Transcript

Stephens Annual Investment Conference

November 15, 2023

Webcast

Corporate Participants:
Nadeem Velani – Executive Vice-President & Chief Financial Officer, Canadian Pacific Kansas City

Other Participants:
Justin Long – Managing Director, Stephens

PRESENTATION

Justin Long
Managing Director, Stephens

This is Justin Long with Stephens. I want to welcome everybody back to our next Fireside Chat with Canadian Pacific Kansas City, CPKC. It's been a very exciting year for the company. We're thrilled to have them here at the conference.

Sitting next to me representing the company is Nadeem Velani. He's the CFO. Nadeem, thanks for your support. And this will be a fireside chat format. So I'll start with some questions, open it up to any questions from the audience. And then we'll -- we'll go from there.

But Nadeem, maybe to just get things kicked off, could you just provide a state of the railroad, how things are playing out now that we're halfway through the quarter relative to what you were expecting coming into 4Q?

Nadeem Velani
Executive Vice-President and CFO, Canadian Pacific Kansas City

Yes. So first of all, thank you, Justin for hosting us and inviting CPKC. It's been seven months now under the CPKC journey. And I can tell you that first of all, I'm thrilled to be here to represent our 20,000 employees. It's been a tireless and a very exciting seven months of CPKC, and I couldn't be more proud of what the team has delivered when you think about integrating systems, putting the team together, putting three cultures of Mexico, Canada, U.S. together, advancing our safety agenda, improving on our industry-leading safety metrics.

You think about what we've done in terms of investing in supporting growth near term and future, and investing that capital successfully, and providing competitive options that certainly is stirring the market to provide even more competitive options. So it's an exciting time. We laid out our five-year plan, our five-year agenda, at investor day not too long ago, and we see an opportunity that's unique in the industry, high single-digit revenue growth. We see the opportunity to improve our margins, double-digit EPS growth over that longer-term horizon over the five years through 2028. And free cash flow, which I think is maybe an underappreciated part of the story, of free cash conversion of about 90% plus.

So, excited about what the long-term holds, and excited about the team that we have, the network that we have, and couldn't be more excited for what CPKC is going to deliver. Going to your question on the near term, we're trending around 1.5% growth in RTMs quarter to date. Overall, there's some pluses, the potash and coal story of met coal have been kind of in line with what we expected, you know, strong performance year over year with some pretty easy comps.

Our energy, chemical, plastic area is growing tremendously. We've got some synergy opportunities that we're starting to ramp up on that with a new contract from Shell. We're seeing growth in automotive. That's been an area that we expect to continue to grow through

the end of the year. We have some new contract wins there that are also going to ramp up starting in 2024. But near term, those are kind of the strong areas.

There are a few challenges. It's been consistent with what we've seen so far this year is on the domestic intermodal side. I think that's a story I'm sure your conference has shared just the challenges in that sector that we've seen, and we haven't been immune to some of those near-term challenges. And then on the Canadian grain side, we're seeing some variability in terms of volume. The Canadian farmers specifically are being challenged in terms of selling into the markets near term. So, the way I look at that, though, is probably a bit of a shift of volume. So shifting from '23 into '24. The crop is going to move.

Our part of the crop is certainly less favorable than maybe the north. We had some drought conditions in part of the southern parts of Alberta specifically. And so, what doesn't move this year will move next year. So I think that's been more of a shift in volumes timing-wise. So overall, the quarters playing out not too differently than we anticipated. I'd say that volumes are maybe a point or two lower than we thought they'd be. But nothing to be concerned about.

From a cents/RTM, we're doing better, so the yields are going to be stronger. And from a cost point of view, we're certainly in line with what we expected. I mean, we talked about sub-60 type of OR for the quarter, and I don't see any reason why we won't be able to deliver that. September was very strong. We ended Q3 the right way with a very good operating ratio. And October was also very strong. So I think we're, we're starting to hit our stride from a cost point of view, hitting our stride as the network is improved and service is improved, and we're going to finish 2023 strong and enter 2024 kind of on a very high note.

QUESTION AND ANSWER SECTION

<Q – Justin Long>: Okay. Great. Well, that's a good way to start. And there's some puts and takes it sounds like right now. On yields being a little bit better than you thought, what's driving that? Is that just a function of mix? Is price better than you thought? Is it both?

