



Transcript

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Conference

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Webcast

Corporate Participants:

John Brooks – Executive Vice-President & Chief Marketing Officer, Canadian Pacific Kansas City

Other Participants:

Steve Hansen – Managing Director, Raymond James

PRESENTATION

Steve Hansen

Managing Director, Raymond James

Good morning, everyone. Thank you for the time. Pleasure to have you all here with us on the final day. Some of you might have been in the earlier session. But again we're saving the best for last with the Canadian rails. We're really excited to have John here from Canadian Pacific Kansas City.

It's been a remarkable journey for this group over the last couple of years. For those of you have followed the transformative transaction that's gone on. I'm going to let John give us just a few remarks, a state of the nation to get started, and then we'll get into questions right afterwards. Then, of course you can always follow up later with the breakout afterwards. With that, John, thanks for being here.

John Brooks

Executive Vice-President and CMO, Canadian Pacific Kansas City

(Audio interruption) the 20,000 plus CPKC family of employees out there that are battling every day to integrate these two great companies, but also deliver the results that this group certainly expects. You know what, as we sit here today it is a transformative, unique combination. It creates a product in the marketplace, regardless what is attempting to be replicated by our competitors, that can't be replicated. It's a unique, seamless network that connects three countries, period. It's a one-stop-shop.

So we're approaching -- we're getting close to our first year anniversary here as we get towards April. I can tell you, as you look at how we finished 2023 and as I look at 2024, Steve, I was super pleased with how we closed out Q4. We saw a nice inflection in the volumes. I think we had a really good operating environment and we produced the results. Volumes grew at, I think at around a 4% RTM clip to close out the year.

Then we moved into, obviously Q1. We saw a little bit of a weather blip in January. Nothing that we aren't accustomed to in Canada, certainly. We battled through that. I think one week, we were down about 20% RTMs. But it's rebounded nicely. Super pleased with how the operating team has performed. February turned out to be a strong month.

I want to say plus 8%, 9% RTMs with the extra day. And as I sit here today, we talked about a quarter that would be flattish RTMs to slightly down. And actually, I'm seeing flattish to slightly up as more likely an outcome. So, I feel good. It's a story about synergies. It's a story about putting these unique networks together. And frankly, not counting on the macro to do a whole lot for us. If it does, that might be a little bit of a

tailwind.

QUESTION AND ANSWER SECTION

<Q – Steve Hansen>: That's great. So if we take a step back and just think about some of the forces that have been driving this recovery, is it possible to peel back what's been macro-driven thus far versus, again some of your own initiatives and the synergies that are starting to come together, or is -- maybe speak to the category or two that you're finding as being that a bit of upside surprise.

<A – John Brooks>: Yes. Well let me start by saying, I'd say it's definitely a self-help story. It is the synergies that has certainly helped to date in Q4. We really saw a step up and a ramp up of that run rate. I think we closed the year from a synergy standpoint in excess of USD350 million annualized run rate. So a really strong position.

And I look to have that be the story for 2024, Steve. Now, as we sit here today there are some surprises. I would say that our grain business, both US and Canada, continues to be, I would say somewhat what we planned for on the US side. The Canadian side, a little stronger than we anticipated. I do expect that to have a tail – a little bit of a tail to it, but then, be a little bit of a headwind for us yet in 2024 because of the drought condition in the southern part of Canada.

We're a really busy railroad in our western corridor as a whole. So think about that as being not only grain, potash, coal, but actually our international intermodal business has bounced back quite well. I'm certainly trying to get a read from our customers if that's a short-term blip or something maybe unexpected that we're going to see going forward.

I can tell you, we were out in Long Beach meeting with a lot of them this week. It's actually been pretty positive news about what the forward bookings look like in that area. So certainly international has been a little bit of a bright spot.

<Q – Steve Hansen>: That's great. So the visibility on that is still to be determined, I suppose. But managing both the outflow and the inflow is a key part of the focal operation, I imagine, in the short-term?

