# Transcript

## Q4 2021 Earnings Call

**January 27, 2022**

**Canadian Pacific Corporate Participants:**

Keith Creel – President & Chief Executive Officer
John Brooks – EVP & Chief Marketing Officer
Nadeem Velani – EVP & Chief Financial Officer
Maeghan Albiston – AVP Investor Relations & Pensions

**Kansas City Southern Corporate Participants:**
Patrick Ottensmeyer – President & Chief Executive Officer
Michael Upchurch – EVP & Chief Financial Officer

# MANAGEMENT DISCUSSION SECTION

## Operator

Good afternoon. My name is Sylvie, and I will be your conference operator today. At this time, I would like to welcome everyone to Canadian Pacific's Fourth 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 will be a question-and-answer session. [Operator Instructions]

And I would like to introduce Maeghan Albiston, Vice-President Capital Markets, to begin the conference.

## Maeghan Albiston

Thank you, Sylvie. Good afternoon, everyone, and thank you for joining us today.

Before we begin, I want to remind you that this presentation contains forward-looking information and 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, which are outlined on slide 3.

With me here today is Keith Creel, our President and Chief Executive Officer; Nadeem Velani, Executive Vice President and Chief Financial Officer; and John Brooks, Executive Vice President and Chief Marketing Officer. Also, attending our call today on behalf of Kansas City Southern are CEO, Pat Ottensmeyer; and CFO, Mike Upchurch, who will be happy to answer questions regarding KCS. As CP investors are aware KCS is now beneficially owned by CP through a voting trust, pending control approval by the STB.

During this trust period, and prior to the STB approving CP's controlled KCS, CP and KCS operate independently and KCS's business is managed by its own officers, and is overseen by its own board of directors. During this trust period, and prior to the STB making a determination regarding control, CP and KCS operate as two independent arm's length companies. As a result, only KCS management is truly in a position to answer investor questions regarding their performance and results.

I would highlight that KCS has posted an information package to their website. And should you have any questions about KCS' performance that aren't addressed on today's call, please feel free to reach out to Mike, Ashley and the KCS team.

We will start the call with some formal remarks and follow that up with a question and answer period. In the interest of time and to allow as many participants as possible, we would appreciate, if you could limit your questions to one.

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

## Keith Creel

Okay. Thank you, Maeghan. Let me welcome Mike and Pat to the call today as well. And then proceed to thank our CP family, I say this a lot, railroading is an outdoors sport that I can tell you this quarter had some exceptionally challenging conditions that the team's commitment, grit and determination certainly was tested, but to overcome and produce this result under those truly incredible conditions that I think deserves a special thanks.

From the catastrophic flooding in British Columbia, which we're all very aware of that occurred in November. They took a deep breath from what I would call was a miraculous effort to get the railroad open again in eight days to step right into 40 degree temperatures again as we closed the year out which

carried into January.

So again, outdoor sport, yes, winter, yes, we know but I'll tell you this was an exceptionable outcome given the challenges that they face. So thank you for that and thank you for your commitment, your sacrifice.

To the results themselves the quarter we delivered fourth quarter revenues of $2 billion and operating ratio 57.5% and adjusted EPS of $0.95. For the full year, our total revenues were up 4%. The operating ratio 57.6%, which is 50 basis points increase over last year's record OR, adjusted EPS of $3.76 represents revenue growth of 7% versus last year.

As I said, the CP Family finished the year with a strong operating performance in spite of the challenges we faced to think that we were able to drive productivity improvements and still increased train lengths and weights 3% respectively, again as an outstanding results. Fuel efficiency as well, in spite of those challenges improving by 1%, an outstanding result, and all three of these metrics were new record lows for the company.

On the safety front, something we're extremely proud, our personal injuries were down 17% year-over-year to a new all-time CP low. This marks the sixth consecutive year of improvements on the personal injury front and it's a testament to the team's commitment and that's all 12,000 employees to coming home safely every day.

That said, this is an area where we don't rest, safety as a journey. I say that often. You never arrive. While we're certainly proud of the progress that we've made on the injury front, we did see a bit of step up in train accidents from our all-time record low of last year, but that said again for the 16th consecutive year, we're proud that our commitment to people, process, and technology allows us to enjoy the best safety record in the industry. We know there's more to do with that said, we're going to continue to leverage technology and the strong safety culture that we have in this company to drive further improvements in this area.

Focusing on the sustainability front, this is another area that we continue to make significant progress. We're proud to be named the highest ranked freight transportation company on the Corporate Knights Global 100 Index as well as named for the second consecutive year to the Dow Jones Sustainability North America Index. And on the hydrogen front, which is all becoming more topical as the days progress, we continue to demonstrate our leadership in this space, commitment to a more sustainable future. There are hydrogen locomotive projects with the additional grant funding that we received from the Emissions Reduction Alberta, we've been able to expand the scope to three locomotives and two fueling stations as we enter into 2022.

We look forward to moving from the last setting into the next phase of switching in road trials. And I'm very happy to say that our hydrogen locomotive in the fourth quarter moved from concept to reality, it actually moved in its own volition, under its own power. So it's not a concept. It's not a spin, it's fact, and it's going to change in a very meaningful way the emission footprint of freight locomotives in this industry.

On the transaction itself, that's another area. Again, in the fourth quarter, very excited to hit the milestone with our CP-KC journey, closing KCS into trust on December 14. The regulatory review process is well underway. No doubt, many of you have likely seen some of the early headlines related to this process. We're going to respect the regulatory process. We're going to work with the other rails and the shipping groups to find reasonable solutions to address the concerns – reasonable concerns that might arise. And we're extremely excited, too, about our ability to reach an agreement with Amtrak, demonstrating our commitment to passenger service, not only on the CP network, but more specifically to the Baton Rouge and New Orleans network on the KCS railroad.