<A – Nadeem Velani>: Sure, I think it's a combination partly. Currency has helped, so the Canadian dollar has depreciated and so that's certainly, as we translate some of our revenues back to Canadian dollars that's helping. Our pricing has been, has been strong. As contracts come up, we're still seeing favorable pricing above inflation as those contracts turn. And so that's been a positive as well. And I'd say that, that mix generally, has been favorable as well in the near term. So, overall yield is going to continue to show strength.

<Q – Justin Long>: Okay. Great. And maybe just to get this one out of the way. There was some news last week in Mexico on passenger rail, I think that's driven some weakness in the stock here recently. But I don't know if that was too much of a surprise for you. So could you just elaborate on the potential impact that announcement could have and any other thoughts you have?

<A – Nadeem Velani>: Sure. Yes. So you know, first of all, it was not a surprise. I think, been surprised by how the markets reacted to be honest with you. Right after day one, Keith, and John Orr, and Oscar, our president of KCSM, spent time with AMLO and the Mexican government and officials and offered to look at some of their rail infrastructure projects that they had -- were investigating and looking at themselves. And we offered to provide some of our expertise.

They shared that they wanted to look at passenger rail between Queretaro and Mexico City. And so we offered to perform a feasibility study which we're in the midst of doing as we speak. We should have that complete by first half of 2024. And so we're working with the government to look at what that could look like in terms of passenger rail.

So it's certainly no surprise. I'd say that when you think about how passenger rail and freight rail work together on the continent, we work alongside passenger rail across our network. You think about the Canadian network and from Montreal to Toronto, there's VIA rail, passenger rail in and around Toronto and southwestern Ontario. There's Metro links. There's VIA rail. There's all kinds of passenger rail that operates on both Canadian networks.

If you think about the U.S., with Amtrak, we've been seven years, straight years, at CP, the best-performing service provider for Amtrak. And even Metra, our performance in the Chicago area for Metra going on our track is high 90s level of service. So this isn't a surprise number one. Number two, we don't see it as a near term issue whatsoever. And we'll see what happens with the Mexican government and where their priorities are. And as things evolve next year with the new election, once they get the results of the feasibility study and they digest that and see what priorities they see, we'll continue to work with them. But right now, we don't -- we don't see this as a huge concern whatsoever.

<Q – Justin Long>: And do you have any insight into the areas geographically in Mexico that they're most focused on in terms of growing passenger rail, potentially?

<A – Nadeem Velani>: They've looked at for our line that that segment within Mexico City and Queretaro. I know that they've talked about -- they've introduced the Mayan train and some of that. But that's what I'd speak to. I couldn't speak to more of other parts of other rail networks so.

<Q – Justin Long>: Okay. Fair enough. Well, maybe we can go back to the KCS merger. As you mentioned, seven months in, so it's still fairly early. But if you were to take a step back and assess where we are, in terms of revenue synergies, cost synergies, and the base business performance for KCS, are those kind of three buckets, you know, where are we tracking relative to what you thought at the onset of the deal?

<A – Nadeem Velani>: Sure. Yes. So we're one company, one entity. So it's, you know, I won't speak too much into terms of dissecting CP versus KC, the legacy companies. But I would just say that KCS performance has been in line from a top-line point of view with what we expected, when we looked at the opportunity to acquire that entity.

And when we look at, from a synergy point of view, I think we're, you know, our current run rate is in excess of $350 million U.S. and ramping. We're ahead of the game in terms of synergies. More opportunities unfolded as we dug deeper and looked at, you know, peeled back the onion, and looked at the customer opportunities and the market opportunities. So that's advancing extremely well.

We're going to be patient. I mean, this is a marathon, it's not a sprint. So we're not going to try to over-commit. Part of why we -- when we had looked at the synergy opportunities, we wanted to make sure that that we could service it. We wanted to make sure we're not impacting any of our existing KCS or CP customers. So there's some capital investments that's required, from a car point of view, from an infrastructure point of view, siding point of view. So we're going to be patient. But at this point, we are ahead of the game in terms of revenue opportunities, and we have a lot of confidence, I think, over the next five years that our original, you know, billion dollars of revenue

target that we had outlined over the first three years was -- is going to be bigger and longer. So we highlighted that at our investor day.

