Transcript

Q1 2023 Earnings Call

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Canadian Pacific Kansas City Corporate Participants:

Keith Creel – President & Chief Executive Officer
Nadeem Velani – EVP & Chief Financial Officer
John Brooks – EVP & Chief Marketing Officer
Mark Redd – EVP & Chief Operating Officer
James Clements – EVP, Strategic Planning and Technology
Maeghan Albiston – VP Capital Markets

MANAGEMENT DISCUSSION SECTION

Operator

Good afternoon, my name is Raisa, and I will be your conference operator today. At this time, I would like to welcome everyone to CPKC's First Quarter 2023 Conference Call. The slides accompanying today's call are available at investor.cpkcr.com. 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)

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

Maeghan Albiston

Thank you, Raisa. 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 our press release, and in the MD&A filed with Canadian and US regulators. This presentation will also contain 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; John Brooks, Executive Vice President and Chief Marketing Officer; and Mark Redd, Executive Vice President and Chief Operating Officer.

With that I will hand things over to Keith.

Keith Creel

Thanks Maeghan. Listen it's been a journey that we're finally here today. It's an honor to speak for the first time as the CEO of the newly formed CPKC family. It's reflecting the last 11 -- 12 days ago by fast, not that -- we're not quite at the two-week mark since we drove that historic final spike solidifying our combination. But I can tell you the energy and the passion and pride that I'm seeing from employees across this entirely new form network is -- it's energizing. The conviction that I have personally for what this company will deliver for our customers, for our employees, and North American commerce has never been greater.

I'd also like to take a moment to thank and commend the CPKC team on all the work that's been done to this point to ensure a smooth start to integrating these two great companies which, I can tell you is no small feat. We intend for history to show that we integrated successfully. So let me move on to our CP final first quarter results. Most importantly on the safety front, I'm proud that the team has built on last year's record safety performance continuing the strong performance in the first quarter, with FRA personal injuries down 10%, train accidents down an additional 6%. Running a safe and reliable railroad is the key ingredient to what successfully running a PSR operating model is all about and it's something that we take tremendous pride in at CP and now CPKC. On the financial side in the first quarter we produced revenues of $2.3 billion, an operating ratio of 62.9%, and core EPS of $0.90. On the labor front, we continue to make progress with our labor agreements in the quarter. We've ratified recently a collective agreement with the TCRC Maintenance of Way Employees here in Canada. Also ratified negotiated hourly agreement with the SOO-line employees represented by the BLET on the US side as well as several other agreements. And you also noticed in our numbers, we've continued to hire and to train, with headcount up about 10% year-over-year preparing for the volume growth that we expect to deliver.

A couple of comments on the transaction. John is going to talk about it a bit more in a minute, but I am extremely excited about the customer response to the service opportunity CPKC is going to create with our two most recent announcements that we've made this week and last; partnerships with Schneider and Knight Swift are only the beginning. And more to come in June. So with that said, over to you John to provide some color on the markets.

John Brooks

All right, thank you, Keith, and good afternoon everyone. So look, I'm very pleased with our first quarter performance. The volume growth that the team delivered throughout the quarter. While certainly we saw pockets of softer demand, our unique business initiatives served us well and give us momentum as we head into this exciting new chapter of CPKC.

Now looking at the first quarter. I'll speak to the stand-alone CP results for the last time. Total revenues were up 23% on the quarter. Volumes were up 11%, while FX and fuel combined to be a 10% tailwind. The pricing environment continues to be strong with inflation plus renewals across the book of business.

Now taking a closer look at our first quarter revenue performance. I'll speak to the results on a currency-adjusted basis. Grain volumes were up 26% on the quarter, while revenues were up 37%. We saw another strong quarter in Canadian grain, posting our second largest February on record and breaking our January record of 2.3 million metric tons. The strength in Canadian grain was partially offset by softer demand for US grain, corn exports, as well as challenging compares from last year. Looking ahead, although in the first few weeks we've seen challenging crop conditions and grain movements in Canada, with favorable compares relative to last year's crop, I still expect our grain franchise to provide a stable base layer of business as we move through 2023. Finally, although its only in the early days, I'm excited to see a number of new grain flows emerge on the CPKC system with recent movements from the upper Midwest in Canada to markets such as St. Louis, the Gulf, and into Mexico. Further, the CP team is working hard with multiple customers to expand infrastructure development of our industry leading 8,500-foot high efficiency train across the new CPKC network. This network development will enable new grain movements into the South US markets and down into Mexico. On the potash front, volumes were up 10% on the quarter, while revenues increased 22%. We delivered a solid quarter in potash, as we saw volume growth in both export and domestic movements. As I look ahead, although reduced China volumes could impact near term shipments, I continue to expect growth in export potash as Canpotex has effectively expanded its market share across its diversified customer base. And to close out the bulk business, coal volumes were down 2% on the quarter while revenues were up 11%. Despite a modest decline in Q1, I expect to see growth in coal through the remainder of 2023.