Our customers are enthusiastic about the opportunity for the seamless efficient reliable single-line rail service across the US, Mexico and Canada. John will elaborate, I'm sure we can address it in Q&A, but we have all been intimately involved getting in front of our customers. We made over 90 customer

contacts, talking about the art of the possible, talking about what this new transnational railroad, assuming it's approved or when it's approved by the STB. And we'll be able to go to work, creating and reaching new markets and service that, quite frankly, has never been possible. And I believe will only be – forever is a long time, but I think the single one and only transnational railroad to exist in the North American continent.

So with that, let me hand it over to John to bring a bit more color on the markets and then Nadeem will elaborate on the numbers and we'll save the balance of the time for Q&A.

## John Brooks

All right. Well, thank you, Keith, and good afternoon, everyone. So as Keith spoke about the fourth quarter, it was certainly that other reminder that this is an outdoor sport. We knew this quarter was going to be challenging, certainly given the grain comps, but the BC outage certainly applied even more pressure to our customers and into our volumes.

My team did as they always do. We stayed super close to our customers and our operating team and they worked hard to find solutions across our marketplace as our western part of our network continued to recover through the quarter. While Q4 performance certainly was challenging, all-in 2021 full year with a record for our freight revenue and our total revenue.

Now looking specifically at Q4. Revenues were up 1% in the quarter despite an 11% decline in RTMs. Fuel and FX combined to be a 4% tailwind and price and mix combined to be positive 8%. As you've all heard, over the past few weeks from many in the transport industry, the pricing environment continues to be very strong.

Now taking a closer look at our fourth quarter revenue performance, I'll speak to the results on a currency adjusted basis. Grain volumes were down 21% in the quarter, while revenues were down 12%. As expected, the 40% reduction in the Canadian crop is driving this decline in volumes. The good news is we've taken the decline in the Canadian grain crop and created an opportunity.

We had an all-time record quarter and year for our US grain franchise with 30% year-over-year RTM growth. As an example, the team worked extremely hard with our shippers and receivers to create a new supply chain to offset some of the challenges in Canada by moving US corn into Canadian cattle feedlots to supplement the shortage of domestic feed.

We expect the challenges in Canadian grain to persist until we get the new crop in Q3. We will start to get some better visibility into the potential of the 2022 crop in the spring, but we are certainly happy to see snow on the ground across the prairies, providing much needed moisture.

On the potash front, volumes were down 4% in the quarter where revenues were up 14%. The decrease in volume reflects the BC flood outage, but we worked closely with Canpotex to minimize the volume lost by moving more trains to Portland. As you would have seen in December, we announced the signing of our new long-term contract with Canpotex. We are proud to extend this partnership and we expect to see high single-digit volume growth in 2022 as Canpotex continues to see strong demand in its global markets. And as we close out the bulk business, coal revenues were down 14%, while volumes were down 27% as the supply chain was challenged by the floods, resulting in reduced volumes from the mines and more trains routing north to Ridley.

Moving on to merchandise. The energy, chemicals, plastics portfolio saw revenues increase 15% on slightly negative volumes. We had a record full year revenue performance in ECP despite flat volumes in crude. I'm excited to see two new growth opportunities in ECP with Independent Energy beginning to produce ultralow-sulfur diesel and Inter Pipeline commissioning their new plastics facility in the Alberta Heartland. Both of these new customers are expected to start rail operations in Q2, and CP is proud to be their preferred rail partner.

Now full year, we moved about 60,000 carloads of crude. In 2022, we expect that run rate to slightly

decline and the last of our contract liquidated damages to roll off through the year.

The DRU unit at Hardisty Alberta has successfully ramped up and we are at a run rate of 50,000 barrels per day that we expected at Phase 1 of this initiative. As a reminder, the DRU process produces a non-hazardous DRUbit product that CP exclusively serves from Hardisty and this movement goes to Kansas City for interchange to the KCS.

In forest products, volumes were flat while revenues were up 10%. It was a record Q4 in forest products and the team continues to deliver strong price performance.

In MMC, revenues were up 28% and volumes increased 20%, largely driven by our frac sand business, our steel business and almost double-digit growth in our transload business. Our service product is winning in both unit train and single carload business in these manifest markets.

Automotive revenues were down 18%, while volumes were down 19% on the quarter. The chip shortage and COVID-related facility shutdowns continue to challenge our OEMs. Despite these latest disruptions related to the Omicron variant, the 2022 outlook is looking better, particularly as we move into the second half of the year. We were excited last week to see our first Chevy Silverado vehicles load onto rail at GM's Oshawa plant. CP and GM have partnered on this new business for the distribution of these vehicles.

Now finally, on our intermodal side of our business. Quarterly volumes were down 5% and revenue was up 9%. We have now had five consecutive record quarters for our domestic intermodal franchise even with the significant disruptions in BC. The new Pacific Transload Express facility we opened in Vancouver with Maersk is offering our domestic intermodal customers new distribution solutions, while enabling Maersk to spin their containers back faster to overseas markets.

Our transload solution will take thousands of trucks off the roads of Vancouver, while at the same time delivering new revenue growth in 2022 to our franchise. We are also very proud of a new multiyear contract with Canadian Tire. Our long-standing partnership with the Canadian Tire is growing stronger, and we look forward to continued collaboration with their team to deliver supply chain solutions across Canada.