From a cost point of view, we're pretty much in line. I'd say that as you get more opportunities from a volume point of view, as you grow the volume higher than where we are today, which is flat to plus 1% type of levels for the year, you're going to get more opportunities on the synergy front. So the G&A side from a headcount point of view is going to be a part of it, and we are realizing that today. But when you look at some of the sourcing opportunities and procurement, that's something that as contracts come up, and as you start negotiating with your vendors, it does take time. So we're starting to see some of those benefits here as we stand here today. But those are going to take a little bit of time for some of those opportunities to come up.

Bottom line, we're confident with the synergies, we're confident it's going to have a longer tail, and the size of the prize is going to be a bit larger.

<Q – Justin Long>: Okay. Great. And when you think about that $350 million revenue synergies that you've locked in already, what's the rough split between intermodal and non-intermodal within that number?

<A – Nadeem Velani>: Yes. So, you know, we introduced that Chicago to Mexico service, the MMX train, the one train 180/181. The anchor customers on that train are Schneider and Knight-Swift and their businesses is ramping up on that existing train. So that, you know, I put that at around $100 million type of revenue. We announced the ordering of 1000 reefers, refrigerated units that are starting to come into the network. And the size of that prize, about $150 million type of revenue number. That's going to ramp up, we're not at that run rate today. But that's going to involve proteins going south, and then coming back with produce coming north from Mexico.

So that's an area I think that will start ramping up later this year. We announced some -- a deal with Americold. That's going to take time for that development to occur on the network, on the land that we've allocated towards that. But when you look at overall of the existing $350 million, you're probably looking at about 40% of it existing today of intermodal and the rest, you've got automotive, ECP, and some of the metals business as well. And so yes, that's the way it split it up.

<Q – Justin Long>: And when you think about the opportunity for revenue synergies longer term, what -- do you think that split of that pie will look similar 40% intermodal, 60% everything else?

<A – Nadeem Velani>: You know, I think the intermodal piece we, our original view was probably we underappreciated the opportunity on the intermodal side. So I think our initial view was probably less than that. But I think that 40/60 split, as we stand here, as I just mentioned, I think that's a fair, fair estimate of, you know, five years down the road what it could look like. Because I think the intermodal conversion opportunity and truck conversion opportunities is certainly larger. And as you think about what you know, what it means, from a customer point of view to shift truck as a part of their transportation solution over to rail, I think that's going to be the easier conversion overall. So I think a 40/60 split is probably a fair estimate.

<Q – Justin Long>: Okay. That's helpful. Maybe I'll ask one more. And then I'll pause for questions for a moment. But you talked on the earnings call about an expectation for double-digit earnings growth in 2024. There's still a lot of uncertainties about the economy and the freight market. But you've got a lot of company specific tailwinds that we've been talking about. So can you just speak to your level of visibility in that forecast for next year, and some of the key drivers that inform that?

<A – Nadeem Velani>: Sure, yes. So you know, number one, as I mentioned, we're really starting to hit our stride here, from a margin point of view from a, you know, synergy point of view. So a lot of the self-help type of non-macro-driven opportunities that are unique to CPKC will, we're starting to see those and realize that.

So we're going to take a bit of a more of a bearish view of what the macro is going to deliver. So it's difficult to call that. I do like seeing some of the CPI numbers that we've seen this week, and what that could mean for rate hikes or rate cuts for the next year. So that could be supportive to the consumer. But overall, it's difficult to predict the economy. That being said, you know, when we factor in what we think is on the table for us as far as our key markets, I think we have a high level of confidence on what we can deliver from a revenue point of view. The pricing that we've been able to lock in this year, and recently, as well as the new contracts that are going to be coming up, I think it's going to be very favorable to overall yields. And then, when we look at how we're operating, we've gone through seven months of the integration.

We've seen some real improvement over our operating metrics the last, call it, three months, and you see that momentum building, and what that could mean to overall operating leverage. I think it's exciting for what it means as far as what we can do from a margin point of view, and from an overall earnings point of view. So I have a high level of confidence in terms of generating, you know, double-digit EPS growth. We'll see what happens with winter. It's pretty mild right now in Canada, but winter usually lasts about five months. So difficult to predict that either.

But I think, overall, when we look at our key end markets, we think about how we're operating. Think about what we can control and what that means for our overall earnings visibility, I'd say it's a very high level of view of delivering double-digit earnings. And that doesn't include any sort of buyback or any sort of other self-help financially.

