two railroads that drove positive EPS, maybe one of those two and we had a big headwind with crude that goes away after this quarter this year. So it's pretty exciting there.

Brandon Oglenski: Barry?

<Q>: Yeah. I have two questions. One just on the new wins and the sales front, I think you brought in a new head of sales and a year or so ago, if I my memory serves me and if you were to look at new wins versus business lost, kind of quarter by quarter going back over the last couple of years, are you already starting to see meaningful progress yet or is it more in front of us? So that's the first question.

The second question, are you seeing anything in terms of comeback yet in oil and gas or sand? Thanks.

Keith E. Creel: Yeah. So I would say that we're seeing some of it. Again, it's been muted by the crude piece. The things that we've lost, what I would say the losses has been low margin business. I am not going to – I am not going to chase business, I've said this all along, I've been talked better than this, I understand. This is a heavily capital intensive business. At the end of the day, if you go after business, that doesn't earn us cost of capital, eventually, it might be make you happy now, but if you are a long term investor, you're not going to be very happy with this team at all and you can't sustain it. So sustainable long-term growth is key to make it and to succeed in a capital intensive business. This is an operating company that's never going to change.

So if its low margin business and a customer comes to me and I'll – this past year, I had to make two of those decisions, never easy decisions to make. Part of the business that we've lost, that's not, if I had that business margin, growth would be even larger because it's muting it. It's been stuff that at the end of the day, if the customer comes and asked you to take a $10 million haircut on a $60 million contract on low margin business, what are you going to do? I couldn't say no fast enough, I am sorry, I appreciate your business, but I am not going to buy your business.

And then the other piece of the business we lost was also not in the biggest margin, damages, those kind of things cost a lot of money. It only takes one or two, drop a couple of those car loads and cars over and you're not making a whole lot of money in that business. Margins that in the past, the business that we walked away from, was business we weren't making money on. It was business that were in lanes, that our profitability didn't earn us cost of capital.

So when it comes down to rebid on that contract, what you're going to do? I'm going to play this strength with our franchise, I'm going to go to the customer and say, listen, I can help you save money in these lanes, I cannot cut my rate, I can increase my rate, I think I can increase my profitability and I can increase my return and does it mean I got to walk away from some business that I don't make money on. I'll do it if I need to do it, and that's what we did. I think they were very smart decisions, right business decisions staying long-term growth for this company.

So we're – long answer to your question, but we're starting to see some wins, but the real opportunity is really as we go forward and with the new marketing team we have, John Brooks who is with me to the left is our Chief Marketing Officer now. I'll tell you a little bit about John. John has been in the industry over 20 years, he worked with UP, he came to the CP from the DM&E. I met John when I first came to the CP and realized that this guy has the kind of the discipline, pricing discipline, market knowledge that fits the operating discipline that we want to expause and that we've created inside of our company.

So over the last two years, he has run the Bulk unit and the intermodal unit force. The international intermodal, we had another gentlemen that we had an attempt for a Chief Marketing Officer about two years ago, that turned his focus only to that. John is the guy that created the strategy and drove the strategy and drive – that drove the domestic growth for us last year.

John has a phenomenal knowledge of the bulk franchise as well. So when I look to create a Chief Marketing Officer, the thing that I know from history, this is an operating company. If you understand how to run the operations and sustain service and low cost, it's a sustainable business. I know how to do that, I've been taught by the best in the business to do that. I'm not going to dilute my effectiveness as a leader.

So I knew when I became the CEO, I couldn't spend the same amount of time that I spent with the marketing group and still fulfill my CEO responsibilities and not diminish the time that I spent in operations. So by creating John's position again, John is going to have a laser focus, and 100% of the time in marketing on the growth side and then, in the absence of John and the position he vacated, we went out and recruited a phenomenal talent for the company, that gentleman's name is Jonathan Wahba, who has a vast experience, previously worked for another railroad, another Canadian railroad, left in 2010, worked for Schneider, Canada certainly knows the trucking industry now, so he knows international intermodal. He knows trucking and then his most recent position he spent three years as the COO of Kriska Trucking, which is located in Ontario and feeds the whole cross border domestic market as well as domestic going across the country. So he's got truck knowledge, domestic knowledge, international knowledge, tons of energy and he's our ace player that wants to perform that if he gets paid for performance he's going to do it, he's been with us for two weeks. So I'm super excited about our ability to grow the top-line and they convert this value creation from service.