<A – John Brooks>: Yes, yes, absolutely. There's a lot of constructive tension around how much throughput we can put in that western corridor right now to maximize that opportunity. And, of course continue to capitalize on the opportunities in and out of Mexico and with our synergies related to this transaction.

<Q – Steve Hansen>: And if we think about the domestic side of the intermodal business, you guys have been very progressive in launching your own new service with 180/181. How do you think about that uptake thus far? And how do you see that progressing through the course of the year?

<A – John Brooks>: It's the best service in the industry, Steve. It is truck-like. It is four days, Mexico to Chicago. It can't be beat, can't be replicated. I'll tell you, our border is secure. I'm super pleased. As we looked at the transaction and understanding the amount of money and the effort KCS put into the relationship with Customs Border Control, with the Mexico government, with the state of Texas, it's paying dividends. It is a true differentiator as you think about our product relative to some of the other products in the marketplace. We have a fluid border. So that has been a catalyst to growing those volumes.

I'll just give you a little sound bite. We exited -- our February was up about 23% versus what we exited December in terms of volume on that train. So we've seen a nice step function. The team just

laid out 21 new opportunities that are going to start up over the next 60 days on that train. So our partner, Schneider, is doing a heck of a job. But we've also seen a number of other customers step up, like the product. So as I looked at 2024 as a whole around that product, it's going to be a big year. I think that train fills up.

<Q – Steve Hansen>: That's exciting. I'd love to dig deeper on that one specifically. But I want to make sure we cover the broader portfolio on the ECP side or the energy chem., it was actually another period last year where we went through quite a subdued period, but that's also had quite the recovery. Do you want to maybe speak to some of – how you think about that through the balance of '24?

<A – John Brooks>: Yes. My energy and ECP and merchandise sales and marketing team have been rock stars. It's been an area that, frankly, has maybe uptake some of the other synergy areas that we identified, maybe didn't happen as quickly as we thought, like a Lázaro import/export. It's that single car load, onesie-twosies in that merchandise and ECP space that's overachieved.

We've had some really nice -- we've talked publicly (audio interruption) Shell contract win. The neat thing about that is really, that was towards the end of the year, the ramp up given some of the outages they had at their facilities was quite slow. So we haven't even really seen the full benefit of that significant contract win. We're starting to -- we'll see that ramp up through Q1. But that's not the only part of that story.

We've grown our (audio interruption), as an example, down into the lumber business, down into the Texas market. It's just been a home run for us. That's an area where we're using existing assets, land capacity that KCS had. In the past, not having that line haul up into the markets, really hindered their ability to grow it. They were fully dependent on a UP, a BN, the other carrier to deliver that traffic into that market, where now, they're not. We can control that. We can create the product at the destination to let that flourish. That's what we're seeing in those areas.

<Q – Steve Hansen>: That's great. Now, in the auto space, you've talked a lot about the potential to build this closed loop system or dedicated system for the auto manufacturers. Is that playing out? How have you seen that thus far?

<A – John Brooks>: It's definitely not a field of dreams. That's a reality. And as much as it was our vision in terms of an opportunity to create that tight-knit control with an OEM, just as CP-standalone or KCS-standalone, it couldn't work. What you ultimately need is a network of production facilities and destination compounds that can link those two networks together, and the CPKC.

Honestly, our -- as much as I'm bullish about our intermodal product and some of our other, what we can try, the grain industry, if you think about the auto industry, that's an area where we can link the production in Mexico that's rapidly growing with our production in southern Ontario, and again create that open -- honestly, maybe it took a little bit of a crisis with all the vehicles left on ground and ready to be shipped last year. But we turned that crisis, I think into an opportunity. That's an area where I'll remind this group, when we looked at our synergies in the art of the possible, really now, going on three years ago, (audio interruption) area in that parts business with an area where was long entrenched with some very standardized carriers. We figured it would be very tough to break into.