<Q – Justin Long>: Okay. And I know you're exiting this year, it sounds like, at a sub-60 OR. There'll be some seasonality. There'll be some weather, realize that, but feels like that's something that's baked into the forecast for next year as a continuation of sub-60.

<A – Nadeem Velani>: Why don't we get -- why don't we wait until January for that, so.

<Q – Justin Long>: Okay. Yes.

<A – Nadeem Velani>: Thanks, Justin.

<Q – Justin Long>: And any questions from the audience? We'll go right here and then over to the right.

<Q – Unidentified Participant>: (inaudible)

<A – Nadeem Velani>: Sure. Yes. So you know, I'd say that when we looked at the transaction and what it means in terms of generating, you know, significant revenue growth. We looked at the base infrastructure, you know, making sure, ensuring that the sidings the network can support -- PSR can support the growth that we have in front of us, can support our service design. And so, even prior to Day One on the CP network, we were investing in the base infrastructure. KCS, while they were in trust, they invested in base infrastructure.

And so when we look at what it means, in terms of incremental capital, we were talking about $250, $300 million of pure incremental CapEx. Now, offsetting at -- that's a net number. We're also

offsetting with some synergies on the capital side, so, when you combine the two networks. So it's not significant. We've guided our -- on our five-year investor day to CapEx of $2.6 to $2.8 billion. And that's supportive of the growth profile that we highlighted kind of mid-single digit RTM growth over that period.

<Q – Justin Long>: Question over here to just cost inflation.

<Q – Unidentified Participant>: Yes. Just thoughts around the inflation and then maybe your ability to price above that. What you've lost may be over the last 18 months (inaudible), and how long it might take you to (inaudible).

<A – Nadeem Velani>: Right. So in terms of when you think about the inflation that we've faced in our industry, obviously labor was a huge increase in inflation that we saw this year. Now you can't time all your contracts to be able to mitigate that labor inflation, that same period. So I would put it this way: in 2023, we saw a huge jump in inflation, primarily labor, but even some of the purchased services and some of the raw inputs that we have in our industry. So inflation closer to 7%-7.5% type of number. Whereas pricing, you know, you can't get all your contracts, your 100% of your revenue to price in any given year. So there's a bit of a lag effect, right? So a third of our contracts would come up. You can price above inflation. And then a third of the contracts have annual escalators, but they're also, there's sometimes, there's a lag.

So what we face this year, speaking CPKC was higher inflation than we were able to price timing-wise. But now, as these contracts roll in, we can over the near term and into 2024, and you can price above those -- that level inflation and so higher than that 7%, and then you factor in when we look at 2024, you know, I certainly don't think we're going to have inflation anywhere near that level. I think we're probably closer to the 4% type of level when we look at what we have in front of us from a labor point of view, from a key materials and inputs. So, I think we're going to see the benefit in 2024 of being able to price inflate -- above inflation.

There's going to be a wider gap. And then you're going to get that lag benefit in 2024. So that's how I foresee it.

<Q – Unidentified Participant>: (inaudible)

<A – Nadeem Velani>: Exactly.

<Q – Justin Long>: Question in the back.

<Q – Unidentified Participant>: With the regulatory process with the KCS, your labor seems like you got a little bit above and a headcount (inaudible) levels have been over the last year. So to get the macro is weaker than it is between '24, you have the opportunity to go out of (inaudible).

<A – Nadeem Velani>: Yes. So absolutely. So yes, we were caught by surprise to an extent about from a macro point of view. But also, it was also by design. We're not going to answer the first Class 1 merger in 20 years with -- and being short on people, especially in this environment that we've seen the last several years of trying to hire and train and the challenge that that's created on service. Last thing we want to do was hurt our customers and hurt our ability to provide the service that we have high expectations for, that can support the pricing I just described.

So we intentionally, you know, we're going to be long on employees and then you factor in the macro weakness that was probably worse than expected. We became extra long on employees. That being said, we're in the midst of right now looking at the near term and into 2024. What's the right level of employees and I think we have the opportunity to not hire as much, to slow down some of

that pipeline of new hires and we can take some of the employees that we have on guarantees and we can put, invest in them to make them engineers. So we've been kind of pre-investing and pre-paying on the labor front. And again, I think that gives you another opportunity to why it can be accretive into 2024. Because you're not going to have that, that level of headwind that we saw in the past call it 12/18 months.