Now, specific to the energy side, frac sand, we took it up turn I guess over the second half of last year, probably more so the fourth quarter. We've seen continued strength in that market and the partnerships that we have, the product coming out of Wisconsin is speeding the locations of crude, where as long as crude is going to be mined, the light stuff, it's going to be eating the sand. So those are – those to me are long-term strategic plays that serve again to strengthen this franchise, that's pretty positive for us this year.

<Q>: Thanks.

Brandon Oglenski: If there is other questions, just let us know and we'll get a mic to you. Okay. So Keith, I don't want to simplify too much, but is it just that you look at a real estate portfolio like a railroad and say, press on the management teams and a lot of these companies didn't really leverage the portfolio in the right market, is that right? Maybe took the easy way out with what used to be the backbone of the rail business like coal, and there's just a lot higher value opportunities in the freight market that...

Keith E. Creel: I would – I don't want to be critical of anyone, but – and I come back to one fundamental thing. It's an operating business. If you don't know how – if you don't know the operation and you don't know how it should be run and can be run versus the way it's being ran, you don't recognize the opportunity. That's the difference. So if you've got the right operating model in precision railroading, where you effectively, you got to provide service, you do it by turning assets faster, which means you have less assets, which gives good service, especially if you're the car owner, if you think about a railroad, about 50% of the cars normally rough plus or minus on a railroad, are not owned by the railroad, they're owned by the customers.

So if you're going to turn their assets better, you're going to lower their cost, you can charge them the higher rate and still lower their overall transportation cost to give them good service experience, by doing, actually controlling your own cost. And as long as you do it safely, you need to develop people, that's the key to the whole thing. You get to have a team that can execute it. This is – it's not rocket science, there's not some secret recipe of the key ingredients of precision railroading – a service scheduled railroad, I mean, Hunter has written three books about it.

We've all read them, the key is do you have the team to execute it and do you have – what I call the discipline, it's a performance culture number one. It's got to be all rules – railroads can be dangerous and if you don't run railways safely, especially in today's environment, you're going to lose your license to do business. You're going to beg for regulation and make things so onerous, so you can't make money in the business, which is going to hurt the nation's economy, which is – it's not for any one. So the safety piece is key, but the people are the ones, who make it safe.

So if you create a performance culture, where you comply with rules and people work safely, they work efficiently, you understand how many assets you need be it a locomotive, be it a railcar, be it a track, be at a hump yard, whatever, those assets, if you understand what it takes and you work towards what you have versus what it should be and you close that gap, which is what this company has done for the last four years, it's a recipe for sustainable success. But again, it takes tough change, it's not easy. You can't get business and then not have the discipline to go to negotiating table with the unions that you work with and as much as you value those employees, they're human beings.

We all want to make more money, so if you give them 10%, they'll take 10% all day long. You got to have the ability to say no, and this is why, in your best interest I can't do that because I am going to give away all of the profitability, and I am not going to have low cost anymore and I'm not going to be able to compete in marketplace. So it's not a complex recipe, but you're going to have the right people to execute it, you have the discipline to execute it. And if you do, you're going to make money in this business.

And fortunately, I was – I've been blessed with great people I've worked with. I had a phenomenal mentor. I happen to believe and I know because I've done this now in three railroads, this recipe works, I don't care where you're at. You could take the same approach to any business, in a sense and make money in operating more efficiently and improve your margins and provide better service and grow the top line. This is simple, basic fundamental, the right way to run a business, to run a company. That's what we're doing day in and day out.