And now finally, our international franchise, supply chain challenges and the BC outage negatively impacted our volumes in the quarter. But I can tell you, the team is working hard with our port partners and customers to regain fluidity. We see strong pent-up import demand and anticipate ongoing recovery as we move through 2022.

So let me close by saying, we're looking, as I see it, at record demand levels across many of our lines of business and see opportunities to overcome the Canadian grain headwind ahead of us.

As always, my team is laser focused on pricing to the value of our service and capacity, and we are working closely with our customers to help them win in their marketplace. As Keith referenced, we met with almost close to 100 customers in Q4 to educate them on our new routes and the competitive alternatives that the CP-KCS combined network, once we're approved by the STB, will create. I can tell you, the opportunity list is growing longer and the customer feedback remains extremely positive.

So with that, I'll stop and turn it over to Nadeem

## Nadeem Velani

Thanks, John, and good afternoon. 2021 was a year of challenges that highlighted the team's resiliency. As we look to 2022, we are excited about the opportunity ahead of us, but it's not without some noise. You will notice that we did not provide formal guidance in our press release.

With so many moving pieces, we think it would create false precision to provide guidance as there are more variables than usual that we don't control. For example, on the KCS front, we do not have control of their operations and did not create their 2022 plan, so we'll not be providing guidance as to their expected performance and its impact on our earnings.

With the timing and conclusion of the regulatory process in the hands of the STB as well as with Omicron and other macro factors presenting some near-term uncertainty, we felt it was prudent not to provide formal guidance. We are committed to providing as much transparency as we are able to and I'll provide key modeling data points in my remarks where appropriate.

So now looking at Q4 overall. The operating ratio increased 530 basis points to 59.2%. On an adjusted basis, the operating ratio was 57.5%, a 360 basis point increase from Q4 2020. I will remind you that Q4 2020 included a 330 basis point impact from the Detroit River Tunnel transaction.

Taking a closer look at a few items on the expense side, I will speak to the variances on an FX-adjusted basis. Comp and benefits expense was down 6% or $25 million versus last year. The primary driver of the decrease is lower volume in the quarter.

Fuel expense increased $66 million or 40%, primarily as a result of higher fuel prices. This year, we once again achieved a full year record fuel efficiency moving us a step closer to our 38% locomotive emissions reduction targets.

Materials expense was down 6% or $3 million as a result of lower volumes in the quarter. Equipment rents were down 12% or $4 million as a result of lower volume and lower prices paid for pooled equipment. Depreciation expense was $206 million, an increase of 6% as a result of a higher asset base. For CP standalone, we expect a similar $40 million increase in 2022 as our asset base grows.

Purchase services was $250 million, an increase of $56 million or 29% when adjusted for acquisition costs. The main driver of the increase is lapping the gain related to our acquisition of the Detroit River Tunnel for a total of $68 million in Q4 2020.

Moving below the line, we are recognizing 18 days of equity pickup from KCS, which included $169 million of transaction costs incurred at the end of the year, which we've excluded for our adjusted diluted EPS. Other components of net periodic benefit recovery increased $16 million, reflecting lower discount rates.In 2022, we expect this to be relatively flat to 2021.

Net interest expense is up $12 million as a result of higher debt loads since we issued $10.7 billion in acquisition debt during the quarter. We issued a total of $6.6 billion and CAD2.2 billion denominated debt with a weighted average coupon of 2.4%, financing across multiple tenors allowed us to finance at very attractive rates while also maintaining the financial flexibility to delever in accordance with our plans.

For 2022, CP stand-alone interest expense should be approximately $650 million. Income tax expense decreased $44 million or 23%, primarily as a result of a lower effective tax rate. Rounding out the income statement, adjusted diluted EPS decreased 6% to $0.95 in the quarter.

Moving on to full year results on the next slide. The fourth quarter performance caps a challenging year for the CP Family. Our full year adjusted operating ratio was 57.6%, a 50 basis point increase year-over-year. Adjusted income grew 7%, and our record adjusted diluted EPS increased 7%. As you model out 2022, we would expect CP's average share count to be approximately 930 million shares and for the corporate tax rate to be in the 24% to 24.5% range.

We are prudent with our balance sheet this year with actions taken to pause the buyback program and dividend growth as we work on the transformational opportunity of our merger with KCS. Leverage is currently at its peak, as we have issued all of our acquisition debt. You will see our leverage rapidly come down as we pay down acquisition debt over the coming 24 months. The buyback and dividend increases will remain paused until we return to our 2.5 times debt-to-EBITDA target. We are already starting to see cash flow from KCS with a dividend in January this month that will be applied to outstanding debt.

Before wrapping up, I want to provide a little accounting context around the KCS equity pickup. We are recognizing 100% of their net income in our financial statements as one line below operating income, reflecting that we do not have control. In Q4 2021, we only owned the shares for 18 days, so you see 18 days of equity pickup, which includes $169 million of transaction costs, creating a loss you see in those

18 days.

Embedded in the equity pickup will be the step-up in depreciation and amortization from the preliminary purchase price allocation. In 2022, we expect the depreciation step-up to be approximately $220 million, partially offsetting the increase in depreciation will be credits for deferred taxes and interest expense. So the net impact to the equity pickup is a reduction of $125 million from KCS' 2022 equity income.

2021 tested our mettle and our team of railroaders rose to the occasion at every turn. 2022 will be a year of opportunity, but it will not be without some noise. We'll work hard to be as transparent as possible as we move through the regulatory process. I'm proud of the team and look forward to what we can accomplish in 2022.

So with that, let me pass things over to Keith to wrap things up before Q&A.