And what we've found and the synergy that we're very back end loaded in our mind, what has actually happened is we've pulled a lot of that forward. In actuality, the desire for the OEMs to have another choice, to create optionality, to create competition, all the things we thought, we thought it

was going to be later in the journey, it's accelerated. So we're quite pleased. We're going to see a significant step function in this business unit in 2024.

We set a record in 2023. I fully expect us to set a record in 2024. I'm excited about some things and discussions we've got in play for 2025. A lot of the contracts, other contracts begin to roll over in 2026. So I think the auto story has a long tail to it. It should be something that this group should be quite excited about.

<Q – Steve Hansen>: That's fantastic. On the -- if we think about -- I want to come back afterwards, just talk about the capabilities to handle the synergies being pulled forward. But sticking to some of the broader category topics first. (Audio interruption), side, you mentioned grain already being maybe a little less worse or better than expected. But you had a lot of challenges last year in both potash and coal. Not so much on your side, but the customer side. So as you look into this year, do you foresee a more fluid network as it relates to those two key categories?

<A – John Brooks>: Yes. You know what, I was quite bullish in 2023 around that (audio interruption) in our potash business. Things were set up well. I feel what went wrong, went wrong. You know what? The Portland terminal specifically for export potash with Canpotex is back up and running. It's running well. It started up in December. We're actually working with Canpotex to do a -- quite a surge into that terminal. So we're expecting big potash numbers.

As a whole, I think that market, the expectation is some modest growth. Finally in the potash market and certainly, we'll be well-positioned to capture that. Teck is well- positioned, prices are right, they are pressuring us to move as much of that metallurgical coal as we can move today. So again, as much as maybe we see a bit of headwind as you think about Canadian grain as we move forward, you definitely have the potential to offset some of that if in fact the potash and the coal delivers as we expect.

<Q – Steve Hansen>: That's great. So let's go back then now to thinking about the network. As much as a year ago, you were talking about the synergy potential as being, certainly big, if not bigger than expected. But you were also tempering expectations that you would want to bring that on at the risk of jeopardizing any service. So it sounds like you've been able to pull some of that forward. How do you think about the network and its capability to handle the volume flow this year?

<A – John Brooks>: Yes. You know what? I would say unlike maybe all the other rails and certainly if you know my boss, he hits home pretty hard on this. We're not going to oversell our capacity. And as much as I want to capture every synergy out there, if we can't handle it, we failed the customer, we damaged our product and reputation. That does us no good. We've seen that with others too much in the industry. So certainly we're being very calculated on how we bring on this traffic.

It's certainly a very collaborative effort, myself and Mike Foran, and Mark Redd, and John Orr, making sure that we actually can deliver and do what we say we're going to do. That being said, yes, we have pulled ahead. There's been other opportunities that maybe have slipped back. So we're constantly, Steve, calibrating that cadence on how we bring on this traffic.

The good news is, we talked about the intermodal. We launched that train. We still have a lot of capacity in that train. We can add a lot of boxes at a very low incremental cost. We don't need to add crews. We don't need to add train starts. All that will be very accretive to the margin as we move through the year.

The automotive space, a little different area. There's an area where we hadn't planned to buy a bunch more auto racks. So maybe we've redeployed a little bit – pulled capital away from one area

that maybe is a little longer-term project, redeployed that capital certainly worked with the customers to make sure we have the business to underpin those investments. That'll help drive, in that case, that automotive business as we move forward.

<Q – Steve Hansen>: So if I think about your description of the pattern of traffic that you're seeing thus far, we know that the comps will get a little bit easier as we move into summertime, break issues, and a few different events. If I tie it back to the guidance with a low single-digit guide for the year, does it feel conservative at this point to you? How do you feel about the balance of the year?