Moving on to merchandise, the Energy, Chemicals and Plastics portfolio saw volumes grow 5% and revenue by 13%. Our plastics and LPG portfolios performed well this quarter, driving significant volume growth, along with strong volumes of gasoline moving to our transload and distribution facilities in Ontario. Our Forest products volumes increased 1% while revenues were up 13%. Despite some fears and demand softness in this sector, we worked closely with our customers to find opportunities and deliver record Q1 volumes in Forest products. The Metals, Minerals and Consumer products portfolio grew revenue 23% with a 16% increase in volumes. The strong growth in this book was driven by higher volumes of frac sand and steel year-over-year, as well as continued strong pricing in this carload book. Automotive revenues were up 32%, while volumes were up 18% on the quarter. Demand in automotive remains strong as the industry has moved past part shortages and inventory restocking continues at an accelerated pace. We saw strong performance in our automotive segment as we executed to fill this demand and we also ramped up volumes into our new auto compounds in Edmonton and Bensenville. Now finally on the Intermodal side of the business, quarterly volumes were up 9%, while revenue was up 8%. International intermodal volume led the growth in this space as our self-help wins with CMA, and also growth we are experiencing at the Port of St. John, more than offset softer demand in this segment.

On the domestic side, we saw softer demand for many of our retail and wholesale customers, however, we were able to partially offset this by continued strength in our food segment. And of course as Keith spoke to, you've seen our recent press releases. We are extremely excited about the unique partnerships that we've created with Schneider and Swift, who will ride our new 180/181 train pair that will launch service on May 11th between Chicago and Mexico. I can tell you being at the table with these customers and many others over the months, it's been a lot of hard work to not only understand these customers' needs, but also the multiple interline trials that we've taken place on our network to help refine the single line-haul operating plan that will be, in fact, the fastest service in this marketplace.

So let me close by saying, we're 12 days into CPKC and the team is energized and we're focused on delivering sustainable profitable growth. There is no shortage of opportunities in front of us and my team is staying focused and in lock-step with our operating team to pick the right business partners for CPKC. We are excited to launch new products, we will continue to sign up new customers, and we will build on the success [of] these two historic companies as we move into the future. We are looking forward to showcasing all of these opportunities and many more when we present our commercial playbooks at Investor Day in June.

So with that I'll pass it over to Nadeem.

Nadeem Velani

Alright. Thanks, John. Good afternoon. I am pleased with the results the team produced this quarter and extremely excited about the path ahead for the combined CPKC family. Looking at the quarter, the adjusted operating ratio came in at 62.9%, a 690-basis point improvement from last year's challenging Q1. Taking a closer look at a few items on the expense side, I'll speak to the variances on an FX adjusted basis.

Comp and benefits expense was up $18 million or 4% versus last year. Increased volume, training, and hiring as well as wage inflation were the main drivers of the increase. These were partially offset by lower stock-based compensation expense, and lower current service cost in the DB pension plan resulting from higher discount rates at the end of 2022. Fuel expense increased $38 million or 13% driven by higher volume and a modest year-over-year increase in fuel price versus last year. Materials expense was up 14% or $9 million, driven mostly by increased maintenance activity across the network and cost inflation. Equipment rents were down 19% or $7 million as a result of increased receipts from the use of CP assets by foreign roads. Depreciation expense was $225 million, an increase of $11 million as a result of a higher asset base. Purchased services came in at $334 million, an increase of $35 million or 12% when adjusted for acquisition costs. The main drivers of the increase were lower land sales compared to last year, increased casualty expense, and some third-party cost inflation, including pickup and delivery fuel surcharge cost.

Moving below the line, the equity pickup from KCS in the first quarter was $256 million when adjusted for KCS' acquisition related costs and purchase accounting. Other components of net periodic benefit recovery decreased $15 million, reflecting higher discount rates compared to 2022. Net interest expense decreased by $6 million versus last year as a result of increased interest income and a lower debt balance. Income tax expense increased to $78 million reflecting higher income. Excluding KCS related items, the effective tax rate was approximately 24.5% on the quarter. Following the close of merger with KCS, we expect the CPKC effective tax rate to be approximately 25.5% in 2023. Rounding out the income statement, core adjusted EPS was $0.90 in the quarter, 34% higher when compared to last year. We continue to generate strong cash flow with cash provided by operating activities of $881 million in Q1, an increase of 44% versus the first quarter of 2022. Our first call on capital remains the business, and in the quarter we reinvested just over $400 million. In the first quarter, we received the final dividend from KCS totaling CAD300 million which we used to continue to de-lever our balance sheet, paying down close to

$490 million of debt in the first quarter. You will also see that following the end of the quarter, we successfully completed the debt exchange that we launched in March replacing seven KCS notes with CPRC notes on the same financial terms. Additionally, in April, we purchased and subsequently irrevocably deposited approximately $650 million in government securities that satisfied a discharge the 2023 KCS notes that were maturing in May and November. Our combined leverage is down to 3.6 times on our path back to our target leverage of 2.5 times net debt to adjusted EBITDA. Inclusive of the KCS dividend, we generated $495 million in free cash flow on the quarter. While it's been a long path to get to this point, when I look at the opportunity set in front of us, it's certainly been worth it. We're at a historic point in this industry and with a unique story to tell. I look forward to providing you a more fulsome update [at] our Investor Day at the end of June. With that I will turn it back over to Keith, to wrap things up.

Keith Creel

Thanks, Nadeem. I'll tell you -- before we open up for questions, I can tell you this is my 31st year of railroading, I've never been more excited about the path that this newly formed company creates for our employees, for our communities, for shareholders of the commerce in North America. We look forward to showcasing how we're going to start that journey in June when we all come together. But for now, let's open it up for questions on our first quarter results. Go ahead, operator.

