Transcript

Q1 2021 Earnings Call

April 21, 2021

Corporate Participants:

Keith Creel – President & Chief Executive Officer
John Brooks – EVP & Chief Marketing Officer
Nadeem Velani – EVP & Chief Financial Officer
Chris de Bruyn – Managing Director, Investor Relations & Treasury

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon. My name is Christine, and I'll be your conference operator today. At this time, I would like to welcome everyone to Canadian Pacific's First Quarter 2021 Conference Call. The slides accompanying today's call are available at www.cpr.ca. All lines have been placed on mute to prevent any background noise. After the speakers' remarks, there'll be a question-and-answer session. [Operator Instructions] I would now like to introduce Chris De Bruyn, Managing Director, Investor Relations and Treasury, to begin the conference.

Chris de Bruyn

Thank you, Christine. Good afternoon, everyone, and thank you for joining us today. Before we begin, I want to remind you, this presentation contains forward-looking information. Actual results may differ materially. The risks, uncertainties, and other factors that could influence actual results are described on slide 2, in the press release, and in the MD&A filed with Canadian and US regulators. This presentation also contains non-GAAP measures, outlined on slide 3.

With me here today is Keith Creel, our President and Chief Executive Officer; Nadeem Velani, our Executive Vice President and Chief Financial Officer; and John Brooks, our Executive Vice President and Chief Marketing Officer. The formal remarks will be followed by Q&A. In the interest of time, we would appreciate if you limit your questions to one.

It is now my pleasure to introduce our President and CEO, Mr. Keith Creel.

Keith Creel

Thank you, Chris. Good afternoon. Appreciate everyone joining us today. Certainly, we've got some exciting things to talk about. I would suggest – the results are very compelling. I look forward to getting to those and sharing those great results, and thanking our 12,000 strong family of railroaders that enabled them.

But before we get to the actual results, I think it's appropriate that we address perhaps the M&A buzz that's in the air. And I'm going to take it from an approach where I'm going to focus on the truth, because the truth matters. I think the truth will indicate that yesterday we all woke up to witness CN's unsolicited alleged superior offer to the KCS board into the market in comparison, to our partnership agreement with the KCS that we announced a month ago, and I'm sure the truth is you're all sitting there thinking, well, where does CP stand? What do we think? How we'll react? Perhaps, were we surprised? And I think the best and only way to address those points and, frankly, anything tied to what is truly the only unique and unparalleled strategic value opportunity combination is with the truth. The undeniable facts, I think that's perhaps the best way to do that.

So, let's start with, were we surprised? The answer is no. Obviously, perhaps I've got a bit of unique industry experience in my history, uniquely around both companies as a CEO obviously of this company, as an Operating Officer of this company, as the Senior Operating Officer of the competitor, the alternative, both with experience on the CN network, and actually I think perhaps people realize by now, if it's not my vernacular that gives it away, then my resume does, I started my career with the Canadian National and Illinois Central in Memphis, Tennessee, and worked in Jackson, Mississippi where I – as I shared with our KCS partners last week in Kansas City, my first experience 25 years ago working with the KCS started competing against and partnering with at the same time in Jackson, interchanging with, and actually the truth is that my Senior Operating Chief here, Mark Redd, actually started his career on the KCS, spent 20 years there. And that's where, if I go back to my IC days, I developed the respect for Mark as an operator.

So, that's true. Beyond that though, if you think about the unique value that this combination, this partnership, this very unique partnership represents, there are undeniable truths, and I think I'm just going to go through them.

So, truth number one, based on the merits, the facts of our proposed combination and partnership with the KCS, our combination, CP-KCS is the only true USMCA network and opportunity. It's the only possible Class 1 combination that answers the STB's public interest test. The only, not one of many, the only. Why do we say that? Why is that true? Why is that undeniable?

Well number one, let's start with truth number two. It's pro competitive. Multiple fronts, new routes, new markets, new competition introduced. Customers get reach today with this combination, when approved, and we believe it will be, that quite frankly, with that it, is impossible. New competition is introduced, be it with BNSF, be it with UP, be it with CN. That simply doesn't exist today that's enabled by this combination.

Truth number three, pro service. The service that this creates where service doesn't exist for many of those customers. The opportunity perhaps to invest in a grain elevator. 200 miles north of Kansas City, in the heart of Iowa territory where our line runs. The KCS shipper today that perhaps have always wanted to have a better origin market, but the investment wouldn't support it. The economics didn't work. On a single-line railroad, that changes the entire conversation. In fact, I know that's true because the truth is last week in Kansas City, when I had the opportunity to meet and share vision with and discuss and listen to concerns of several KCS customers, that happened to a topic. And the truth is, that's not the first time we discussed it. So, pro service.

And then truth number four that's undeniable, the resounding, overwhelming support of our customers. 400-plus, 408, 409, the number continues to change. In fact, we welcome Bartlett which, the truth is, is KCS' largest customer that supports the opportunity this deal uniquely unlocks, just yesterday that we filed with the STB. So, to deny that 400 voices-plus have spoken and continued to speak is denying the truth in support of this value creating transaction.

Truth number five, there are no true losers. Zero, that's a pretty undeniable number. It's a very unique number. And again, the truth of this proposed transaction it is the only combination that results in zero instances of any customer that enjoys a level of service today, optionality from different carriers, to truly lose zero, only gain.

Truth number six, in support of truth number five, not one customer with less option.

Truth number seven, this uniquely enables quality growth. And when I say quality, quality matters. That's a keyword. You've got two railroads that the last three years have led the industry, producing sustainable, profitable, quality growth; not growth for growth's sake, growth that matters, growth that comes to the bottom line, that drives earnings performance, that drives value creation. And the truth is, these two railroads have led the industry the last three years in total shareholder return. It's undeniable. The truth speaks for itself.

Truth number eight, this investment uniquely unlocks and enables additional investment to create capacity on these lines, key lines of needed capacity, especially in light of what's happening in North America today in key routes from Mexico to Chicago, on existing infrastructure that we uniquely own being CP and KCS that, quite frankly, standalone would never be possible.

Truth number nine, it benefits the environment. True realistic opportunity to take trucks off the road and put them to rail. And another undeniable truth, if you think about some of the communities that that matters in, I think about Chicago. And you know why I think about Chicago? Because the truth is, I'm a Chicagoan and I live in Chicago. I understand the congestion on the highways in Chicago. I've lived it. I understand the congestion in the rail network and how exposed we are at times. I have lived through it. So, to suggest that bringing more traffic into Chicago is beneficial, I think it's untrue. To suggest that taking traffic out, to suggest that taking trucks off the road that otherwise would be populated on Highway

294 or on Highway 80 or on Highway 90 or on Highway 94, to take them off the road and put them on the rail, that's a huge opportunity, not only for local congestion and less greenhouse gas emissions in the Chicago metropolis area, but for the entire route from Mexico, from Monterrey, Mexico City that 2,800 miles we talked about yesterday I heard so much about, to truly realize that opportunity is undeniable.

Number 10, the truth that it unlocks unique actually attainable value for the shareholders. This deal is approvable, it's doable, and in order to realize the value, you got to get the deal done. There's over USD 800 million of conservative synergies that we've spoken to, that this deal represents for our shareholders to benefit from; for our employees, both KCS as well as CP's, job creation to benefit from; for the environment truly to benefit from. Value across all areas.

Truth number 11, all those reasons stated, 1 through 10, leads to one undeniable truth and that's called deal certainty. This deal represents a path to true realized value. Compelling value now and the value it represents, and even more compelling value long-term, long-term sustainable value that is only uniquely created by this combination. Those are undeniable truths.