<A – John Brooks>: I knew that was coming. Look, some of these trends have been so hard to predict over the last 24 (audio interruption). Let's not forget, we got two wars, we got two elections, a Mexican election, a US election. I think we have a consumer out there that's still a little confused. Interest rates still maybe on the higher side. I'm not banking on the macro. That's just simply how we've set this up.

Perhaps, is it conservative? If some of these macro forces continue to play well as we get to the back half of the year, yes, I'd say that's upside opportunity for us. I think about it simply like this: my core focus right now, deliver the synergies. We do that, we'll double our run rate of how we closed 2023. We'll deliver that low single-digits based on that business. We're going to be intensely disciplined on our pricing.

I still think (audio interruption) in some areas that we can get after. There's some legacy-KCS deals out there that have yet to totally roll over or are rolling over now that we're getting a first crack at. But we're taking the opportunity to reprice. I'll remind you, my sellers are paid you know, based on how they deliver price in that. So it matters that they get an extra half point, quarter point and try to make the catch up for the high inflation that we saw. So those are the core areas I'm focused in on. If the macro is a tailwind on top of that, that is upside.

<Q – Steve Hansen>: That'd be great. And just I think it's a good segue into pricing. You've been vocal about your ability to try to go back and reprice some of that book. I think you've described it as process, though. It's not going to happen all at once. So is it a -- it's a two to three reprices every year? How do you think that plays out?

<A – John Brooks>: Kind of, Steve. But a couple of comments on that. One is, as we develop some of these premium products, they, I believe, command a premium price. If we're making investments, we need to make sure we have the payback in those investments. So I would say we've been able to pull ahead in segments of the business on that basis. So that's some upside. I'm quite pleased with how we closed out Q4 from a pricing perspective on the top end of what we would consider good. That's Q4. So we're going to see that tailwind as we move through 2024.

Then I'll remind you, a lot of the KCS agreements were annual, a bigger percentage than what the legacy-CP book might look like. So there were a number of contracts that before we had control, maybe even out to the end of May had already been rolled over and renewed that now we're getting the first crack at.

So we're taking some opportunity to make sure that we're getting those prices. And a combination of all those pieces that I think gives us a little bit of a tailwind there.

<Q – Steve Hansen>: Okay. And just sticking maybe to the Mexico topic briefly, there's been a lot of talk about congestion in Mexico. You send your SWAT team down there to deal with it. There's been good reported progress thus far. I think that shows in, frankly, a lot of the speed and dwell metrics thus far. But if we look at the aggregate improvement in the network that we've seen, is a lot of the

improvement (audio interruption) Mexico solution that you're providing or where are you getting the benefits coming from?

<A – John Brooks>: Yes. So first of all, many of you might know John Orr who led KCS operating team. John is solely focused on that Mexico operation. He's done a tremendous job with Jason Wilkerson down there, leading that team and improving that velocity. Certainly, we had some setbacks. (Audio interruption) half year down there, but we've come out of strong. I can tell you, there's been a number of days we've set the all-time (audio interruption - GTM) single day record ever moved in and out of Mexico. So we're quite pleased with that.

And frankly, we have to do it. The volume growth opportunity down there is quite exciting. I can tell you, there's a lot of, though, what I would say typical PSR principles that we're still working on down there. How do we lengthen out trains? How do we put in the first mile, last mile?

We're working tightly with John and the team, the Mexico team down there right now and doing that white boarding. Keith and Hunter always talked about white boarding with the customers to really understand what their volumes and needs are. That was a big part of our transformation at CP in the day. We're taking that same principle down to Mexico.

We are working with customers, understanding their facilities and squeezing out every bit of efficiency that we can get. But with that comes additional volume and opportunity. So we're working hard with the steel guys down there. We've done a fair amount of work with the grain customers down there. We'll systematically move customer by customer, region by region down there to continue to drive efficiency into that Mexico product.