## Keith Creel

Okay. Thanks, Nadeem and John. Let me close my remarks by saying – sort of looking forward, as we move past some of the uncertainty and disruptions, we're super excited about the opportunities that lie ahead of us in 2022. The demand environment is strong. You couple that with our unique initiatives and our service capabilities [indiscernible] (23:52) to succeed in 2022 and beyond. You combine our stand-alone opportunities with that of this combined CP-KC network, the future is extremely, extremely bright.

[Technical Difficulty]

Okay. So I'm going to assume that everything that I said, that's quite frankly, I think the remarks that I made a minute ago were not heard. So I apologize for the technology difficulties. So let me back up and just say thank you, John and Nadeem, for that color, and I'm going to close my remarks by saying as we look forward to 2022, we get past some of the uncertainty and the disruptions. We're excited about the opportunities that lie ahead. This demand environment is extremely strong. We couple that with our unique initiatives and our service capabilities. We're extremely well positioned to succeed.

[Technical Difficulty]

## Nadeem Velani

Operator, I think – it's Nadeem Velani. We have myself and Keith Creel. We can open up for Q&A

# Question & Answer

## Operator

Certainly. [Operator Instructions] And your first question will be from Walter Spracklin at RBC. Please go ahead.

**<Q – Walter Spracklin>:** Yes. Thanks very much. Good afternoon, everyone

**<A – Nadeem Velani>:** Hi, Walter

**<Q – Walter Spracklin>:** So perhaps what we could start with just a question on concessions. I know I get a lot of those. Keith, you can hear me. If there's – we get a lot of those from investors. There's been a lot of noise in the filings. You mentioned that you're separating what's reasonable from what's not reasonable. Can you highlight what areas of request that you might deem reasonable that you received and that we may see? And are you – do you continue to be of the view that material concessions continue to be unlikely as part of the outcome for this review?

**<A – Keith Creel>:** Well, let me – Walter, hopefully you can hear me okay. I'll start with confirming the statement that you just made. Often, we think about this. Significant concessions have required to offset losses to competition. Network overlap, predatory pricing or poor service and none of those points are

true about this transaction, this proposed transaction. So that's the starting point. The requests that have been made so far, not a surprise, obviously. We expected everybody to come to the table asking for certain things.

But at the same time, as we said from the very beginning, we're going to negotiate on reasonable terms and reasonableness is the two-way conversation, obviously. Again, pro-competitive facts to me, leads to a good outcome for the customer, for the country, for the freight network. So significant concessions, when you have good facts and they all support competition are not a reasonable expectation for anyone to come to the table with. That's probably the best way I can say it.

I can tell you, Walter, I was very encouraged to see the STB recent ruling. I think about what that says to me, I think it's – this is a fair and open process. I think it demonstrates the commitment to the procedural schedule and a commitment to an efficient timely review of our proposed transaction, all which bodes well for the very positive pro-competitive facts of this combination.

**<Q – Walter Spracklin>:** Appreciate the time as always. Thank you, Keith.

**<A – Keith Creel>:** Thank you, Walter.

**<Operator >:** Thank you. Your next question will be from Tom Wadewitz at UBS. Please go ahead.

**<Q – Tom Wadewitz>:** Yes. Good afternoon. Keith, my understanding is that you're obviously constrained on the operating side. You can't touch the KCS network. But from a customer perspective, you can go to customers, obviously, I mean, you said, I guess, I don't know if it was in conjunction with KCS management, but 100 calls or meetings is a lot. Do you think that we would expect any kind of new win type of announcements in 2022 of business related to the combination that you're able to reach talking together with KSU auto contracts, new ag sites you'll be serving, things like that?

**<A – Keith Creel>:** Let me start by saying we have to handle this in a very singular fashion. Pat and his team are handling KCS' business. CP, obviously, myself and our team handling ours. There's nothing that prevents us from going to a customer that might be interested from or that might benefit from this new proposed single line service, assuming the STB approves the transaction, we could make any discussion contingent upon that. So the answer is yes, that's possible.

But at this point, I can tell you the meetings that we've had, the lion’s share I’ve participated in the CP team talking about CP opportunities with our customers and then obviously, we discussed what the future might look like. So the groundwork is being laid, the key point with our customers – we get into long-term contracts that lock you out of the opportunity to benefit from the full competitive nature and opportunities and options in this transaction, for me, it's a customer's decision to make.

But obviously, we're doing our best to educate them to the benefits of not choosing that so that they can uniquely benefit from the unique benefit this combination is going to create. So hopefully, that answers your question, Tom. We got to be very careful not to exert and we will not exert, control or influence over KCS standalone. But again, the two together can talk about what the future looks like and what that might mean for the customer, assuming the STB approves our transaction.

**<Q – Tom Wadewitz>:** So it sounds like maybe keep the expectations low for this year and probably setting the stage for more to come after the approval.

**<A – Keith Creel>:** Yes. We're certainly not taking in any customer wins or business as a result of the transaction. We're just preparing for and laying the groundwork for what's to come, the art of the possible.

**<Q – Tom Wadewitz>:** Great. Thank you Keith

**<Operator >:** Thank you.

**<A – Keith Creel>:** Thank you, Tom.

**<Operator >:** Next question will be from Fadi Chamoun at BMO. Please go ahead.

**<Q – Fadi Chamoun>:** Thank you. Good afternoon, everyone. A question along the same lines. I mean you have this Amtrak support statement, which clearly addresses the key concern by regulators. Are there other things that you can potentially kind of try to firm up ahead of this regulatory process with other key parties in this transaction, like short line or even other railroads? I just wonder if there are things that you can address potentially before this – if we go to the hearing process, maybe a little bit later on, so?