Now, keeping with that thought, let's now take a look at the CN-KCS proposal. Let's talk about what's undeniable truth. So, were my eyes opened yesterday when I read the press release? The truth is, yes. The headline value number was undeniably eye opening. $325, but the reality is, that only matters if it's attainable. Unrealized value is still equal to zero. If you can't do the deal, if it's not doable, you never get there. The facts matter.

Truth number two, why I feel so strong about number one? This deal's anti-competitive. When you look at it, the facts and not just the spin or perhaps the small, I think, disingenuous comments yesterday, that this really boils down to 65 miles in Louisiana. Come on – come on man, that's not the truth. It's anti-competitive. How many customers, multiple customers, are losing service options? How many customers today that just CP, CN alone enjoy an opportunity to choose between the two of us, and partnership with KCS lose that option? How many 2- to-1 scenarios? How many losses of routes 4-to-3? The undeniable truth, if I'm in Superior, Wisconsin today, and I happen to know who is in Superior, Wisconsin today, it would be CN, UP, BN. And guess who? CP. Well, guess how CP gets to the southeast out of Superior, Wisconsin? CP partners with KCS over Kansas City. The truth is our deal represents a single-line move with the CP-KC combination. The truth is also that in the absence of that, you eliminate an option in Superior, Wisconsin, and that's just one of many, and somehow that truth didn't come out yesterday.

Truth number three, its anti-service. How many customers are left with no service or less service options? The truth is, once it's analyzed, those numbers will be revealed because certainly they weren't spoken to yesterday, but the truth will be revealed because the truth matters.

Number four truth, already an overwhelming outcry of opposition from customers. And here's some undeniable truth. The reality is this proposed transaction, CN-KCS, is already picking winners and losers. The truth is, if you're in the ag industry and you happen to be located in North Dakota, South Dakota, Minnesota, Iowa, and the grain belt of America, Middle America, this deal represents a lost opportunity. This deal strands our product. This deal says you never enjoy single-line service that the CP-KCS provides or creates in the history again. This is, if you're an ADM or a CHS, and those are our customers at CP, the truth is they hurt, the truth is they're penalized.

Let's talk about the automotive industry. The truth is, if you're Ford or GM, you're a current CP-KCS OEM that enjoys business coming out of Mexico, moving to all Canadian markets over Kansas City through that partnership; in the absence of that partnership, what are your options? The truth is, and if I were at Ford, I would be concerned. Conversely, General Motors. The truth is CN has four plants in the US, two in Canada. And in this instance, if CN were to combine with the KCS, they'd have three uniquely single-line served GM plants in Mexico. The truth is that creates imbalance. CN would serve nearly half of their North American plants. If I were General Motors, I think I'd be concerned.

Let's talk about ECP, energy, chemicals and plastics. Truth is, think about the propane customers. CN will have virtually a monopoly on the propane market. They'd have control of complete markets, access for

LPG, CN Rupert export, US and Canada destinations in Mexico.

If you're Exxon, and that's a customer we care about at Canadian Pacific, and you happen to be located in Edmonton, because they are, and you're also on the refinery in Baton Rouge that today is uniquely served and provided access by CP-KCS combination over Kansas City, or the alternative would be a CN direct line to Baton Rouge, that goes away, that's the truth.

Forest products. There's some more painful truth there too. If you're a customer single-line served by CN in Canada, you understand they've already got control of 90% of the Canadian production. In this model, they're suggesting the truth is they can direct forest product flows based on broad control boards in destination markets across Canada and US. They could pick and choose. The truth is, I don't know a customer that would enjoy that or choose that.

Now, let's go to intermodal. That's where the real value creation is in the story. That truth is there's only four north-south options today; UP, BN, CN, and KCS. This deal suggests there would be three with the CN-KCS merger, UP, BN, CN-KCS, as the CN absorbs the KCS option, pretty undeniable truth. If you're Maersk, again that's a partner that we care about CP especially, so with our new partnership, and the long-term commitment they've made to us and the long-term commitment we made to them, and the unique investments we've made with them, and the unique investments they've made with us, we care about their long-term health. Because CN will control access to the ports in Mobile, their terminal; Lázaro Cárdenas, which would be their terminal. I think it's undeniable that would create a lot of leverage in that relationship that if I were Maersk, the truth is, I'd probably wouldn't be happy about.

Truth number five. I think it's important we keep talking about the truths. To suggest overlap is isolated; again, to my point earlier, to 65 miles in Louisiana, it's not true. I guess that suggests, if you believe it to be true, that the overlapping connection in Springfield, Illinois doesn't exist. The customers that are served by KCS or served by Canadian National, in Omaha or Council Bluffs that would go to one, I guess that doesn't exist. Same concerns in St. Louis to the points I made about Superior, Wisconsin. Mobile, Alabama, Jackson, Mississippi, of many, perhaps to some that don't understand, that's not material, but I would suggest that every one of those locations with every one of those customers, the truth is they care.

Truth number six, and I think this to be true. They either don't know how much damage this proposed combination could create, or worse yet they do and they prefer not to share the truth.

Truth number seven, I don't think they really know what growth this may or may not create. They obviously haven't done their homework, or understand the markets, or worse yet they have and they do and they prefer not to speak to the adverse impacts and the lack of growth, the lack of stifled competition that this represent back to my earlier truths when I'm thinking about the Ag shipper or the chemical shipper or the lumber shripper that get stranded because of this proposal, that uniquely would be benefited compared to ours.

Truth number eight, I think about investment. To realize these growth potentials that they spoke to, it takes some investment. And to think about the truth is they're prepared to go to a 4.6 times balance sheet, locking up their capital, and the money they would need to invest in this proposed combination to unlock this growth is undeniable.

Truth number nine, the benefits to the environment. I heard that spoken too a lot yesterday. I think pretty aspirational, road to rail conversion. I think we understand the market better than they have because we've done our diligence, we've been at this for quite some time, in partnership with our partners, the KCS, developing these opportunities. John will get to the facts, the truth of our synergies. Conservative, yes, but realistic, absolutely at the same time yes. And to think about the number I heard yesterday, 75% of the synergies, of these CAD 1 billion synergies is out in intermodal. If you look at the facts, suggests that this intermodal is coming off the road, going into the rails, coming out of Mexico, Monterrey, Mexico City, it's going to Chicago, it's going to the Detroit, it's going to Toronto.

Again, if I go back to our truth about our deal, let's just speak about Chicago, the truth is their terminal is

located on the south side of Chicago and perhaps a smaller terminal in Joliet. If the traffic is going there, to get to its markets, which are currently all over the greater Chicago area, it's a very large population center, the truth is it's going to be on the highway. The truth is it's still going to congest the streets of Chicago. It's still going to create greenhouse gas emissions in Chicago. And again sticking to the Chicago truth, if I think about the western part of their network and I think about all those other truths, with the way they would direct traffic CN's only route to access the new network they proposed via Kansas City or their existing network is through Chicago.

And you know what, it is true that it would go over the EJ&E. The truth is probably the folks that live in Barrington, the same folks that were concerned about the deal when it was created, the same environmental impact, the adverse environmental impacts that CN has had to mitigate, I know to be true because I understand those, I was there when that was created. It's those same communities, it's Barrington, it's Aurora, it's Naperville. It's Joliet. Those are truths. And I would suggest that their truth in their reality would beg to differ with perhaps the version that CN has put forward.