Question & Answer

<Operator >: Thank you. (Operator Instructions) Our first question comes from Fadi Chamoun with BMO. Your line is open.

<Q – Fadi Chamoun>: Good afternoon, everyone, and congrats team on closing this transaction. It's very exciting, but I have a couple of quick things, first John, can you give us an estimate of what the revenue synergies that you're expecting from Schneider and Knight out of the gate just some – I'm guessing some loads are going to transfer to the CP network out of the gate and then ultimately you're anchoring these customers to grow faster after, but what does that look like and Keith you mentioned the integration in your remark. And I just wanted to get your thoughts that this is not kind of an overlapping network and probably it doesn't have the same challenges we've seen with prior mergers. But what are you focused on in terms of a key aspect of this integration to ensure it goes smoothly. Is it technology, is it people alignment, if you can give us an idea about what is your key focus to ensure that this is going to go smoothly going forward.

<A – Keith Creel>: Well, let me take -- welcome back Fadi, it's a been a while since we've been able to speak to you on these calls, so, glad to have you back on the call. Let me start with the integration piece. This is a process -- an issue itself, it doesn't have a really good history in our industry and we've known that going into it. In my railroading time I've lived through some integration, and history shows did not go well and I've participated in some that have. So with that said, I can tell you we did not underestimate the magnitude of this. This team has been hard at work with our counterparts at the KCS when they're in trust focused on integration.

So we integrate well because the last thing we need to do obviously is not provide safe and efficient service for our customers as we bring the two roads together, so we hit the ground running. We have an integration management office that I chair, that we've created the last nine months. We have a cadence, we meet every couple of weeks, we have integration champions, we've broken down our disciplines in our business into eight different groupings, those are full-time assets committed to that, and I think over 168 processes that we have active plans against that all defined integration from the way we pay employees, to the way we work with our customers, to the way we manage the real estate.

Everything is covered, for the lack of a better term. So very thought out very disciplined approach. So we triggered that obviously day one, we had a day minus 30 countdown. We had a day one hit the ground running. But I can tell you this, we were all in Kansas City on day one. We decided that we're going to celebrate the historic day that it was in railroading history, I think it warranted that. So we celebrated in a very -- I think reflective positive way. And then we went to work, and we've been there ever since. I've been there every week except this, obviously I'm in Calgary this week, but I'm going right back there next week. John Brooks is located there now. Our Chief Operating Officer, Mark Redd, is located there. My US office will be there and I'm going to be there 75% to 80% of my time, focused on most importantly, culture, to make sure that we bring these two cultures together.

I have said from the beginning, they're very similar cultures, very like-minded people that are customer focused that love railroading that quite frankly CP and KCS had been the smallest for a long time. We now have a level playing field, we have a franchise and a network that I believe will become the most relevant in North America and it's fun to come to work. We just got to make sure that we integrate well, we lay the business on correctly, we don't oversubscribe the network, and we sequence the business with these opportunities so that we can deliver the service in a safe and efficient manner as we've committed to. So that's what my attention is on. That's what it's going to be on for the next six, eight, 12 months -- next year. The following year. We're going to stick with this thing to get it right because there's one thing I am committed to and that's history reflecting that we've done what we said we're going to do, its reflected well on us and it's reflected well on those who trusted us to bring these two great companies together, be it board members, be it shareholders, be it regulators, be it the communities we operate in and through.

<A – John Brooks>: Welcome back, Fadi, it is John here. So, look, we are super excited about having Schneider and Knight Swift part of the CPKC team here. I can tell you; we worked hard as I've said previously, really for two years really finding the right partners that can best utilize our capacity and service in this marketplace. We're excited – Schneider, over 30 years of experience of operations in Mexico. The Knight Swift team, very excited about the compelling value proposition that a single line-haul will bring from Canada, US, and into Mexico.

I'll tell you both of those shippers are going to be on the doorstep of our terminals day one, May 11th, they will be on that train and bringing volume and synergies to the new CPKC. We will ramp that business up, but you should expect it to be $100 million plus line of business for us and that's just the start of filling that train, Fadi. So, I can tell you there's going to be some more exciting announcements on the horizon in markets that not only deliver and can utilize best our service -- this intermodal service, but most importantly take trucks off the road. We have been very focused on opportunities that can capitalize on the 60% to -- up to 75% greenhouse gas emission savings that this service is going to bring when you compare it against an over-the-road truck heading down from Chicago down to Laredo and into Mexico. I will tell you this, as much as it's been a long sales cycle in educating of what the power of what this network can do, I can also tell you these customers are excited and compelled with the capacity that we offer. It's been a tough couple of years of railroading for the industry and a lot of these customers are ready for a differentiator, and I truly believe come May 11th that's what this service will bring.

<Q – Fadi Chamoun>: Great, thank you.

<Operator >: Your next question comes from Ben Nolan with Stifel. Your line is open.

<Q – Ben Nolan>: Yeah, thanks. I guess my question really is, we heard from your competitor in Canada that they are expecting or already seeing a recession in their numbers -- haven't seen in yours and even so far in April haven't seen in yours. Are you guys under the impression or are you seeing recessionary environment or is this just something where you're finding other ways to supplement your volumes despite what may actually be recession?

<A – Keith Creel>: I'll let John provide a bit of color, but as we said from the beginning, we have a very unique story in this industry and this combination only makes it even more unique. We're not recession-proof, obviously if the macro was bad enough anybody could be impacted, but I can tell you we have some very unique recession insulators that no other rail network has in North America.