**<A – Keith Creel>:** Yeah. Fadi, great question, and the answer is absolutely yes. And I would suggest that the individual part is if we can reach agreement on whatever the item might be, come to reasonable terms between ourselves, whether it's with the short line, whether it's for the main line, whether it's for the customer, whether it's with an association, I think the STB would prefer that.

So obviously, those discussions are being had in all those areas. We've had discussions, some more than others, with all the Class 1. We've had discussions with short lines. We're having discussions with shipping organization.

So we're prepared to making ourselves available to have reasonable discussions, to listen to concerns and hopefully come to reasonable, acceptable solutions between all of those parties prior to alongside, I guess, in parallel with the merger application process.

**<Q – Fadi Chamoun>:** And are the views – like when you kind of address some of these things with the other Class 1 carriers, are the views widely different between where you see things and where they want things to go?

**<A – Keith Creel>:** Well, the way I look at it, number one, I'm going to listen what you ask is, but the backdrop I compare it to, obviously, I've got a lot of precedents, I've got a lot of history that we can review because this is moving forward over the old rules.

So obviously, there's a catalog of different deals that have been done and concessions and agreements that have been made that have been filed with the STB. So we have the benefit – precedence and the benefit of those that have navigated these waters before us.

We've made certain commitments, obviously, to keep interchanges open on reasonable terms and in physical terms. We're not going to create new bottleneck pricing. We're willing to enter into some reasonable arbitrated settlement process in individual discussions with our shipping groups and/or our customers.

So there's a menu of options that are on the table, but always with the backdrop. Look, I understand – we understand what the laws are. We understand that pro competition is what the STB seeks. And when we represent pro-competitive facts that puts us in a very strong position to have these discussions on reasonable terms, again, to come to reasonable solutions. And if they're not up to this before, if we can't resolve it because someone is being unreasonable, then if we have to at the end, that what will be tabled, and that's what the STB ultimately will have to opine on.

**<Operator >:** Thank you. Next question is from Chris Wetherbee at Citi. Please go ahead.

**<Q – Chris Wetherbee>:** Hey, thanks. Good afternoon, guys. I appreciate that there's a lot of moving parts to this year, certainly. But I was hoping that maybe we could talk a little bit about you've got two fronts, maybe how you see the volume dynamic playing out? Obviously, there's been some challenges outside of your control in 2021, but maybe thoughts around at least maybe the ramp of

volume as we go through 2022?

And then just any thoughts that you may have in terms of operating ratio. I know you gave us some help on some individual line items within the cost, but I guess, I want to get a sense of on a CP stand-alone basis, how you're thinking about OR for 2022?

**<A – Keith Creel>:** Let me...without getting into guidance, I'll give some high level color, and I'll let Nadeem to cover any point that he might want to. But this is the way I see it, Chris. This is a tail of two stories this year. We obviously have pretty tough comps. First half, we don't have grain this year. We had grain last year. We had a unicorn January, the best weather condition in January that I've experienced in my history railroading, in the Canadian railroad as compared to last year. That's not the case this year. So there are some obvious pressures from fluidity, from operating conditions and from a compare standpoint on volumes that we won't benefit from that are headwinds in the first half.

So you could expect RTMs to be down in the first half, but in the second half. And again, what's true in the first turns to a tailwind in the second. We've got weather on our side. We've got very favorable comps. We hope and we anticipate with all that snow that's falling, we're going to see a more normal grain harvest that comes in. The fourth quarter when the new grain starts to move and I think you're going to see autos, some chip shortages that start to normalize and stabilize. So again, with that demand environment, if you go that valley in with grains and with all these other initiatives with these contract wins that John spoken to, that gives us to from a run rate on the second half double-digit RTM growth. So that leads us to positive RTM growth for the year. That leads us to margin improvement for the year that being reaches to positive EPS growth for the year, all on a stand-alone basis.

**<Q – Chris Wetherbee>:** Okay. That's super helpful. Appreciate that.

**<Operator >:** Your next question will be from Jason Seidl at Cowen. Please go ahead.

**<Q – Jason Seidl>:** Thank you, operator. Keith and the team, thanks for taking my call. I wanted to talk a little bit about the intermodal sector. It seems like the way you guys are couching it, it might be more of a back half story as congestion eases. I just want to make sure I'm reading that right. Also, I wanted to see if you guys have seen any inquiries given sort of the vaccine mandate there for cross-border traffic in the trucking industry?

**<A – John Brooks>:** Hey, Jason, this is John. I'll jump in there. I think, certainly, on the international side of the business, we've got a lot of pent-up import demand out there, not only in Vancouver on the water. But – so, I do think it's going to take a little bit of time to grind through that. The good news is that the volumes are nowhere representative of the demand environment as you think about international intermodal for us. Domestically, we've hummed strong. I expect our domestic intermodal franchise to continue to execute. I think you'll see a strong Q1, Q2. And as I said, I think we're expecting another record year for our domestic intermodal franchise in that space.

So, maybe it's a little different between the two. Yeah, probably more of a second half story on international. But I would expect a strong full year in our domestic franchise.

**<Q – Jason Seidl>:** Okay. And regarding the cross-border?

**<A – John Brooks>:** You know what, we were looking at sort of our volume on a few of our train pairs earlier this morning. And we haven't seen a lot of variability yet. I can tell you there's a fair amount of discussion going on with our customers on that front. But I would say we're kind of in a

wait-and-see mode right now in that cross-border.