Truth number 10, is the value really attainable? To me if value is unattainable, it's not true value. And I think you got to think, is it attainable? Even if we're in denial, I think this is a fact, I think nobody would discount this or disagree, I heard yesterday a mention of pioneers, PSR pioneers, well the last I looked, the truth is they don't work there anymore. They are not there. They're running other railroads. That talent is all over this industry. It's not the pioneers at least still working at Canadian National.

So then I think about the current company, they say they can, but can they? And the truth is I have to go back – the only thing I can look at – and that's fact. And the facts show, and I think I spoke to it earlier, the track record, that's all I can gauge it by, that's the truth, 10 years of underperformance in our industry. 10 years of underperformance, not 1, 10, a decade. And if I go back in history because I was there then 10 years ago, that team, those pioneers led the industry, they didn't trail the industry, it's a different team, it's a different game. So to assume the same future performance because we did it in the past, we could do it in the future, the truth is that as an investor that's a pretty risky proposition.

That leads me to the truth 11. Absolute truth that's undeniable is deal uncertainty for all 1 through 10 which means to me the headline value could be 500% more than our real attainable value, it's fantasy money. It's fool's gold.

And then my last truth, I know the team at the KCS. I've got a deep respect, I've had time to work with those future partners, like-minded company, proud company, smart railroaders, engaged board of directors, they're no fools. STB, I feel the same way. They're experts in this space. They understand what pro competition means. They understand what pro service means, and to suggest that they'd be foolish enough to believe what was said yesterday, as fact points that represent that proposed deal is just simply not true.

And then finally the investors, that's you. At the end of the day, you're the ones that had to make the decisions. Ultimately, and again I think, truth matters. I think if you're an investor and you look at what story do you believe, what represents truth, I think the train that you want to join, the train you want to get aboard is the one that's most probable based on not what they say but by what they've done. Our story at CP, it's a story of doing what we said we're going to do. It's a story of turning this company around, taking this proud talented group of railroaders and creating a unique value in this industry. That's a 10 times multiple over the last decade compared to that story. And again, the truth is you'll have to decide where to put your value. So that's my story of the truths. I think the conclusions are pretty obvious and we'll save discussion about that for the Q&A.

So now let me get to the other real truth, and that's exciting results that we're about to talk about, and I want to thank our team of railroaders. Again I say this over and over again, it's because I mean it. We couldn't do this without these railroaders. These railroaders are a family of railroaders, that's all of us. That's not just management, that's not just leaders, that's our partners, that's our family, enable these results. It's our collective efforts that enable it. That's never going to change. They are extremely proud of this company about this historic transformation, they're excited, they recognize what this represents

whether it's the man or woman on the ground or whether it's the union leader we've been engaging, the partners in our business are excited about this opportunity and they're excited about these results. So to these results, again I think the truth is it's pretty unique in this industry.

First quarter revenue is CAD 2 billion and adjusted operating ratio of 58.5% and adjusted EPS of 1%. It's pretty impressive. It's a strong performance enabled by strong operating performance. Mark and his team have done a phenomenal job. If you look into the details, the truth says records for weights again and lengths again even in spite of the polar vortex that we went through in February, optimizing our assets, our operation finding new levels of efficiency – essentially creating new levels. That's what a true culture of PSR enables. It's an outcome, it's not an aspirational goal. So again, they've done a phenomenal job.

I'm going to stop at that point and turn it over to John to bring some color on the markets and then Nadeem will wrap us up with the color on the numbers and we look forward to having a truthful, frankful discussion after. Over to you, John.

John Brooks

All right. Thanks, Keith, and good afternoon, everyone. So let me start by saying I was very pleased with how the quarter played out. Aside from the challenging winter weather conditions in February that Keith spoke to, January came in significantly above our high expectations and March was an all-time record month for us.

The demand environment across most of our business lines continued to strengthen, and I'm frankly super excited and more excited than I was coming out of Q4 on what this year is going to shape up to be. So, looking specifically at Q1, RTMs are slightly positive in the quarter, total revenues were down 4%. Fuel on FX combined for about a 4% headwind and the pricing environment continues to strengthen for us. I'll take a look at our revenue performance here now by commodity and speak to the results on a currency adjusted basis.

So starting with grain, volumes were up 19% on the quarter with revenues up 10%. So every month this quarter in Q1 was a record in Canadian grain for us marking it as six straight record quarters. I'm incredibly proud of our operating team across the entire network and our partners in the grain supply chain that helped us execute and deliver this exceptional performance.

I'm also pleased to provide an update on the Volume-Related Composite Price Index or the VRCPI. This is the index set by the Canadian Transportation Agency in which we had appealed the methodology changes that had taken place for 2020-2021 crop year. And we were successful in the appeal and the CTA is reevaluating their cost of capital assessment on the VRCPI. We expect that change for the current crop year to now come in at about a negative 2% to 3% compared to the original assessment of around negative 7%.

On the US grain front, another great story. Our strong origination franchise continues to see robust demand. Again, the operating team here working closely with our customers to deliver the US grain to market. Our RTMs are up over 35% year-over-year. Demand to the PNW for export remains steady and some of the strongest we've seen in years. Now looking forward, despite some declining stocks in areas across Canada and dry conditions in some regions, I continue to expect grain on both sides of the border to continue to deliver steady volumes as we move through quarter two.

On the potash front, volumes were down 9% on the quarter. The decrease in volume reflects the impact to export volumes as a result of some track expansion work that's been ongoing at Canpotex's Portland facility. I can tell you this work is now completed. We're working closely with Canpotex as this will drive increased capacity and new efficiency through this terminal outlet. Although April here is off to a little bit of a slow start, the demand for potash remains extremely strong and I still see an opportunity to deliver record tonnages in potash for Q2.

And to close out the bulk business, coal revenues were up 9% while volumes were up 19% as the supply chain executed very well and we lapped port maintenance issues that had occurred in Q1 2020.

On the merchandise front, turning to energy, chemicals and plastics portfolio where we saw revenues and volume decline about 19%. Excluding crude, ECP volumes were up 6% in the quarter driven by improving export and domestic demand for LPGs. We expect to see continued strength in ECP excluding crude as recovery from the pandemic continues in this area and demand returns to more normalized levels. As areminder, Q1 was the last quarter with tough crude by rail comps. In 2021 [2020] we moved 36,000 carloads of crude and in Q2 2020 we moved about 7,800. I expect crude volumes to continue at a similar pace into Q2 as we saw in Q1 and then to gradually improve as we move into the back half of the year.

Forest products volumes were up 7% and revenues were up 8%, a record Q1 for both metrics as we continue to see strong lumber prices and significant demand for pulp and paper products. We have recently added about 125 center beams to our fleet which will continue to drive positive trends as we move through 2021.

In MMC, revenues declined 12% and volumes declined 10% largely as a result of lower frac sand volumes driven by the reduced drilling. Excluding frac sand, volumes in MMC were positive.

On the automotive front, revenues were up an impressive 32% in the quarter while volumes were up 56%. Again this auto area is an excellent demonstration of the power of the unique customer solutions we've been able to create for the OEMs. While manufacturers have most recently been challenged by the chip shortage, we focused with our OEMs and those vehicles with high demand which are manufactured on our lines. We expect some continued impact of production in railroading volumes over the next few weeks, however, current customer forecast show improvements as we move through May. I continue to expect to grow auto revenues at a strong double-digit pace, and I see opportunity in the future for further utilizing our land holdings to grow in this piece.

So finally in the intermodal side, quarterly volumes were down 9%. On the domestic intermodal front, we had a record first quarter. March was an all-time record month. And despite COVID-related restrictions tightening across Canada, we see consumer demand continuing to be strong. We are pleased to announce a new long-term contract with Loblaw that'll expand our relationship with Canada's leading food and pharmacy provider.