<Q – Justin Long>: So I guess building on that point, that was actually one of my questions. If we get into an environment in 2024, where volume growth is call it mid-single digits, in that ballpark? Does headcount grow low-single digits? Can it be relatively flat, given what you've just mentioned and the synergy opportunities?

<A – Nadeem Velani>: Yes, I think it can be -- if we were to generate mid-single-digit volumes/RTMs, I think flat to low-single digit employee/headcount growth is in line.

<Q – Justin Long>: Okay. Great. And cost per employee, I believe, on the last call, you gave guidance to be up mid-single digits. Was that on a sequential basis in the fourth quarter, and maybe you could talk about the opportunity in that area going forward?

<A – Nadeem Velani>: Yes. So my comments were more year over year, than sequential. The comp per employee is one of those that can be a bit difficult, because year over year, you get the pension impact. So our current service costs depending on discount rates. So next year, I can't guide to that until December 31st when we lock in our discount rates on our pension plan. That being said, stock-based comp is also one of those variables, right? So we mark-to-market each month. So each quarter depending on what occurs there that can be a headwind or a tailwind. So right now, it's going to, as we stand here today, it's going to be a big tailwind for Q4.

I'm optimistic that won't be a tailwind for Q4. But just something to keep in mind that that stock-based comp is always a moving part and it can have a meaningful impact on comp per employee.

<Q – Justin Long>: Okay. Question Over here.

<Q – Unidentified Participant>: (inaudible

<A – Nadeem Velani>: Yes. You know, so there's some easy wins on the intermodal side in terms of, you know, as we've seen with our service, and, offering a service that didn't really exist in the market, right? Alone is we've seen a step function in growth in this opportunity with the 180/181. We can, we can add additional train pairs and that's certainly something that we can do that can allow for growth pretty easily. Then, if you think about the terminal capacity, that's a key part as well.

We have a deal, maybe four years ago, with the Tollway, three years ago, in Bensenville. So we have investment in Bensenville that we have in front of us that can support the terminal capacity that's needed to grow into that end market. We have plans and opportunities in Vaughan, in Toronto as well, where we can grow. We have existing capacity today. We have existing capacity in Montreal.

So for us, when we look at our key locations, key terminals, we're in a very, very good spot. Where there's been some need in terms of other, call it, you know, capacity requirements to support growth is, you know, we've got the land. We've talked about some of our land philosophy in some of the southwest parts of our network. So that's going to be something that we can do a deal like we did with Americold where they can put in the capital. We can give them the land and they can provide an opportunity to grow with them.

And then lastly, it's the cars, right? So you know investing in reefers for example. Investing in other railcar assets that are required for the growth would be the last thing. So I think from all of those pieces, I think we have a strong plan to be able to grow pretty significantly over the next five years.

<Q – Justin Long>: Question, Dave.

<Q – Unidentified Participant>: (inaudible)

<A – Nadeem Velani>: Yes. So when you look at kind of the mix of business, it's -- it can be very different, right? When we look at the CP network, very bulk-centric, very -- we'll run 8,500 foot grain trains. We've been investing in coal, which is long trains and potash as well, which is significant. So that capacity and those sidings aren't necessarily as comparable. But there are some commonalities. We're going to introduce our 8,500-foot grain model into the U.S. grain side on the KCS network. So that's an opportunity over the next two years that we'll be able to work with Bartlett and others to introduce into the KCS network.

Over that three-year period that we had highlighted over the, in our application, we'll get the sidings in place that are required that we think are going to optimize the network. Improve train speed. Improve overall service. Reduce kind of, capital needs elsewhere, in terms of locomotives and rail cars, just support overall asset utilization. So I'd say we're probably, you know, because some of it was done pre-Day One, we're probably at that 40% level as we speak by the end of the year. And so we're kind of on track in that three-year period to be able to have the sidings in place.

<Q – Unidentified Participant>: (inaudible)

<A – Nadeem Velani>: Correct.

<Q – Justin Long>: Go ahead.

<Q – Unidentified Participant>: (inaudible).

<A – Nadeem Velani>: Yes. So it's a great question. So we've seen Canadian ports grow for, for many years, for over a decade, I'd say. Now, near term, we've seen some challenges. I think the port strike certainly didn't help. And the way the government responded to that probably didn't help -- in Canada. I'd say that, we've seen some near-term headwinds with the alliance that suspended their PN3 service in the Port of Vancouver through the end of the year.