**<Q – Jason Seidl>:** Okay. I appreciate the time as always, gentlemen.

**<A – John Brooks>:** Yep.

**<Operator >:** Thank you. Your next question will be from Steve Hansen at Raymond James. Please go ahead.

**<Q – Steve Hansen >:** Yes. Thanks, guys, for the time. John, I wanted to circle back on one of your comments on the pet-chem side where you talked about the opportunity on – I think it was both plastics and the ultra-low sulfur diesel opportunity. Your peer has also been talking about this concept of renewable diesel and the big opportunity it might present in the coming years. Is that something that you see also starting to ramp up on your line as well? And just give us some context around that broader step up over time?

**<A – John Brooks>:** Steve, thanks for the question. It definitely is. Not only across Canada as we're working certainly close with the input side with the – whether it be canola oil or other oils, but also on our US franchise as we're looking at opportunities for additional soybean crush on our franchise as feedstock for those opportunities. So I think the easy answer is, yes, we see this as sort of a long-term opportunity for the franchise.

And frankly, if the STB grants control and as we look to the future relative to CP-KC, I think it's a tremendous opportunity as we've got the feedstock in the origin franchise planted in the right spot with the grain customers and potentially the single line haul to get down to the refineries and into the gulf market. So I think, stand-alone, it's a good story for CP. And in the future, CP-KC could provide a pretty good opportunity also.

**<Q – Steve Hansen >:** I appreciate the color. Thanks.

**<A – John Brooks>:** Yep.

**<Operator >:** Thank you. Your next question will be from Brandon Oglenski at Barclays. Please go ahead.

**<Q – Brandon Oglenski>:** Hi. Good afternoon, everyone, and thanks for taking my question. Just a point of clarification. I think I heard earlier that Pat Ottensmeyer and Mike Upchurch were on the call. Is it okay if I ask a question to them on KSU?

**<A – Maeghan Albiston>:** Of course

**<A – Keith Creel>:** Absolutely

**<Q – Brandon Oglenski>:** Yeah. Hey, guys and I apologize, I didn't realize you put out your earnings release until this call, so I'm not that great at multitasking, but it looks like things came in pretty much in line with where maybe we thought it would be, maybe margins a little bit ahead. I guess what can you talk about some of the opportunities and challenges that you see approaching here in 2022 for your network? Appreciate it.

**<A – Michael Upchurch>:** Yes, this is Mike. I'll give you just a quick overview here. I think on the volume and revenue side, we would expect to continue to see nice growth. We believe that all of our segments, with the exception of chemical and really due to the refined product issue, that I think has been well discussed in past, should grow. We have a lot of new facilities on our line, particularly in the steel side of the business. We have Mittal, Ternium, Steel Dynamics, all with major facilities built in the US Gulf Coast or down in Mexico at Pesquería and Lázaro, should see a little bounce back in auto. Grain, I think, looks

really strong with significant growth in the cross-border grain shipments.

We also are really excited about an expansion of the diamond green renewable diesel facility that's going to add some growth. The DRU facility down in Port Arthur should add some growth. So we're pretty excited about the growth opportunities, and that should lead to good volume and revenue growth.

On the cost side, as you know, from our first three quarterly earnings releases we had in 2021, we had some cost challenges. Those are behind us. Really to John Orr's leadership and the entire operating team. Many thanks to them. We really have a network that's running very, very efficiently right now and 2022 is going to be all about continuing to generate productivity on the labor side and around fuel efficiency and continuing to better leverage our equipment and our franchise. So we're pretty excited about those opportunities here in 2022.

**<A – Patrick Ottensmeyer>:** Yes, Brandon, I would just add to that. If you look at the package that we put on our website, look at some of the operating metrics and statistics that we included in that package, including the performance of our grain fleet. So we definitely had some weakness in a couple of the areas that Mike mentioned.

The cross-border refined fuels continues to lag because of some regulatory changes in Mexico. But our service has improved just substantially since the middle of last year. So we are well-positioned. We think we've got good visibility to some of these opportunities coming back, and our network is performing extremely well. And I think we're in great shape to see and take advantage of those growth opportunities when they come back.

**<Q – Brandon Oglenski>:** Thank you.

**<Operator >:** Thank you. Your next question will be from Ken Hoexter at Bank of America. Please go ahead.

**<Q – Ken Hoexter>:** Hey, great. Pat, Keith, congrats on closing the acquisition. Keith, obviously, a lot of cost impacts here. Maybe you can talk a little bit about anything ongoing costs, talk about the restructuring costs and what you plan to spend? I don't know if it's too early for that or maybe just walk us through what we should expect this year in terms of the impact on costs? And then Pat, just coming back to your thoughts there on KCS, any thoughts on the outlook that you're providing for KCS at this time?

**<A – Nadeem Velani>:** Yes. So Ken, it's Nadeem. So I just want to clarify, when you say impact of costs, can you just clarify that?

**<Q – Ken Hoexter>:**Yes. I guess there are two phases. One is on M&A and the second would be any kind of restructuring costs. I guess it's too early until you blend the companies, right? So just a standalone operating, it's just a mathematical example. Is there any other costs we should be aware of in terms of the ownership structure here in 2022? And I guess it's too early to talk about restructuring into 2023.

**<A – Nadeem Velani>:** Yes. No, you're right. It's too early on 2023. But I would say we've talked about this being a growth story. So that's going to be additive to head count over time as we grow the two networks and add on the synergies that we talked about, the $1 billion of synergies, and then some cost savings through IS and finance and some head count, as we talked about their shifting to Kansas City.