We're ramping up our domestic and international service into Atlantic Canada and look forward to this highly competitive service offering being a strong growth engine for us for years to come. So while the international franchise did face some challenges with port congestion and container shortages and ONE comps, we expect this to improve as we continue to accelerate volumes with Maersk, we lap the ONE contract, the Port of Saint John calls continue to ramp up, and our exclusive Vancouver transload comes online here in Q3.

So let me close by saying, looking forward, I see strong opportunity across all of our lines of business and I remain very confident in the underlying demand environment. My sales and marketing team remains laser focused on executing those specific marketing playbooks and delivering our pipeline of opportunities that build unique customer solutions that optimize our land assets, and as Keith said, continue to generate that sustainable profitable growth. So with that, I'll turn it over to Nadeem for the financials.

Nadeem Velani

Thanks, John, and good afternoon. I'm proud to present our Q1 results which highlighted record Q1 operating ratio for CP of 58.5%. Our exceptional team of railroaders once again proved their resiliency in the strength of the model by navigating the challenging conditions in February and then producing an all-time record month in March. Despite plenty of opportunity to make excuses given weather, rising fuel prices, higher stock, comp accruals, and the negative impact of a stronger Canadian dollar, the team delivered these record results which is a testament to CP's execution abilities no matter what the environment. You'll note that we have adjusted a total of CAD 36 million in transaction costs related to our pending KCS transaction, CAD 33 million for purchase services and other and CAD 3 million below the line in other expense. I'll speak to the adjusted results today.

Overall, the adjusted operating ratio decreased 70 basis points to 58.5% driven by strong operating efficiencies including record train lengths and train weights and the recognition of the gain from the agreement with the tollway in Chicago.

Taking a closer look at a few items on the expense side, comp and benefits expense was up 2% or CAD 7 million versus last year. The primary driver of the increase was higher stock-based compensation of CAD 13 million driven by a higher share price in the quarter.

Fuel expense decreased CAD 6 million or 3% primarily as a result of lower foreign exchange, partially offset by higher prices. This quarter we achieved a record Q1 fuel efficiency as we continue to improve our operating performance and modernize our locomotives. The change in fuel prices was a CAD 37 million negative impact to operating income in the quarter.

Equipment rents was down CAD 3 million or 8% as a result of efficiency improvements year-over-year more than offsetting increases in rents expense from automotive contract wins. Depreciation expense was CAD 202 million, an increase of 5% as a result of a higher asset base. Finally, purchased services were CAD 241 million, a decrease of CAD 71 million or 23%. Again, the main driver to decrease is the gain related to closing the tollway transaction.

Moving below the line, as expected, other components of net periodic benefit recovery was up CAD 10 million, reflecting lower interest costs related to a decrease in discount rates. Income tax expense decreased CAD 6 million or 3% primarily as a result of lower effective tax rate. Rounding out the income statement, adjusted EPS grew 1% to CAD 4.48 in the quarter.

On the next slide, moving to free cash, we generated strong cash flow in Q1 with cash from ops increasing by 19% or CAD 93 million. We continue to reinvest in the railroad and are on track to meet our CAD 1.55 billion guided CapEx spend for 2021. Given the strong volume outlook in 2021, we'll benefit from our decision last year to pull forward capital when we saw softer demand resulting from the pandemic. That decision and the solid execution by our operating team and the engineering team allowed us to take advantage of the increased available track time. The efficient capital work in 2020 has the network in fantastic shape to capture the robust volume outlook John highlighted and won't need incremental capital spend.

Our proposed 5:1 share split was approved by shareholders at the AGM this morning. We're taking steps to implement the stock split and expect to complete in May. The share split will encourage greater liquidity for CP's common shares and provide enhanced opportunities for ownership by a wider group of investors.

Our balance sheet liquidity remains very strong with leverage of 2.4 times adjusted net debt to adjusted EBITDA. We continue to pay down short-term commercial paper with excess cash as our share buyback program remains paused and we are committed to our target leverage range and strong investment grade credit ratings. We finished the quarter extremely strong and it brought a lot of momentum into Q2. The demand environment is set up well, led by our self-help story. I feel convicted in our ability to fully realize guidance we set out in January and reiterated today. With that, I'll turn it over back to Keith to wrap things up before we get into Q&A.

Keith Creel

I think maybe I'll close with where I started. The results sort of speak for themselves they are undeniable, I think overall given the challenges that we faced to the compares that we faced, I remind the market last year in 2020 a very new story. We had – memory says 9% growth year-over-year. And against the toughest compares in a very tough environment, especially the same that all of our peers in the industry face for this result to be enabled by this team, I am extremely proud of it. With that I think we've said enough and let's open it up for some truthful discussion.

Question & Answer

Operator

Thank you. [Operator Instructions] Your first question comes from the line of Fadi Chamoun from BMO. Please go ahead.

<Q – Fadi Chamoun>: Okay. Thank you. I appreciate the time and taking the time to explain through this, Keith. So quick question maybe on the synergies now that you've had kind of multiple weeks here to talk to customers, maybe understated on the ground a little bit more what this means. How do you feel about the synergy outlook, do you feel that there is a kind of significant upside to what your initial expectations were?

<A – Keith Creel>: Absolutely understated. Big opportunity for these two teams together to create – overachieve well-beyond what we assumed in our deal

<Q – Fadi Chamoun>: Okay. And maybe just a quick follow-up on that, like ultimately it feels like this may come down to who wins the hearts and minds of customers at the end of the day to sway maybe in the STB mind which way they should go. Is that how we're going to see this playing out?

<A – Keith Creel>: Well, Fadi, I think that's obviously – it's critically important. I'm not going to say it's not because if the customers are against you, the customer is who we serve, the STB is going to listen to that, which is why I feel so good about our deal. The customers overwhelmingly for us. But when it gets down to truly comparing the deals, if you're – and I try to put myself and I've tried to along this whole process put myself in Pat's seat, put myself in the KCS Board of Directors' seat, it comes to doability, it comes down to can you get the deal done, it comes down to risk that you have to embrace to realize the value for your shareholders.

And the truth is that the trust, the voting trust is the trigger here. The new rules mean that CN has no choice but to have its voting trust approved by the STB and their proposal under the new public interest test. Unlike CP, CN can't pass the test because ultimate regulatory approval of this deal is so complex and uncertain, that's undeniable.

The STB will not want KCS to go into trust with so much uncertainty about whether it comes out as part of CN or not. And I believe the truth is nor would their board or their shareholders. That's what it comes down to, can the deal be done, can that I would be realized and there is only one answer that truly meets that test, not two, just one.

<Q – Fadi Chamoun>: Thank you.

<Operator >: Your next question comes from the line of Ken Hoexter from Bank of America. Please go ahead.

<Q – Ken Hoexter>: Hey, great. Good afternoon, Keith. If we could just focus on your performance, maybe just talk about your outlook now on volumes given the improved economy or maybe it's for John I guess you had talked about upper-single-digit carload and RTM growth. What's changed? Are you seeing more acceleration to that given the exit in March? Maybe just talk about updated performance. And, Nadeem, I don't know if you want to throw in maybe a margin outlook thought on that as well. Thanks.

<A – John Brooks>: Hey, Ken, so it's John. I'll take that and let the others jump in here. Yeah, extremely convicted high single-digits. That's the path there. It's still directly where we're marching. I was super pleased with how January got launched. Of course, February was a little bit of a struggle

but I expect to see us perform well. We're off to a good start here in April. I expect Q2 to be strong, Q3 double-digits, and then as move out to close out the year, remain convicted.