When you look at some of the steamship line earnings commentary, it's been pretty abysmal. And so certainly, when you think about the consumer, you think about the macro environment, and hopeful that as inflation subsides and you start seeing rates maybe go the other way, and some strength from the consumer. That's what I think what's going to take for that to recover.

I don't think it's going to happen anytime in the near term. I think we're probably a year away from trying to see that. We're not seeing a peak season today. Certainly by any stretch. That being said, when I think about, you know, when we looked at this combination, part of the benefit was the diversity. So, you know, reducing our reliance on Asian import-export, reducing our reliance on Vancouver, getting exposure to other parts of the network. So, Lazaro has been up 26%. And that's helped us mitigate some of the headwinds that we've seen in Vancouver. So part of that dynamic of diversification, I think we're seeing play out and supportive to CPKC.

<Q – Justin Long>: So there are near-term challenges in intermodal. But earlier, you talked about the intermodal opportunity being underappreciated, and it sounds like that's been one of the upside drivers to your revenue synergies going forward. I wanted to ask about the mix implications of that

because if you go back historically with the rails, there's always been this narrative that intermodal margins and returns are well below everything else. Has that gap closed at all for your business? And as you think about the synergy opportunity going forward, and incremental margins, incremental returns, how much does it matter if it's intermodal versus the other categories?

<A – Nadeem Velani>: Yes. So when you look at, call it the, the CPKC or the CP network, we always looked at intermodal. If you look at our average length of haul, it's closer to 1,600 miles. So, uniquely, in Canada, we have a much longer length of haul, which I think is supportive for margins relative to maybe some of our US peers. And it's no different when you think about what we're doing with the MMX train Chicago and Mexico. It's a longer length of haul than what some of our peers have had. It's a longer length of haul than what KCS has had, right? So that was a lot of traffic that would kind of end at the border and you don't get the full value, and you don't get the full benefit of it. You don't get that density.

So when we look at our intermodal opportunity, it's that longer length of haul that's going to create, you know, take trucks off the road, that's going to create a value proposition to the customer. But you can also price it at not a big discount versus your average book of business. So I don't think that that's going to be margin-dilutive to us growing intermodal.

<Q – Justin Long>: Okay. Maybe we could talk about the balance sheet. I believe your target for leverage is 2.5 times. Any update on when we could hit that target? And as we think about the potential for buybacks being reinstated at some point, is the plan to wait to get to that 2.5 times before we restart that program or could we see something in the interim?

<A – Nadeem Velani>: Sure. So we're going to wait till we get to 2.5 times. Number one, I want to be, you know, when we told the market and told our debt holders, what we're going to do, told the rating agencies, we plan on delivering that, which is to get back to the 2.5 times. There's times when you look at the market and say, well, you know, it'd be nice to have a buyback like today. But that being said, we're going to do the right thing. We're going to, you know, de-lever, we'll get there probably mid-next year. Currency does have an impact, obviously, with the benefits we -- I spoke to on yield from the Canadian dollar depreciating, also has the negative effect on the balance sheet, which hurts our overall leverage.

So 2.5 times kind of, probably mid-2024. And then we'll reassess. We'll certainly, we've been strong proponents of buybacks. It can be supportive. It gives you flexibility. And gives you support at times like this, when you see a bit of a dislocation between your stock price and the intrinsic value. It's a good way of rewarding shareholders and at the same time our dividend, our yield. We've gotten feedback from shareholders and that needs to be looked at. So I think you'll, you can expect -- we'll go to our Board with a recommendation of doing, you know, revisiting introducing a buyback program, and also increasing our dividend.

<Q – Justin Long>: Okay. Great. And you gave a range on CapEx for the next, or, going forward. One thing that came up on the earnings call, though, was I think Keith mentioned, more of a focus on the locomotive strategy going forward, given your growth plans and ESG targets, could -- any color on what that could entail as it relates to both purchases of new locomotives and modernizations? And just trying to balance that comment versus some of the cost opportunities you've discussed.