But apart from that, in 2022, I talked a little bit about the equity pickup, and we'd have – our net income from KCS would be – would come up through our net income, but there would be some depreciation step-up, about $220 million. And there will be an offset to that of about $40 million of credit for the fair value increase in Kansas City Southern's debt and also an offset of about $55 million credit for deferred taxes. So that's the income statement impact that I'd highlight. So apart from that, nothing as far as cost or restructuring.

**<Q – Ken Hoexter>:** And then, Pat, any thoughts in your outlook, did you provide an outlook, any different than what...

**<A – Patrick Ottensmeyer>:** No

**<Q – Ken Hoexter>:** ... CP is talking about in terms of forecast?

**<A – Patrick Ottensmeyer>:** No. We have not, and we're going to shy away from that at this time, just so many uncertainties about COVID and the impact on workforce and supply chain congestion and chip issues affecting auto and auto-related business and then the future trend in refined products.

We're going to stay away from specific guidance at this point. But as Mike covered and I touched on with our service, I think we see opportunities for some pretty nice productivity gains when volume recoveries occur.

**<Q – Ken Hoexter>:** Okay, great. Thanks for the timing.

**<A – Patrick Ottensmeyer>:** Thanks, Ken.

**<Operator >:** Next question will be from Jon Chappell at Evercore ISI. Please go ahead.

**<Q – Jon Chappell>:** Thank you. Good afternoon. Good timing for the follow-up. Pat, you've touched on just really briefly there, refined products. Obviously, Mexican administration has made a big announcement since we last spoke to you in October on oil dependency or independency, I should say.

Refined product has been such a huge growth silo for you over the last couple of years. I know you're not giving guidance, but how should we think about the Mexican administration's new views on oil and refined products and how that relates to your rail and either growth or maybe even some deceleration there?

**<A – Michael Upchurch>:** Yeah, this is Mike. I'll go ahead and take that one. Obviously, this market has been a terrific opportunity for us, at least through midyear 2021. Then the government really stepped up regulations, inspecting cars because some shippers were illegally labeling the product to avoid excise tax.

And the next step the government took was to inspect and shut down a number of refined product rail terminals that were receiving this product in Mexico. We're beginning to see stabilization in that business, so that's good news. Hard to predict exactly where that's going to take us here in 2022.

But if you think about the overall macro environment here, the demand is still relatively weak in Mexico. Pemex did in 2021 over easy comps in 2020, increased production but really not above 2018 and 2019 levels. So we'll kind of see what their production is for 2022 – but imports have clearly shifted from rail to truck, and that's what's hurt our business, because of the closure of these rail receiving terminals in Mexico.

They've inspected pretty much every terminal in Mexico. The good news is companies are beginning to get approval to continue to be open. So we're optimistic that, that market will stabilize here and hopefully even grow because the macro environment, Pemex is only producing about 1/3 of the overall demand in Mexico.

So the other two-thirds has to come from imports. And that's where we are very hopeful that we'll see a shift back from truck to rail, which is much more economical. And then maybe one final point, Pemex just recently announced acquisition of the Deer Park refinery and they're really looking to ship a lot of fuel, heavy fuel oil, into that facility and then refined product down back into Mexico. So we're going to be ultra-focused on finding a way to work with Pemex to make them successful, both on the shipments north and the refined products back. So hopefully, that gives you a little bit of color on this market. And still, long-term, we believe this is a good growth opportunity for us.

**<Q – Jon Chappell>:** Definitely it does. Thanks for that detail, Mike.

**<Operator >:** Thank you. Your next question will be from Scott Group at Wolfe Research. Please go ahead.

**<Q – Scott Group>:** Hey, thanks. Good afternoon, guys. So, last year, we talked about potential for a 55% OR stand-alone. And obviously, there were a lot of challenges last year. Keith, do you think there's

possible of getting there this year? Or is that more of a 2023 when we get the grain recovery?

**<A – Keith Creel>:** Yeah. Realistically, Scott, without giving you guidance. Obviously, again, tail of two stories, is going to be challenging. Obviously, to get to that level, I see a path to OR improvement. And obviously, if things normalize, we get into 2023 with a normal grain crop. And the benefit of that meaningful volumes, and those outcomes become more achievable, not in 2022.

**<Q – Scott Group>:** Okay. And then can I just ask John just one question. So with the revenue synergy targets, I'm sure there's some bigger, lumpier kinds of contracts that you have in mind. Just directionally, are there a lot of those opportunities in late 2022, 2023 in terms of the bigger contracts in mind?

**<A – John Brooks>:** Yeah, I think so, Scott. As Keith said earlier, we've undertaken a pretty aggressive outreach to the customers in some of those areas that might have lumpier contracts to talk to them about why they need to think about if the STB does grant control that don't miss the opportunity for this new competitive option in the marketplace. And it's been received well.

Scott, so you've got that bucket of opportunities. And I think you got a whole bunch that are out there that this contract timing works well. And as we create a new product, it opens up those opportunities for those customers regardless of their contract status.

And I'll just give you an example, and you probably saw some of this. But most recently, you've had two major Canadian companies announce where they've made acquisitions into the United States and more of the global and North American markets, one being Richardson International and the other one just most recently being Viterra.

And you look at those opportunities, and those are synergies that sort of go above and beyond, but they're totally indicative of what we believe this North American combination can create. And in the desire for some of these companies to invest to be able to help create the opportunity or share in the new routes that this combination creates is powerful. And with those two examples and those are big base customers for CP today that are very excited about what this combination, if we get approval, presents them.