<A – John Brooks>: So I would say, Ben, we definitely -- we're not completely immune to it in some of the sectors. In the international intermodal space certainly the volumes through all the ports in North America are down. To your point, this is a self-help area. We've been aggressive, we've been able to grow, we've been able to find some customers that wanted to shift the business to our best-in-class service out of Vancouver with CMA. You're familiar we've had a ton of success out of the Port of St. John in growing that business and I'm actually -- I'm very excited Hapag started up a new service with our alliance partners here a few weeks ago through the port.

So albeit that area is being hit by volume pressures and we've been insulated by it. I would call out, not only the KCS network, but also most recently our network, so domestic intermodal area has felt pressures. We're seeing quite an imbalance of our flows with maybe decent demand west-bound, but certainly, demand degradation if you think about the eastbound flows. So, we're not immune in those areas, but I think to Keith's point, there are self-help initiatives that are helping keep us float a little better. Obviously CPKC and these synergies and -- every day my expectation and my team reports out to me where we're at in converting some of these business opportunities, and again regardless what the macro does in the coming months there's going to be an opportunity for us to buck some of those trends as we continue to layer on some of these opportunities on the new CPKC network.

<Q – Ben Nolan>: All right. Appreciate it, thanks.

<Operator >: Your next question comes from Walter Spracklin with RBC Capital Markets. Your line is open.

<Q – Walter Spracklin>: Yes, thanks very much operator and thank you for taking my call -- my question. Really want to come back to Schneider but look at it little more conceptually. I think Schneider was an example of where KCS had to kind of interchange with UP to bring it to Chicago and converting that over to a single line now makes a lot of sense and is – I don't want to call it an easy win, but it's certainly a very attractive proposition to that customer. Can you bench -- or can you ballpark for us how much more in revenue dollars is out there where KCS was interchanging with a partner that you can now deliver a single line service to and perhaps get some easy proposition wins right out of the gate along those same lines?

<A – John Brooks>: Yeah, Walter. So, you're kind of getting in the weeds a little bit on me here, I can tell you there is a compelling opportunity there. I think you've hit the nail on the head. We are going to speak very specific to those conversion opportunities and that on our Investor Day. So I can't go into a lot of details there. I will tell you this though, certainly I think what you described extending that haul and in -- that single line-haul value proposition was important to Schneider, and that reliability of capacity and service. But again I'm going to point more to as much of that story is about that, it's about taking trucks off the road, and if you look at the value proposition we're going to create in terms of Laredo to Chicago on the third day delivery and into Monterrey and a fourth day delivery and down into Mexico City on a fifth day delivery, it's competitive with truck over the road. And as much as again Schneider and Knight Swift saw the value prop to stay on one railroad and use that the single line-haul advantage, they saw the opportunity to make headway on our own greenhouse gas emission savings opportunities with our own truck fleets and to go after some of those pieces of the business that I think the rail sector has long sought to get after but just haven't been able to demonstrate the service to really compete. So -- but we'll get into those details also as part of our Investor Day story.

<A – Keith Creel>: Yeah, I want to add a little color to that Walter. I think about this and talking to Schneider and Swift, both, you think about what this enables. You think about asking them that same question; what freight do their competitors all over the road today that this service reliability and this single line reach into Mexico, be it going south be it going north, gives them to be able to go compete for. So there's revenue out there that's moving across the road that's not moving in a Schneider vehicle, that's not moving currently in a Swift that's going to be able to be competitive for them to bring to our rail network in partnership with us to get it into Mexico and to get it out of Mexico. So there is such -- I would call maybe the conversion, just the tip of the iceberg for the lack of a better term, it's what we don't know yet that excites me so much. And once we put this product in the marketplace, it's not spin, it's not rhetoric, it's truly best in class service connecting it seamlessly, Chicago to Mexico and Mexico to Chicago and those locations in between, that's a game changer. It's a new market, it's markets we don't know about, it's markets that we're going to enjoy uniquely with the people that partner with us and I'm super encouraged that Schneider and Swift see the value in that.

<Q – Walter Spracklin>: That's fantastic color. Look forward to hearing more about it in June. Thanks everyone.

<Operator >: Our next question comes from Konark Gupta with Scotia Capital. Your line is open.

<Q – Konark Gupta>: Thanks, operator. Good afternoon, everyone, and I echo my congrats on this historic moment. I just wanted to dig into these intermodal contracts with Schneider and Knight Swift once more. My understanding is your line, single line, between Tex Mex and Chicago is probably a little bit longer in terms of mileage compared to your competitors on the vessels to -- how fast you are getting service faster there compared to those guys. I mean are you making any significant changes in the way you operate or strengthen that route?