The environment, just about across all lines of business, continues to be strong and recovering. We're watching obviously a little bit of blip with this chip shortage but again have spoken to all of the auto industry over the last couple of weeks around the opportunities certainly with the KCS merger and certainly talked about this chip situation. And I think for the most part, most of the OEMs see some recovery in that. So I'm optimistic in that but the grain front continues to be strong for us. We're starting to see maybe a little bit of dwindling of stocks in certain areas across Canada but nothing that I see we would really impact us here in Q2 so I remain optimistic there.

As I said, the potash opportunity, Ken, is tremendous in Q2. There has been a lot of pent-up demand in that space and actually the Canpotex forecast versus what we moved in Q1 are up about 70%. So there's a lot of opportunity on that front. And you know what, we're only going to gain momentum on the intermodal side of the business. Maersk business is ramping up. Hapag-Lloyd is – expect to see a press release here in the coming weeks around their first port of call into Saint John. As I spoke about our domestic intermodal business is really starting to ramp up in that marketplace too. So all that to say, still a lot of conviction and excitement on what 2021 holds.

<A – Nadeem Velani>: Ken, just on the margin side, I mean, we're extremely convicted. We talked about in January getting to a mid-50s type of operating ratio and we're still on pace for that despite the polar vortex in a tough February, and obviously fuel prices have been challenges for the industry in terms of the overall operating ratio headwinds that creates but that's not an issue for us, we'll overcome it. Stock comp was a big headwind in Q1 as well. So, again, we're not worried about headwinds, we feel more convicted that we have a path to potentially even hitting that double nickel.

<A – Keith Creel>: Yeah, we could see it, Ken, even through the snow. It's the sun shining today, it's a little bit clearer.

<Q – Ken Hoexter>: Great. We had hail here, so appreciate the insight. Thanks, guys.

<Operator >: Your next question comes from the line of Brian Ossenbeck from JPMorgan. Please go ahead.

<Q – Brian Ossenbeck>: Hey. Thanks. Good afternoon. Appreciate taking the question. Maybe just to stick with the fundamentals for one more here, can you just talk about the capacity and your confidence in having that capacity for the growth that you're projecting here? Maybe even if demand is a bit more pent-up than you think, obviously you have some pretty big numbers in potash that John just mentioned, but, I mean, you can address it from both the head count perspective to how the hiring is working since you gave the December bonus. And then just from the network side, can you really keep those trains at the same length and size as volumes comes back?

<A – Keith Creel>: I'm not concerned about capacity. And the answer is yes when it comes to train length and train size and weight which all leads to the productivity that drives your crew starts, that drives your crew productivity, obviously your cost. I say that I look at second quarter, what we did in the first quarter is being surpassed already. Train length has increased, train weight has increased, productivity on crew starts, RTMs per employee, locomotive productivity. We've got locomotives that we have prepared for an even higher level of business, given what we had assumed to be if we go back in history would be a different demand environment in the crude space. So we have that in our back pocket, we have capacity. Obviously it depends on when it comes and where it comes, and we control that – we're very careful not to overcommit and underdeliver in our railroad, that's value destruction, that's not value

creation, but resources are not an issue.

<Q – Brian Ossenbeck>: Thank you.

<Operator>: Your next question comes from the line of Allison Landry from Credit Suisse. Please go ahead.

<Q – Allison Landry>: Thanks. So, Keith, you suggested that at around 4 times leverage that CN is locking up capital that could be needed for investments to capture growth and synergies. Should we interpret that as a comment as sort of unwillingness by CP to take up leverage to a similar range to come closer to the CN bid? And I guess, I mean, are you willing to raise your initial bid or is your view that you don't need to because of the regulatory risks.

<A – Keith Creel>: Well, I think you just answered the last question. When it speaks to leverage, it's 4.6 is what I was speaking to and I just frankly don't believe that's the right value proposition for our shareholders, to put our balance sheet at risk, to use all of our capacity on our powder to take away our ability to respond with shocks to the market, I just don't think that's a healthy place to go to at this point.

And in all honesty, I don't have to think about that because it's not a true alternative. That's a hypothetical situation. It's not a real deal as far as I'm concerned. It's kind of fantasyland. So my answer would be it's nothing that we're considering at all.

<Q – Allison Landry>: Okay. Thank you.

<A – Keith Creel>: Thank you.

<Operator>: Your next question comes from the line of Steve Hansen from Raymond James. Please go ahead.

<Q – Steve Hansen>: Yeah. Thank you. Keith, just building on your crystal clear response on the last question, in the outside scenario that shareholders go the other way, how do you feel about your growth prospects otherwise? I mean, do you feel like you still got lots of growth prospects in the absence of the KSU? I mean, is this a deal that you view as absolutely essential to get done or you're comfortable with not having it?

<A – Keith Creel>: I think we've demonstrated that we can create our own unique success, our value creation story, we've done it without it. Obviously the value that would create compared to what we can create without it, it's two different outcomes, I'm not going to suggest it's not. That would be disingenuous to suggest that.

But I would say that this railroad has shown its resiliency. We've got a very capable network in Canada at least now. When you get to the States, if the dynamic changed in a very unhealthy way in that space, then obviously we've got a responsibility to grow and create value and provide options for our shippers so it would suggest perhaps we have to look at alternatives. And in all honesty we've thought about those, we've talked about those, history says we've even considered those. And if you look at them in comparison, the truth says that those potential hypothetical scenarios are less complex than one is being suggested by CN with KCS.

<Q – Steve Hansen>: Indeed. Thank you for the time.

<A – Keith Creel>: Thank you, Steve.

<Operator:> Your next question comes from the line of Chris Wetherbee from Citi. Please go ahead.

<Q - Chris Wetherbee>: Yeah. Hey, thanks. Good afternoon, guys. Keith maybe I could pick up there. Can you elaborate a little bit on that in terms of potential alternatives? Obviously there has been that discussion in the past, several years ago. How is that a less complex transaction? Can you just sort of help us sort of think about that a little bit?

<A – Keith Creel>: Well, it's simple math. I think about all the overlaps and I spoke to some with the proposed CN, KCS and what that represents from pro service and pro competition versus the alternatives, and you could run a bunch of scenarios combining us with either the railroads East of the Mississippi, these are all hypothetical discussions, and I'm not suggesting that it's necessary. I'm committed to this deal. And I quite frankly think that this is so unique and special and value creating this will happen, this is going to be our reality, this going to be our future, and it's exciting. So I haven't wasted a lot of time breaking out those other alternatives. And I certainly don't think I'll get to that point where we have to, but if we did hypothetically, I think there's a case to be made and a responsibility that we'll have.

<A – Nadeem Velani>: And, Chris, we'd be the small Class 1 in that scenario.

<Q - Chris Wetherbee>: Okay, understood. Thank you.

<Operator>: The next question comes from the line of Justin Long from Stephens. Your line is open.

<Justin Long>: I wanted to ask about the synergy target you've laid out. Obviously the commentary around that is it airs on the side of conservatism. I would guess in the last month or so, as you've collected feedback from some of your customers – we can see the results that it's overwhelmingly positive. Is there anything you can share in terms of what the upside opportunity looks like on synergies? Are we talking closer to CAD 1 billion? Just some more detail around that and maybe where you see the opportunity that's incremental by geography or a particular commodity group. Would love some more color around that.