<A – Nadeem Velani>: Sure. Yes. So you know, as we integrate the two companies, we're getting full value of putting the fleets together, putting locomotive fleets together. And so you know, if we look at our growth profile, and if you look at the age of our locomotive units, we will see the need in a few years to start potentially looking at other modernizations or acquiring tier fours. If the vendors

are willing to come to the table, and we can see some benefits as well on the procurement side, we may have an opportunity to acquire some tier four locomotives that will also help with our emissions targets and fuel efficiency.

We're also looking at, obviously, our hydrogen locomotive strategy. So we're in the midst of building up that program. We announced the deal with CSX to look at conversion kits on diesel-electric locomotives. We've announced the deal with Teck that we'll be testing some hydrogen locomotives on the coal loop in British Columbia. So we're excited about that opportunity in 2024. And we've done some -- we built our first high horsepower locomotive that's going to go out for testing shortly and two low horsepower locomotives that have done some mainline testing and it'd be doing some switching testing later this month.

So a lot happening on the hydrogen side. We think that that's kind of the natural opportunity to de-carbonize and provide a sustainable solution in our industry. It's going to take some time. But that's going to take a bit of time and a bit of CapEx, which I think is going to be well-earned back from our customer base as well. So what does it mean for -- from a CapEx point of view? We guided to $2.6 to $2.8 billion of capital over that five-year period through 2028. I don't think much changes on that guide based on locomotive requirements.

<Q – Justin Long>: Okay. That's helpful. Any final questions from the audience Dave?

<Q – Unidentified Participant>: (inaudible)

<A – Nadeem Velani>: Yes. So certainly when you look at volumes, you know, as an industry, we haven't seen a huge surge in volumes since the 2021 levels at all, so we have room on our network. We have room on the KCS network. And if you think about the benefits and the opportunities of the synergies, as you combine the two entities and running longer, improving train speed and the value of the sidings we talked about earlier as well. We have plenty of capacity. I don't see any sort of capacity challenges from a network point of view.

When you look out on that growth profile that we highlighted over the next five years of mid-single digit RTM growth over that period. So you know, there's your natural kind of pinch points that you can address in different areas of terminals and assets. But as far as overall network capacity, I don't see any challenges.

We also have that second bridge that will come into effect over the next few years as well, which I think will help with overall capacity in north-south. And then when you think about some of the changes in dynamics of what's moving intermodal in the Mexico area, we could create additional capacity by others choosing to go short-haul -- reducing some of that short-haul traffic that's on our network. And that frees up capacity that we could sell at a much better yield and a much better market. So I think these are all positives overall to market, to the value of our service and the value of our capacity.

<Q – Justin Long>: Okay. Well, maybe I'll wrap things up with a final question. One notable trend we've seen in the industry is the Class 1's starting to come together more and collaborate. And I feel like every week I wake up, and there's a new service offering that's hitting my inbox with a press release. Can you just comment broadly on some of the opportunities and maybe the risks as well with some of the new service offerings that have been offered and your collaboration with the other Class 1's?

<A – Nadeem Velani>: Yes. So when we look at what we had mentioned on our integration and why it's supportive for customers and supportive for the economy, we said it was going to be induce and

drive more competition to the industry. And we've seen some of that occur. And so, to us, it's a compliment. And I think it should be a huge compliment to the chairman of the STB, who made that decision and supported this pro-competitive acquisition and deal.

For us, when we look at where our opportunities are, you know, we've announced the MNBR deal which is subject to STB approval. We think that that's going to be a great opportunity to have a direct linkage between the southeastern U.S. and into the, some of the southwest part of our network into Mexico and in Dallas. And so we think that unique offering is great for customers. Great for, kind of, key end markets of autos, which I think CSX has six or eight new auto plants coming online in their network. And we've announced a new auto compound that we're building in Dallas, which I think can be a very favorable landing point for some of those automotive production facilities.

So for us, there's some natural opportunities to work with that MNBR. But we're open for business to work with all the rails. It's something that when you can do things co-productive and can be supportive for customers, and it can be a very cheap and effective way to drive -- improved capacity and promote capacity on the existing rail network. We think that that's a win-win for all. So we will work with each of the key Class 1's where there's opportunities. But that's the key one right now that we're focused on.

<Q – Justin Long>: Okay. Great. Well, we'll wrap it there, Nadeem. Thank you so much for being here.

<A – Nadeem Velani>: All right. Thanks, Justin.

<Q – Justin Long>: Appreciate it.