<A – Keith Creel>: I think it just kind of boils down to the way we execute versus the alternative. And again as follows, we're not surprised that our combination surprised -- triggered competition. We said from the very beginning this combination would create new competition. It's going to create new options for shippers and that's exactly what this is. So that announcement that was made this Falcon Express or premium service that I heard about yesterday -- complement my friends in Montreal, they finally validated our case for consolidation. We knew it from the beginning, the facts would support and I think history is going to show the STB got this right because of this very specific issue, but then you get to -- it's ironic, I was sitting in the same seat two years ago and I made a comment that the facts matters. So let me explain to you, just because it might be a shorter distance, if you don't convert it does it really make the difference. So speaking the facts, getting from Chicago to Salinas Victoria, which is the CPKC ramp that serves the Monterrey market, yes it's true that the Falcon service is 194 miles shorter, however the reality is we delivered in four days and we run a 194 miles longer versus their advertised 5.9. So we're beating them two days to the market. Now let's go closer to Mexico City into Porto, which is our CPKC terminal versus the FXE Silao terminal that's advertised with the Falcon service, and actually there it's 76 miles shorter via the CPKC network because what happens in US where UP enjoys as the crow flies a shorter length of haul, it's the reverse to these same markets when you get across the border in Mexico. CPKC calls that back, but from a service standard from what we deliver to the customer is 4.6 days on the CPKC 180/181 service versus this premium service that I heard yesterday aspirationally was untouchable at 7.9. So perhaps it is today, but on May 11th, it's going to be touched with a much superior service. So again, the facts matter, rhetoric, spin. We're just people of fact here, and people of truth, we're about to launch a train service that's unparalleled in this industry and those that partner with us are going to be winners in this game of service reliability, they're going to be winners in the game of serving our environment, taking trucks off the road and making everything we said to be true about this perfect combination fact-based truth, not rhetoric, not spin, history is going to show that. So we're ready to compete, ready to get after it.

<Q – Konark Gupta>: That's great color, Keith. Thank you so much.

<A – Keith Creel>: I'll let you know tomorrow what we're going to name it, it won't be Falcon and we're going to come up with something that truly exemplifies the superior service that this is.

<Q – Konark Gupta>: Okay, thanks.

<Operator >: Our next question comes from Chris Wetherbee with Citigroup. Your line is open.

<Q – Chris Wetherbee>: Hey, thanks, good afternoon guys. Keith, understanding that you guys have obviously had oversight of KCS for a while now. With operational control, I guess just kind of curious how you're thinking about sort of sequencing the next either couple of days, weeks, months, however you think about it in terms of things you can kind of get going operationally or from a cost perspective or otherwise, kind of right out of the gate. It would seem that there could be some changes now that we're past that April 14th date, just curious how you're thinking about that.

<A – Keith Creel>: Yeah let me say this, Chris, there was a lot of thought and planning ahead of time and the guy that is responsible for executing that are our COO, Mark Redd, is here and I'm going to let him speak to that.

<A – Mark Redd>: Yes thanks Keith, and Chris thanks for the question. It really mulls around Mexico US operations on KCS and what we're doing is -- it's pretty much aligned. We've got a leadership in place, the metrics and Mexico are starting to stabilize a bit now, we're building on the improvements that the team had in place just prior to control and what we'll focus on is really just back to basics. You'll look at our PSR metrics, we'll make sure that our current fleets are leaned out in both areas, both railroads. We will look at focus around dwell, speed, yard speed, locomotive optimization in the yards and also just inventory reviews. So we're just -- just get the number two pencil out and just start railroading and stay focused on just the metrics themselves, but also just getting into the details of how we railroad on CP.

<A – Keith Creel>: I think, Chris, the other point that I commend Mark on is from right out of the gate, day one, it's about cross-pollinating, it's about best practices as well. We've got some of KCS' talent, Tim Livingston has moved to St Paul, so he is on the former CP network. We've got Tracy Miller who is in St Paul, that's down in Shreveport. We got Mark [indiscernible], who is a very talented Operating Officer at Canadian Pacific, in Shreveport as well. So Mark went through a very methodical, well thought out plan to make sure that we've got an opportunity to drive change on both networks to create a better outcome for CPKC. So they're well into it. I'm encouraged with the progress, they hit the ground running. And we're going to accelerate.

<Q – Chris Wetherbee>: That's helpful, thanks very much. Appreciate it.

<Operator >: Our next question comes from Jon Chappell with Evercore ISI. Your line is open.

<Q – Jon Chappell>: Thank you. Good afternoon. Keith, I want to tie a couple of things together from a little bit earlier. I mean on the integration, it's very clear you don't want to take on more than you can chew as to maybe bottleneck things in the early stages, but it does sound anecdotally like there's a ton of business, maybe more than you are ready to take, that wants to come to you on day one or day 60. So how do you kind of manage what freight you're taking in the early stages of the integration and knowing that there's probably more demand than you have capacity for today, how do you think about pricing for that?

<A – Keith Creel>: Well, the reality is the way we manage it is the way we've managed our business [indiscernible] CP for the last five, six years. Mike Foran is key to that relative to our modeling. We've got John on the marketing side with the opportunities, we got Mark on the operating side with the execution and they've got to deal with me in the middle. So we are very well, all of us, connected, to help assessing these opportunities, sequencing this business. I'm not going to allow this network to get oversold. So as much as -- if we could, we would take it all tomorrow, we can't and we will not.

The last thing I'm going to do is disappoint the customers that I have an obligation to today. Be they former CP, be they former KCS, and especially those that we're starting to partner with. So we've got a commitment and obligation to Knight Swift, as well as to Schneider, to bring them on the right way. We're going to launch this train each way. It's going to be seven day a week service, that's what we're going to start and then we're going to see what's next. And all the while we're doing our infrastructure work. We're continuing to build out our sidings, we're continuing to execute the merger plan that we gave the STB, again, so that we could be men and women of our word, and every bit of that was thought out and sequenced in line with these business opportunities.