Brandon Oglenski: Well, it's interesting you bring that up because a lot of the U.S. railroad do trail your profitability and your predecessor company's profitability – as you mentioned the two highest margin railroads in North America. But is there something different about specifically the U.S. operations, right, because I believe that the big four railroads in U.S. have conference negotiations with labor. And if I am not mistaken, CPMC are not part of that conference, is that correct?

Keith E. Creel: That's correct.

Brandon Oglenski: So does that labor differential really provide some advantage for the Canadian CAGRs in the U.S?

Keith E. Creel: I would say service advantage or liability advantage, some cost advantage, yes, but I'll speak to CP, and I'm going to speak to the other road, where 70% in Canada, where I don't have the agreement and 30% in the U.S., and I don't completely have it in the U.S. So it's not moving the needle. Now, if we ever were to get a progressive agreement like that in Canada, could it be a quantum leap? It could, because the employee is going to benefit, they're going to have more scheduled reliability, their quality of life is improved, our cost is going to reduce and our service is going to be improved. But that takes a lot of change.

And it took us in my previous life a long time, and I think nine different rounds of negotiations to ever get the first one done there. We've – we sort of broke through at it CP after four years last year. So on the U.S. side, I've got everyone except for the Sioux conductors. So about two-thirds of the U.S. running trades employees are under an hourly deal, which is a progressive what we're talking about versus getting paid by the mile in about a third not. And – but we've been back and forth of that third, and I think in time, common sense prevails, better quality alike, you make more money, you're at home more, you're going to get to the point where that changes, it's going to be so hard to accept and people are going to say, what it's not emotional anymore, it's rational. And I think we'll get there with the Sioux conductors too.

Brandon Oglenski: We've run out of time here and we'd like to have you on stage for another 15 minutes if I could, but can we queue up question number four please? In your opinion, what should Canadian Pacific do with excess cash, couple options on M&A, share repurchases, dividends, that pay down internal investment? Not too much of the surprising answer there.

Can we go to question number five, please? In your opinion, what multiple of 2017 earnings should CP trade? And it's been pretty interesting the valuation of your company, I think part of its the political environment here in U.S. too.

And then question number six, what you see as most significant investment this year for CP, core growth, margin performance, capital deployment or execution? Core growth.

So Keith, as we have you for just a little bit more here, help us understand what metrics are you really focused on for managing the business going forward, apart from obviously a big top-line focus?

Keith E. Creel: Well, the key thing for me from a metric standpoint is, we can't give back what we gained on the operating side. So part of our objective this year was, we're not talking about a large RTM growth, but we're talking about getting back to – I'm pretty excited it's not contraction, it's expansion.

Positive RTM growth year-over-year, doing that and absorbing it with existing resources as much as possible, is the key to driving additional operating margins, that's one of the key leverage that we're pulling. So I've got to be very cognizant of that. So I'll focus on those areas, train length matters, train weight matters, train miles matter, those are the three measures I'll look at, and speed matters.

Speed is critical to the whole thing, because it's what you poured over all the assets. The faster they turn the fewer are needed, so that's simple. So those are the areas that I'm focusing on from an operational standpoint and from a revenue standpoint, we're entering into some pretty exciting times. We just bid on a very large contract that we should get an answer on, I would think sometime April or May. This is a customer that in order of magnitude, we did about 60 million of revenue, rough numbers last year. There is an opportunity to grow that somewhere between 60 million to 110 million, and there is some bandwidth in there that 110 million, that is a reflection of those stories that I'm talking about. I've got the shortest route and they own the assets. And if I've got the reliability, then why shouldn't I win in the business? I can help them save money, and I can make money, that's all powerful. So, those are the key focuses on the marketing side, that John and his team are going to be looking at, as we go forward and creating again the discipline in marketing, and the professionalism in marketing that we have on the operating side.

Brandon Oglenski: Well Keith, I think we have to leave it there, but thank you very much for coming down to Miami. Really appreciated.

Keith E. Creel: Thank you.

Brandon Oglenski: Yes. Thank you.