<A – Keith Creel>: I'll let John speak to the revenue side, but I can tell you now on the cost side we took a very conservative approach, and this isn't about cost cutting or rationalization, this is about value creating and it's about growth. But even in a growth world we can become and will become more productive.

We're going to run more fuel-efficient longer trains. We're going to grain efficiencies on locomotive productivity. We're going to close the gap and gain efficiencies on car miles per car day. I heard Sameh mention locomotive productivity last week on their call, and just that alone, if I look and compare and I think about the unique value this creates, I look at our numbers and this is all public information. There's a meaningful opportunity to close that's going to create locomotive capacity without capital expense. Think about it, if you do the math, 30%, what's 30% of 950 locomotives, you're talking about 300-plus locomotives have created capacity just by becoming more efficient. What's that worth? CAD 2 million apiece.

I'd say that's pretty material value. And I again that's just one instance. These things don't just happen. It takes hard work. It takes an ability to execute which we have a track record and an ability to do, and I just believe because of my experience and having lived it and having done it and having shown it with the teams that I've been blessed to work with that that kind of value creation is substantially understated that still allows us to grow and add jobs and create a whole lot of value for the synergies that are driven by the revenue side. So, John, why don't you comment more color on the revenue synergies?

<A – John Brooks>: Yeah. So, Justin, first and foremost, I would say, certainly I think the synergies that we've laid out I would characterize as conservative, achievable. But let me just be clear, I've been personally involved in working with the KCS railroad all my career and spent a lot of time marketing sales in the trenches with those folks looking at opportunities. I have to tell you they're conservative and achievable but we've done that for a reason. We're also being realistic.

We know the competition is going to bite back in certain areas. You know we're going to have let our product develop to realize those synergies and those opportunities. But all that to say, it's much more than one or two commodities. As I see these synergies, it's across all the commodities, it's not just the intermodal automotive play for CP. Certainly we think there is a tremendous opportunity in that space that Keith spoke earlier. There's opportunities to take trucks on the road and add that fourth competitive route North-South. There's opportunities in that auto space that will never be achievable if, in fact, the CP-

Kansas City Southern combination doesn't take place.

The grain business, as you can imagine, I've spoken to hundreds of customers over the last month on this opportunity. And the opportunities that have uncovered themselves, and I'm not going to put a number on, is it CAD 200 million, is it CAD 500 million, it certainly could be, it's out there. The ag industry alone to grow, utilizing our product, our 8,500-foot model with the KCS existing customers today but also working on investment and opportunities on our existing network is a huge opportunity just in itself. So, I feel again the numbers we've laid out our very achievable and I'm excited about the opportunities these customers have brought forward over the last three to four weeks.

<Q – Justin Long>: Great. Thanks. I appreciate the time.

<A – Keith Creel>: Thank you.

<Operator>: Your next question comes from the line of Scott Group from Wolfe Research. Please go ahead.

<Q – Scott Group>: Hey, thanks. Afternoon, guys. So, Keith, I'm sure you've had conversations with Pat or the KCS Board in the last two days. Do they share your view about sort of night and day deal certainty for one deal versus another? So that's one question.

And secondly, if for whatever reason the waiver is overturned, do you still think from a voting trust perspective it's so night and day your offer versus theirs? And then just one other thought – if you think that a CP Eastern rail deal is achievable, why isn't that more attractive if it even further expands network reach? So a few things there. Thank you.

<A – Keith Creel>: I'm going to make some notes that I'm going to – to come back you for some clarity on that. So let me start with the last. CP - eastern rail, I'm not focused on that, I'm focused on the KCS. I'm focused on the unique, simple, pro competitive, pro service, pro customer, end-to-end, one and only transaction of this industry that creates this unique value. Why would I think East? I'm not looking East. I'm looking to one partner and we have an agreement.

So to speak to that, about have I spoken to Pat? Of course, I've a spoken to Pat. We're in a partnership where we're moving forward to pursue this unique value-creating deal that we both believe in. And until or unless their board decides differently once they've looked at the truth and weighed in the facts and made their decision, that's exactly what we're focused on. So there will be no discussions on CP's part with KCS' board about anything other than the value we're creating uniquely for our shareholders that they uniquely get to enjoy, as well as our customers, as well as our employees.

And that's what's unique about this. They see the value in that, we see the value in that. That's been a key principle. From the very beginning, when Pat and I sat down, Scott, and we talked about what this could mean, how this could be something transformational uniquely, how this could be something that checks all the boxes. It serves the customers, it serves competition, it serves the employees, it serves and enables growth that will be unparalleled, it serves commerce, never at a time where it's needed more, in a very unique way.

So that's what we're so excited about and then that gets to the point of your first question about should it be overturned if we don't get the special consideration. I think that makes our value even more compelling because the reality is then it sort of boils down to the trust. Is the trust in the public's best interest? And there is only one combination and it's the only one that's been agreed to, that truly passes that test. The other could never be approved in my assessment, in my view based on the facts.

You can think about the DOJ, the DOJ weighed in about their concern, its institutional concern about trusts overall. We can debate about why it's necessary. It's part of our industry it absolutely is necessary, there's a difference. But when you compare these two deals and you compare the facts, the DOJ's number one concern in the letter that they wrote and they opined on is preserving competition while in trust. Well, we don't compete with the KCS. To get to the bottom line, the undeniable truth is that's a fact,

we're end-to-end. There's no overlap. Now, compare and contrast the truth to the other proposed combination. If in trust, which I would suggest because of that we'll never get to trust, it's undeniable that they compete, they absolutely compete. KCS and CN complete today.

On the 65 miles they've talked about and all those other locations they haven't, they compete. So, how do you protect competition if you're really concerned about it, and I would suggest, the truth says the DOJ is, if you allow a trust to be approved that has an anti-competitive basis to it, it's just that simple. And I think people are missing that, Scott. I really do.

<Q – Scott Group>: Appreciate those thoughts. Thank you, Keith.

<A – Keith Creel>: Thank you, Scott.

<Operator:> Your next question comes from the line of Amit Mehrotra from Deutsche Bank. Your line is open.

<Q – Amit Mehrotra>: Thanks. Keith, years ago you had said that the fulcrum or the driver for the consolidation in the industry, that would be the need for – basically, need for capacity would be the driver for the consolidation. Do you think we're at the point now today in terms of this hyper dearth of capacity? And more importantly, do you think that's a big consideration by the STB just given how little capacity there is out there relative to demand, and the improvement in that dynamic that comes from the fluidity of a point-to-point network?

And just if I could tack on one more question related to that, when you look at other alternatives, and maybe you won't need to, but if you look at other alternatives, would CP need to be the majority shareholder of the resulting entity and the management team? Is that an important consideration for CP and for you? Thank you.

<A – Keith Creel>: My consideration when it comes to CP and any deal that I would ever consider, is it fair to our shareholders? Does it create value for our shareholders? And do we fairly share? And that was a principle, obviously, in our evaluation of this deal that we're talking about, this combination we're so excited about.

So, let's go back to my thesis. And years ago, timing, again context matters. Years ago, I was sitting in a seat as an Operating Officer and initially as the CEO, both at this railway as well as at the competitor's railway, and I had to deal with Chicago, and the reality is there wasn't enough capacity in Chicago. At that point in time, whether you go back 5 years, you go back 8 or 10 years.