So we're not going to get ahead of our skis, we're going to be methodical about this. I think our customers, as much as they would love the benefits of this network tomorrow, I think they would much rather appreciate our honestly and say, not yet, we're not ready yet, than we just bring them on and we fail them. We're going to get one kick at the can. We're going to make this thing right. And we're not going to fail by letting our aggressiveness and our want for revenue over-subscribe our ability to execute, that's just not what true PSR is about. We've got to make sure the network can handle the business to be able to execute our operating model and that's exactly what we're going to do.

<A – John Brooks>: Jon, I might add just a little more color to that. It's John Brooks. Day one in Kansas City I got the entire sales and marketing team in a room together and spent a full two hours plus just talking around expectations and how we want to grow this network. And I can tell you the excitement to just sell, sell, sell was impressive. It made me excited, but to Keith's point there was also a lot of temperament around we're going to sell to the right customers. We're going to look at those opportunities that can really value our capacity and our service.

We're going to work closely with Mark and the operating team and I can tell you we have a very distinct process that we've used at CP with Mike Foran, that any sort of incremental business that we consider to bring on the network, we make sure it fits our trains and ultimately what we sell, we can deliver to the customer and we layered that process under the KCS network. I guess that would have been about hour 40 of control. So, I'm quite comfortable that the team understands this mandate. They are like thoroughbreds though; I've got to hold them back. But nonetheless, we're not going to oversell this network as Keith said.

<Q – Jon Chappell>: I appreciate that. Thanks, John. Thanks, Keith.

<Operator >: Your next question comes from Scott Group with Wolfe Research. Your line is open.

<Q – Scott Group>: Hey, thanks. Good afternoon guys. So I know we'll get the longer-term guidance in June, so I'll stick a little bit shorter-term this quarter. Any thoughts, color, on how to think about Q2 from a RTM, revenue, operating ratio standpoint and then either core CP or now consolidated, however you want to think about it? And then John, any color on price mix of plus 1% and some of the puts and takes there. Thank you, guys.

<A – Nadeem Velani>: Hey, Scott. Just a couple more months of patience we ask from you then we will give you some -- promise we'll give you some color. And I think John gave you some insight into what we're seeing as far as the near-term volume outlook. Some of the headwinds. Some of the opportunities and we've been reporting our April RTM. So let me just leave it at that Scott.

<A – John Brooks>: Scott, I think a lot of the challenges in April that the other roads have identified, we're not completely immune to those by no means, but I can tell you, you look at the numbers we have fared a little better. And again, I do think we've got some upside as we'll continue to layer on these synergies. On the pricing front, I continue to be pleased with our performance. Contract renewals, I'm going to say mid to high single digits, we continue on that pace.

Mix has shifted a little bit negative on us as we've seen a bigger part of our bulk franchise move and naturally with that sort of longer-haul business you begin to feel a little bit of mix shift negative. I don't see that being that alarming of an issue as I look forward, a little bit of headwind in other freight on the accessorials. But again, I would say, smaller relative to the others in the industry and we actually view that as a benefit as CP as we begin to see operating upside in our terminals as a result of some of that lack of congestion related to the accessorials. That's it.

<Q – Scott Group>: Thank you, guys.

<Operator >: Our next question comes from Tom Wadewitz with UBS. Your line is open.

<Q – Tom Wadewitz>: Yes. Good afternoon and congratulations on the skill and persistence in getting this deal done and approved. Wanted to ask you, I was just thinking about operating changes and some things that have been done in the past. It's probably not a good analogy, but I think 10 years ago CP was doing something called whiteboarding and the idea that you were just reconfiguring the flow of traffic on the system. Is there an exercise like that, is there a process like that, that eventually will take place for CP-KSU and what might be the timing? And I guess if not should be better to think about it as you're really just adding train starts as you bring on new business. Thank you.

<A – Keith Creel>: Tom there, I mean that's part of the way we do business. We still whiteboard on the former CP network. So it's just part of our discipline, part of the rhythm of making a plan, executing the plan, stress testing the plan, adjusting and tweaking the plan. So as the ebbs and flows of business occur, it's never going to be static or shouldn't be static unless we're not growing or we're shrinking. And then we still have a responsibility to adjust.

So I can tell you that John Orr did quite a bit of whiteboarding himself when the company was in trust. Mark and his team are going to build upon that. There's always something that a new set of eyes and ears will see and hear that perhaps the previous didn't. That's true about me, that's true about Mark, but that's definitely part of his play book that he'll be executing with his leadership team and that's part of when you talk about cross-pollinating, when I talk about bringing Tim Livingston and his abilities and skill sets to leadership impact into St. Paul, and then we've taken Tracy Miller where Tim Livingston is. It's kind of a replication of that. Both of those gentlemen will see things the other didn't and it's nothing to be ashamed of, it's nothing to apologize for. To me it's something to celebrate because it creates new opportunities for us.

So whiteboarding in railroading, that way, that is what PSR is. That's a key ingredient to it and it will be part of our DNA as long as I have anything to do with this railroad or anything to do with the people that run this railroad when I'm gone.

<A – Mark Redd>: The add I would have with that is really May the 8th we'll bring the KCS team up to Calgary and we'll have that alignment meeting, we'll talk about what good looks like. We'll talk about the standards and expectations. That's what we'll glean out of the conversations. We will make sure that we time every job that we have, the connections, understand what freight goes where and just align ourselves on what good looks like.