<Q – Steve Hansen>: That's great. There's been a lot of talk about the election. You referenced it earlier. I know there's been talk about passenger rail, these things. I think Keith had suggested on the most recent call that he really doesn't see that as an impediment irrespective of how the election plays out or the studies that you're conducting play out. I mean how -- what gives you the confidence that you can manage that process from here forward?

<A – John Brooks>: Yes. I'd simply leave it at this: whether it's the new leadership or AMLO and his team, they have been unwavering around their desire to have a world class freight railroad system in Mexico. Now, complimentary, where passenger makes sense, we'll see. It's going to be a long process. We're into it with them. Again, the KCS legacy team did a tremendous job with those relationships, were built (audio interruption). We'll take those step function movements with the administration and the new administration going forward to what that looks like.

But rest assured, whatever we do, we're aligned that if Mexico is going to produce and do the things, ultimately, I believe the government wants it to do in terms of being a leader in production and industry in North America, we need a strong freight rail system to support that.

<Q – Steve Hansen>: No, that's fair. I just want to think back to the resourcing side for a minute because referencing the volume opportunity that seems to be coming down the pipe. I think last year, you intentionally held on to some additional resources, protect the service and then traffic really suffered, of course. Now that we're getting into this recovery mode, how do you feel about your resourcing today from a labor standpoint or inbound?

<A – John Brooks>: Yes. You know what, I think not -- there's not hot spots here and there, Steve. And certainly, (audio interruption) we're quite busy in our western corridor. But because of some of the actions we took last year, I think it sets us up as some of these businesses rebound in 2024 to be able to, again, add the business at a very low incremental cost with not a lot of locomotives or

headcount. Now, certainly if this thing -- I was laughing earlier, we're moving 25% more international and the industry wants us to move 45% more.

If we see that trend continue across a number of lines of businesses, obviously we'll have to react in -- whether it add crews or power in certain areas, we'll do that. Right now, we think we're setup in pretty good position, though.

<Q – Steve Hansen>: That's great. Then just as we think about the one last piece I didn't get to touch on earlier, I want to circle back to, but you talk about this refrigerated market opportunity. It's been one you've got some good partners with. Maybe just speak to what that has started to show from a network standpoint. I know it ties back into your broader synergy targets. But how do you feel about that opportunity specifically? And where do you see it evolving?

<A – John Brooks>: Honestly, it's a -- it's not a secret, but it's the best kept (audio interruption). I see it as a \$500 million plus opportunity into the future. We are creating a complete ecosystem when it comes to food certainty, food security, cold storage, temperature-controlled. Obviously, we've partnered publicly with Americold. We're (audio interruption) the 300,000 plus square foot facility that they're going to be building in our ramp in Kansas City, direct access to our intermodal terminal.

A neat thing about that, we've been working with Customs and Border control. We're actually going to have Mexico customs physically located in the facility to be able to pre-clear to make, again our border completely seamless for this product moving southbound into Mexico. But it -- honestly, it is the -- just the first -- we just inked a deal to build a similar-type facility in the Toronto market. I've got good line of sight to another one in eastern Canada. And as Americold has said, I think they fully expect to expand their footprint down into Mexico.

So I can see, this is -- I think and I tell my team is these industrial development (audio interruption) are this gift that keeps on giving. We create a product, we sell it, we partner with the right partners in the marketplace. You create this infrastructure and it makes it real sticky. It makes it real sticky long-term. So these are opportunities that as you start to think about your investments (audio interruption) that these aren't next year, these are start to develop and really see the benefits of it as you get out into '25 and '26, and '27, and beyond.

<Q – Steve Hansen>: That's great. I think Keith said it really well a few times in the past, you're 100 hundred days into a forever story. You're approaching the one year mark into this forever story. It's really going to be exciting to watch you guys continue to grow here for the next couple of years. We're running out of time, so we're going to cut it off there. But just really appreciate the time. Looking forward to watching you guys grow, manage the growth. It's going to be a great time forward.

<A – John Brooks>: All right. Thank you.

<Q – Steve Hansen>: Appreciate it, John.