10 years says there is only one railroad that created capacity with PSR. Five years says there was two. And now in today's world, we have all but one that have adopted this operating model that creates capacity and creates long-term sustainable value and creates an opportunity, contrary to some naysayers' belief, to create cash flow to invest back into infrastructure to create additional capacity in a safe rail operation. And a case study, that is our railway. So, as I sit today and I look at it, I look at Chicago, there's been a lot of capacity created in Chicago. Is it infinite capacity? No. But does it delay that thesis of because we didn't have capacity that drives consolidation? Absolutely undeniably yes. I don't think that's a discussion for today. I don't think the STB needs to worry about a capacity play out of need. I think what they need to think about is competitive balance.

This deal does not challenge that. This deal, you could argue, cements that. This will be the gold standard of the hurdle that you would have to meet or exceed to do a deal number one, but it doesn't create imbalance because, again, it goes to the fundamentals of this. We got the two smallest railroads combining that would still be smallest railroad. How is that a threat other than a threat of competition to any of the compares? Let them answer that question. The answer is it's not.

Unlike this proposal, it undeniably would be – it would make the third largest railway, and you can minimize track miles. We're talking about reach, we're talking about networks. Yes, perhaps mileage is isolated to the US, but this isn't a US discussion, this is a USMCA discussion. This is a three-country

North American commerce, absolute truthful discussion. You can't diminish the connectivity of that and the importance of that and just focus on one little isolated piece. That's not truthful. So, again, I think if I were in the STB shoes and I'm looking at facts and I believe that to be true, they will, those facts are going to matter. And they're going to carry the day and they're going to carry the argument because it's true.

<Q – Amit Mehrotra>: Yeah. And there's a lot of talk about the Eastern rails as alternatives, but we very rarely talk about the Western rails, and there's one in particular that has very good penetration into Mexico. Are those alternatives in terms of, as you think about the possibility of a CN-KSC merger, kind of a competitive kind of dynamic being further penetration in Mexico through one of the West Coast rails?

<A – Keith Creel>: Yes, it's not a possibility if it's not one that I would ever consider, so it's – that's just a hypothetical question and would be a hypothetical answer. Probably doesn't serve anybody's interest to comment on, and I apologize.

<Q – Amit Mehrotra>: Okay. I thought I'd try anyways. Thank you very much. Appreciate it.

<A – Keith Creel>: Amit good try. Thank you.

<Operator>: Your next question comes from the line of Jason Seidl from Cowen. Please go ahead.

<Q – Jason Seidl>: Thank you, operator. Keith and team, thanks for taking the question, and a nice job on the quarter, but I'm going to focus obviously on the transaction that's on everybody's mind. Keith, you seem very certain that there is a lot more overlap in the transaction, where you're Canadian counterparts up there said, there was only, sorry, I believe five customers and nine plants on 65 miles of track. Can you give us some numbers behind surely just how many shippers you believe are at risk in this potential transaction, if CN-KCS were to come to life? .

<A – Keith Creel>: You know what? I – John, you can probably – looking at it. Like I said earlier, I didn't just make up that 100 number. There is over 100 combinations of CP, CN today that would be impacted by that. But let me go back to some real facts, and think of the reality. The reality is I used to be a Train Master in Memphis, Tennessee on the Illinois Central Railroad back 1996, I don't know, that was – it's been a while ago, 25 years ago.

And then I went from Memphis, Tennessee on the IC to Jackson, Mississippi, as I've said earlier, and my territory covered down to Mobile, so I know the lines to Mobile. I understand that in Hattiesburg, Mississippi or going down to the coast in Mississippi, the KCS could operate then and can operate now down to serve that Gulfport. I also know that today the KCS has rights and an opportunity to operate customers' business, say, from Kansas City down to Mobile. I know tomorrow, if this deal were to be approved or suggested, that that wouldn't exist.

Go to New Orleans, I spent a lot of time on that railroad, south of Jackson going down to New Orleans, Baton Rouge, Geismar, Destrehan. I know the sidings. I know the towns. I know the business. To suggest it's isolated to five customers that are dual-served today that would be single-line served tomorrow in the Baton Rouge Geismar area again, ignores New Orleans, ignores the competitive options, ignores the disadvantages, the pains of the customers.

It's just the reality. I don't even have to get into the number crunching, which will be done, and those will show the facts to be true. I know it because I lived it. I understand it. I lived there. I worked there. I worked with those people. I understand the KCS in that space. I understand the IC in that space, I would suggest, as well, if not better, than many people in this industry.

<Q – Jason Seidl>: I appreciate that color. And so, I guess, based on your comments, you would be surprised if there wasn't a bunch of shipper pushback to this potential combination?

<A – Keith Creel>: I – surprised it would be an understatement.

<Q – Jason Seidl>: Okay. I appreciate the time.

<A – Keith Creel>: I think time will show you very quickly how many people might be opposed to this.

<Q – Jason Seidl>: Appreciate it, guys.

<A – Keith Creel>: Thank you.

<Operator>: Your next question comes from the line of Brandon Oglenski from Barclays. Please go ahead.

<Q – Brandon Oglenski>: Hey, good afternoon, and thanks for taking my questions. So, Keith, I guess I want to follow up on that. The interchanges that you talked about, because the physical overlap is rather short, and I'm not trying to spar with you in anyway , but you did say there's a lot of instances in the Midwest where you've gone from maybe three options to two, and the CP option was ultimately leveraging KCS to get down south. Is there an ability when another – let's say that the other deal did go through, what's their ability to then block those interchanges? Is that a real concern for shippers in the market?

<A – Keith Creel>: To block the interchanges? There's a difference between blocking an interchange and it being a friendly interchange. So, I would suggest it wouldn't be as friendly as it is today. I can't imagine a world where today we operate, we actually colocate, and I think we've spoken to this. I was – had the honor of partnering with Pat last week and actually went to our joint agency in Kansas City and met with our employees. We did a town hall.

I can't imagine a world where our trains, our crews, would come in to our primary competitor, which eliminates our friendly partnership into the yard in Kansas City and that being good for any customer, or we – red carpet is not going to be rolled out, and we're not going to be warmly received either in rate offerings, in combination, or in reality. It's just not a realistic possibility. So, if you go through that gateway today, I would suggest you'll be impacted.

<A – John Brooks>: Brandon, I'll add to Keith's comments. Just think of it in terms of a propane shipper coming out of Edmonton. And frankly, we do a lot of our business out of that region, down over Kansas City to connections with KCS to get into Mexico. There has been – were tomorrow CN would have a direct route, I certainly, if I'm one of those shippers up there, I'd get – I would be very concerned about loss of a gateway or loss of an opportunity versus having the opportunity to compete on a single-line haul that the CP-KC route would provide those shippers.

<A – Keith Creel>: That competition word is important. That's not an aspirational goal of us. That's a desire. To be able to create competitive alternatives for our customers so that they can reach new markets, and then they can grow, and they can compete in that market space they reach. We welcome competition at this railway. We think it's healthy. We think it makes us better. We think it makes BN better. We think it makes UP better to make CN better. It makes the industry better. It makes it stronger. Competition is good. Why be afraid of it? Step into it. Don't try to eliminate it. Don't try to snuff it out. Don't try to buy to make it go away, or don't try to damage someone who's trying to create it just because you think you can. I just don't agree with that fundamentally or principally, and I don't our think customers will either.

<Q – Brandon Oglenski>: Thank you.

<Operator>: Your next question comes from the line of Benoit Poirier from Desjardins Capital Markets. Please go ahead.

<Q – Benoit Poirier>: Yeah. Good afternoon, gentleman. Could you talk a little bit about the pricing, whether it has strengthened given the tight capacity, and how we should be thinking about the yield to evolve in the coming quarter in light of the business mix fuel and FX? Thanks.