<A – Keith Creel>: Tom, also --. Yeah, go ahead. I'm sorry.

<Q – Tom Wadewitz>: Yes, I'm sorry, I was just going to say. So we should think of it is more a process not like in some of the PSR stuff in the past, you do a lot of work to plan a new schedule and then you implement broadly the new schedule. But it sounds like this is more of a process and a gradual thing than a point in time where there is a big change to the schedule.

<A – Keith Creel>: Yeah, the schedule itself, the service design teams did a phenomenal job having it ready to go day one. So literally, to say that we had a system schedule day one is unparalleled. I don't know that any railroad has ever been able to do that. So there was a lot of pre-work into that so we could hit the ground running. But it's these whiteboarding [indiscernible] you go out any stress test that schedule. You make sure that the local jobs are right, you make sure the road performance is right. You make sure the stops and the times you switch your customers are correct and you're properly resourced to optimize that plan. And I can tell you, I'll give you a case in point. I walked in Mark's office this morning and we got to a discussion about inspecting locomotives and listen, they're good railroaders but we do a little bit different. It's about best practices. Why don't you provide more color about this, the conversation you had with the train master in Wylie this morning?

<A – Mark Redd>: Yea, so actually I was -- I don't know, probably midnight last night, talking to the train master in Wylie, Texas. And what I noticed was just the detail I'm asking for and he actually had a crew come on duty, walk through the locomotive, but also hear that we had a mechanical inspection as well. So during that I learned that we spend about 20 minutes walking the locomotives, make sure they're set up right, make sure the hand brakes are off and the mechanical person just went through it.

So all I've asked for now let's get a card on the lead engine that's a job briefing card that says this engine has been signed off by Joe or Jane or whoever the mechanical person is, so when the engineer gets on the locomotive they can just leave. They don't have to do a brake test. They don't have to do all that whole nine yards; they can just leave. And just that alone will save 15-20 minutes to every start that comes out of a shop facility and you just multiply that by 365 times a year and think about how much time we'd just save.

<A – Keith Creel>: And Tom, I don't want that to be misinterpreted. You've got a qualified, certified mechanic that's been trained and is an expert at inspecting and servicing that locomotive that signs off on it and they hand it off to the locomotive engineer, who is a trained expert at operating it safely. If that qualified mechanical employee was not there, then of course, the engineer would do that work. The work has to be done. This isn't talking about eliminating work that needs to be done to run a safe efficient railroad. This is talking about eliminating redundancy so that we can convert it to productivity and that locomotive can get moving across the railway, so that we can drive locomotive productivity, so that we can drive service reliability, so that we can take those trains and those cars -- additional car miles per car day. That's what it's all about, it's about optimizing the processes. Not eliminating necessary components of the process.

<Q – Tom Wadewitz>: Great, thanks for the time. Appreciate it.

<Operator >: Your next question comes from Ari Rosa with Credit Suisse. Your line is open.

<Q – Ari Rosa>: Hey, good afternoon, and I'll just echo everyone else in congratulating you on a historic combination here. Keith, it did seem like KCS had a number of operating challenges leading into the closing of the merger. Just wanted to understand what accounted for some of those issues from your perspective and what does the timeline look like to fix those issues? Thanks.

<A – Keith Creel>: The fixes again, I would suggest that John and the team did quite a bit leading up to, to stabilize the metrics and I believe a lot of the deterioration was in Mexico specifically. The US operation was running quite well. On the Mexican front, though, there was some congestion down in Mexico, there were some challenges with labor availability. John, and the team are working hard to address the labor opportunity to communicate to our employees that are in Mexico that listen they are a key piece to this. Now those employees in Mexico and the growth that Mexico can enable, they are success enablers.

And part of that getting out and making sure that they understand that, is part of valuing the hearts and minds of your employees and John's about doing that, Mark is about doing that. I've been down to Mexico myself, I went down, I have done town halls in Mexico City twice. I went down just before control date, I guess it was maybe the day before or two days before, did a town hall in Monterrey and I can tell you those employees down there have energy, they're engaged. They feel like they're part of something I'm going to make sure that they know how important they are to that something. We're creating something special. And I think all that matters. I think as we progress this and educate those employees and they feel like they're part of this, not just the officers but most importantly -- equal importance are the men and women that operate the trains. And quite frankly, I think there's a big opportunity to do that to make sure they understand the opportunity that's before them and how important this is not only for Mexico and for their families, but for the North American continent, and I think that's going to be a game changer. So you should expect to see that performance improve.

The things that Mark's doing today with the team. Taking it to the next level. Building upon that work. Taking cars out of service that are just sitting there, dwelling, that are taking up valuable space that some are eating us up in car hire, getting it back to the railroads they belong to, leaning our fleets out so that we can be more efficient, and turn our fleets and reduce dwells in yards that's all about dots and the size of the intricate nature of running a PSR railroad is about, it's about getting into the details, and that's what we're about doing. And as we do that the performance will continue to improve.

<Q – Ari Rosa>: Thanks for those thoughts, Keith.

<A – Keith Creel>: Thank you.

<Operator >: Our next question comes from Brandon Oglenski with Deutsche Bank. Your line is open.

<Q – Brandon Oglenski>: Hi, this is Brandon from Barclays not Deutsche. But Keith and team, congrats as well. Keith, you did mention culture I think the first question on your prepared remarks as being the most important here. How are you aligning management incentives along these lines, especially coming off that last question about the operational challenges that have been pretty much existing for a while now, south of the border? Thank you.