**<Q – Scott Group>:** Helpful. Thank you, guys. Appreciate it.

**<A – Keith Creel>:** Thank you, Scott.

**<Operator >:** Your next question comes from Konark Gupta at Scotiabank. Please go ahead.

**<Q – Konark Gupta>:** Thanks and good afternoon, everyone. Just wanted to come back to the demands from your competitors that you have received so far and potentially will receive from the remaining guys shortly. If in case, Keith, I know you mentioned that you will address all reasonable demands. When you address any reasonable demand from your competitors actually, do you see or anticipate any kind of impact on your stated synergy targets, considering you may be recquired to perhaps divest some sections or let go some lanes. Can you talk a little bit about the impact potentially on synergy targets from those demands?

**<A – Keith Creel>:** Well listen, I'd be speculating, but let me take it back. It has always works best for me. When it comes to significant concessions, the facts don't support it. Specifically divestiture, I know there was one particular railroad our main competitor that suggested they'd love to see us the best along Springfield to Kansas City. But if you get to the fact some of the assumptions that were made in that request or that proposed requests are based on that fact. There's factual errors, there's misstatement.

If you truly get into the details of our filing and understand what our plan calls for, that specific line will grow. It's not going to shrink. It's not an overlapping track. It doesn't go to Chicago. So again, when I think about an unreasonable request, I would say that is, and you can expect this company to vehemently opposed to that and certainly not concede to that, and I don't think as when the facts are heard and the facts are ruled upon that's going to carry the argument for one moment. That's going to be a viable part of our network.

It's part of our single line benefit that this transaction brings uniquely to the table and competition that is introduced. So again, that one, I would say, is very unreasonable, and I'm not concerned on that based on fact. If you get to the other one, if you think about what's been asked for, the NS is asking for additional rights of the Meridien Speedway, which frankly, they're not currently contemplated in the JV agreement. That was an negotiated agreement between the KCS and the NS back in 2006.

So again, if you think about precedence, you view the transaction to gain advantage or to gain a better position that you otherwise wouldn't benefit from, there's precedence around that. There are rules around that. There are laws around that. The BNSF, they are looking for trackage rights South to Laredo and from Clinton Iowa north to Savannah. Again, as that has been as before, these facts don't change or create bad facts. And if it did make sense, then I can't understand how it might make sense now. So again, in the context of the settlement, we'll talk about reasonable asks and reasonable terms and reasonable outcomes as long as it's reasonable for both parties then we can get there. But if it's unreasonable, we're not going to be in a position to agree to it. Our pro-competitive facts don't indicate that we need to.

**<Q – Konak Gupta>:** Great. Appreciate your time. Thank you.

**<Operator >:** Your next question is from Benoit Poirier at Desjardins. Please go ahead.

**<Q – Benoit Poirier>:** Yes. Thank you very much, and good afternoon, everyone. Gentlemen, given the congestion with the West Coast ports, Keith, do you see an increased interest for East Coast ports? And maybe for Pat, do you see an increased interest for Lázaro Cárdenas?

**<A – Keith Creel>:** You know what, all those things speak to a case for all those potential outcomes, Benoit and all those are all things that we're discussing at different stages of discussion with our steamship lines.

The Port of Lázaro, obviously, they're talking direct to KCS about that. But what I know about it from my due diligence is a port built with a ton of capacity, deepwater access. It can complement what's going on at LA/Long Beach but never replace it. But there's certain business cases that they made looking at today's traffic much less considering what nearshoring is going to bring in the future.

But that's a viable port that should uniquely benefit this franchise. KCS today, CPKC in the future, assuming the STB approves our transaction. And the same can be said for Port of Saint John. The Port of Saint John has a tremendous amount of capacity, as the crow flies from tidewater to the key markets. The CP solution is the shortest route. So in our best day, with the capacity as long as they can handle it expeditiously and efficiently through the port, we've got a better product, and that's exactly what we're selling.

And again, when you have these discussions, the beauty of this now and in the future, assuming the STB approves our transaction, we now have three coasts, atriangle that is a powerful solution enabler, supply chain enabler for growth for our customers and for our stakeholders.

And that's all something we continue to be extremely excited about in those messages and the art of the possible -- it's exciting to those customers, too. So I see a perfect marriage coming for growth, and that's exactly why we're pursuing this transaction, and that's exactly why we're excited. There's something in it for everyone here.

Pro competition, pro growth, our employees get better paying jobs, more of those. Our customers, KCS customers, CP customers and customers of tomorrow that neither of us might serve today all have an opportunity to benefit from what this unique transaction brings to the table that otherwise would not be possible, and I believe to be the last major transaction, major combination or merger in the North American continent that will uniquely connect all three countries at a beautiful time in a world where because of all those supply chain challenges, we need a solution like this. So it's extremely compelling and all those conversations are following that narrative. It just makes too much sense at a perfect time in

history.

**<Q – Benoit Poirier>:** That’s great. Thanks, Keith.

**<Operator >:** Thank you. We are now out of time. I would like to turn the call back over to Mr. Keith Creel. Please go ahead.

**<A – Keith Creel>:** Okay. Well listen, let me close by thanking you for your time this afternoon. I can tell you, as we look forward, obviously, we're seized with, number one, running the railroad efficiently, safely for our customers. Throughout this process, we'll be running and participating, completing the merger application process in parallel with planning for integration of these two great companies so that when we do get a favorable outcome from the STB, which we hope for and anticipate, we'll be prepared to hit the ground running day one as seamlessly as possible and start to create all these unique benefits for all of our stakeholders that we've been so proudly talking about. So that's what we'd be focused on the balance of 2022 and we look forward to sharing our second quarter results or first quarter results on the next call. Thank you.

**<Operator:>** Thank you, sir. This does conclude today's conference. You may now disconnect.