<A – John Brooks>: Sure, Benoit. I'll take. It's John here. So, you know what? I saw good momentum in Q4 in terms of our renewal pricing. I can tell you that that accelerated. So, when I say 3%- plus type numbers into Q1, and I don't see that changing. Frankly, I think that continues to accelerate to those

upper end of those ranges that we have talked about. As you think about fuel and FX or yield as a whole, I think we continue to sort of see improvement, and begin to sort of lap some of those headwinds as we move through the year. On the mix front, ultimately, I see that improving a little bit too, and probably kind of coming back into that – more of that flat range, and I'll even speak to sort of the liquidated damages in that I think that sort of moderates itself through the year. So, overall, I see the cents for RTM gaining some momentum as we move through the back half of the year.

<Q – Benoit Poirier>: Thank you very much.

<A – John Brooks>: Yes.

<A – Keith Creel>: Thank you, Benoit.

<Operator>: Your next question comes from the line of David Vernon from Bernstein. Please go ahead.

<Q – David Vernon>: Hey, guys. So, Keith, I just wanted to ask you a process question. As these alternative offers being either reviewed or not, depending on what the KCS board is going to do, what's your expectation for the STB in terms of moving forward with its determination on whether or not there's going to be a waiver, a grant – whether it's going to be – the transaction is going to be evaluated under the waiver rules or – and separately? Do you expect them to come out and say anything about your proposed voting trust structure while this other deal is out there? I'm just trying to get a sense for kind of what you're hearing from your lawyers around this, the STB's sort of work in process while this competing bids are out there?

<A – Keith Creel>: I think your words best describe it. It's work in process, and I think it would be ill-advised on my part to predict what the STB may or may not do. I think our facts are very compelling. The case is there. I believe that the facts matter. I believe that in 2001, when that carve-out was created, it was fact-specific. And our combination supports the facts that enable that carve-out. That's what I believe to be true, and ultimately I know the truth is the STB will make that final decision, and we believe in the facts, and we're going to continue to work with them. Their – CN's proposal has no bearing, in my mind, on our facts. It's two different stories, two different set of facts, and I think that matters.

<Q – David Vernon>: If I could just kind of take a follow-up on there. Some of the facts that maybe are not on my table right now would be some of things that Canadian National could propose to maybe address some of these competitive concerns. Are you – is your position that those just complicate it and make it harder to do, or that maybe those remedies that you would traditionally look to in a situation like this would not be effective? Like, how do you think about sort of prejudging the deal without looking at the potential for remedies to some of these issues that you're pointing in to?

<A – Keith Creel>: Well, I'm focused on the fact of our deal. There's no overlap. It's simple. It's end-to-end. It's all positive on service. It's all positive on new competitive opportunities. There's no negatives. There's no 3-to-2. There's no 4-to-3. There's no 2-to-1. 0 is a pretty powerful number, it's pretty undeniable number. So, based on those facts, that's what I judge my view on. In comparison – and again, I'm not even going to comment anymore. I've told you what the truth is relative to the way I assess that other deal and the complexity that it represents, and those facts are undeniable, and ultimately it's the STB's job, and they're very capable of assessing the true facts in making their determination. And I just have faith in that process, and I have faith in their professional capacity and their abilities. They're a talented group of folks.

<Operator>: Your next question comes from the line of Tom Wadewitz from UBS. Please go ahead.

<Q – Thomas Wadewitz>: Hi. Yeah, good afternoon. Keith, we – you've obviously given us the pretty compelling framework for why you think the regulatory approval is stronger for CP-KSU. But I think if you look at it and say the first hurdle is for KSU's board and shareholders too to choose which deal, and I've heard that both sides seem to believe a voting trust would be approved. So, it seems to me like with that logic, I guess I'm struggling with why, Keith, your shareholders wouldn't choose simply the highest price because all they need is to get a voting trust approval and then they get their money. So, I don't know if

you disagree with that logic, but if that's the case, if that's reasonable, why wouldn't you raise the bid or would you raise the bid and just do it with shares instead of taking up balance sheet leverage?

<A – Keith Creel>: Yeah. Well, all those lot of questions, Tom, we never get to that because it all stops with deal certainty and with trust approval certainty. Our deal represents something that's achievable. There's certainty based on the facts that the STB will ultimately opine on or not in our trust being established. That supports our deal, that supports our ability to get the trust approved, to get to the value which is the next concern that their board of directors, they're fiduciary concern would be. Now, if I look at and I put myself in their shoes and I'm looking at an inferior deal that represents uncertainty, I don't care how much value you might suggest to me that's on the other side of the fence, if I can't get to it, I don't get to realize it. I don't know any other clear way to articulate that. It's a fantasy. Unless you believe that based on the facts that they will meet the public interest test when it's opined on and ruled on and due based on facts by the STB, you can't believe the value, and I just don't believe it. The facts don't support it. So, if facts and truth matter, it's not achievable. So, you never get to the value. It's worth zero.

<Q – Thomas Wadewitz>: Okay. Your point is not so much that the merger can't be approved with CN, but you think you can't even approve a voting trust, and that – I guess that's your point.

<A – Keith Creel>: Yeah. You don't get to the substantive review of the merger until you get beyond the trust, and the trust is when the KCS shareholder would realize their consideration is not realizable if you don't get the trust approved.

<Q – Thomas Wadewitz>: Right. Okay. And what – you commented on an earlier question about raising leverage. Is it – just to make sure I understand your response, are you saying you're not considering raising the bid or you're just concerned about raising the cash portion?

<A – Keith Creel>: We're not considering changing anything with our bid. We're focused on getting our deal, which represents great value for the CP shareholder, the KCS shareholder. We've agreed to this. We have an agreement. That's what we've put forward in front of the STB, based on the value it creates. That's what we're focused on. There's no need to discuss raising leverage. There's no need to discuss paying more money. It stands alone on its own merits. There's nothing to compare it to. So, why even have those discussions? Not going to. Unless the KCS board gets to a point and they decide differently, they haven't. So, I'm not even going there. There's no need to. And based on the facts, I don't believe they will. I think the decision is pretty obvious. The conclusions are obvious. I don't have any other clear way to draw the scenarios out.

<Q – Thomas Wadewitz>: Okay. But if the board came back, you could consider a different approach, it sounds like?

<A – Keith Creel>: Oh, I'm just not going to comment on a hypothetical, just can't. I'm not going to give it any energy, just not going to do it. I'm focused...

<Q – Thomas Wadewitz>: Yeah.

<A – Keith Creel>: ...on the value of this unique deal that we've agreed to create. And I would suggest that's what matters, that's the truth.

<Q – Thomas Wadewitz>: Right. Okay. Thank you for the time. Appreciate it.

<A – Keith Creel>: Thanks, Tom.

<Operator>: We're now out of time. I turn the call back over to Mr. Keith Creel.

<A – Keith Creel>: Okay. Well, again, thank you for joining us today. I hope that our fact-based truthful discussion has helped clear some of the air. I think that's our responsibility. I certainly feel that responsibility in this industry, to speak the truth, both to the strengths of our deal and what the value uniquely creates, as well as the risks that are associated with alternatives that are being suggested.

We look forward to the second quarter results. This company started strong in spite of some opposition.

The second month of the year, February, was a challenging year. But the outlook looks good. We still see opportunity for margin improvement, single-digit, double-digit, as we progress in to the year. RTM growth finishing well within what we've guided to at the end of the year, which is going to be a result our shareholders will be rewarded for, and I think the market will respect, again, based on our track record. So, we look forward to seeing everyone soon. Stay well.

<Operator:> This concludes today's conference call. You may now disconnect