<A – Keith Creel>: That's a great question and I will tell you it's not lost on me. I'm a person that believes in working hard, but I'm also a person that believes when you create value you should share that value. So something we've done as far as officer compensation we are implementing a more CP-like compensation model. So the KCS had a different program, the KCS obviously they've been in trust, they couldn’t issue equity. All those things that create value. Now we're going deeper in the organization.

The other thing we did and I was proud to announce day one, we're creating more shareholders. I want more owners in the company. The former KCS employees obviously have not been able to enjoy and participate in a share purchase program for quite some time. And in fact 100% of the CP employees were not participating in our program as well. Well day one CPKC we announced 100% of all employees on the US side or the Canadian side could participate in CPKC share purchase program. So that went into effect. Since then, on the KCS side, we've seen in 10 days, 20% of their employees have signed up and registered for that. So that kind of tells you and I believe in this, they're going to create the value they should enjoy the value. And as owners, I think they behave differently and perform differently than if they're not owners.

On the sales side too something that's very CP-like, we're introducing the sales incentive plan. So the sales force that are going to go out and sell this product, they're going to be motivated to meet and exceed their budgets and they'll be rewarded handsomely for doing that. So we're trying to sweep out all the corners. We're not trying to boil the ocean, but at the same time create some CPKC-like motivational compensation measures that are there to make sure that our employees' interests are aligned with our shareholders' interests. That we can get at creating this value faster not slower.

<Q – Brandon Oglenski>: Thank you, Keith.

<A – Keith Creel>: Thank you.

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

<Q – Amit Mehrotra>: Thanks. Nadeem can you just give us a sense of any expectations around RTM growth this year? I know there's just a lot of moving parts, macro, grain and then obviously some of these new business wins which are great. But any sense of RTM growth this year? And then just another topic on synergies, I assume you will update the synergies at the end of June, but there's obviously a volume component to synergies and a pricing component to synergies and pricing is up a lot over the last couple of years. And so I'm wondering if you could just kind of give us a sense of if you mark the pricing to market kind of where the synergies would be relative to when you first get them out. Thank you.

<A – Nadeem Velani>: Sure. So I'd say we're still, being 12 days, we're still evaluating their plan, incorporating that into our view and then obviously, as you know, it's a pretty volatile macro right now. So for me to give you an RTM outlook for the rest of the year is not going to happen. I think we'll update, as I mentioned to Scott earlier, we'll update in a couple of months at the Investor Day and a lot more visibility into the details of their plan. And then as we go through our whiteboard process and so forth -- and I'd say recall our whiteboard process isn't just on the operating side, it's also meaningfully on the revenue side, and so we spent some time this week with John and some of his sales and marketing teams, some of my financial planning team, our costing team and et cetera to look at some of the revenue contracts and opportunities that are in front of us and that we've inherited. So I think that's an important point, it's all on the whiteboarding.

So we will get back to you in terms of revenue outlook for 2023 when we meet in a couple of months, give you a sense of what the second half of the year looks like. At that same time, we'll also give you a longer-term view in that three to five-year type of time frame and we'll give you visibility into what the synergy outlook looks like in terms of execution so we've given you some visibility near term. John mentioned there's going to be more that come out between then and now, but I think at that Investor Day, a big part of it is going to be visibility to the synergies that we laid out as part of the acquisition and part of the application and give you more color.

As far as the pricing environment, yes, it's certainly from the two and a half years ago and we answered the process of acquisition that pricing environment changed meaningfully and that should be an opportunity as far as the overall revenue outlook. And so what we've said consistently over the last few years is the size of the pie is probably larger. We're in a mix of a challenging macro environment, but I would expect that the size of the pie is going to result in [indiscernible] synergies than what we've outlined. It might take a little bit longer to realize, it might take -- and that's why we're going to give you a longer outlook as well on how we're going to execute that.

<Q – Amit Mehrotra>: Great. Okay, very helpful. Thank you very much.

<Operator >: Our next question comes from Ken Hoexter with Bank of America. Your line is open.

<Q – Ken Hoexter>: Hey, great. Good afternoon and congrats on closing CPKC as well. I'm certainly not a fan, but I think the Patriots beat the Falcons so maybe -- but I think Patriot rail was taken. Just watching from afar I guess now that you're under the hood, Amit just asked about the synergies, maybe go on the other side, are there some bigger projects where it might take a bit longer now that you look through it and you've been at this for a while, whether it's software. I remember when UP and SP merged the network almost came to a standstill and I know you don't have those issues, but are there some major projects that might take a little longer that you can maybe walk us through, Keith?

<A – Keith Creel>: You know what, I've got James Clements, he is our expert in that space. I'm going to get him to speak to that but before I turn it over, I can't resist commenting. We can't be Patriots. We've got to be [indiscernible] chiefs.

<Q – Ken Hoexter>: Trust me Keith, I'm not a Patriots fan. I'm a New Yorker.

<A – James Clements>: Thanks, Keith. Thanks, Ken. Its James Clements, I'm Executive Vice President, Strategic Planning and Technology. And when you look at the integration, what we said to the STB is that we were going to go through a very measured approach, we were going to make sure that we tested everything before we launched it and put it in place. And day one we certainly did launch some important tools. As Keith mentioned, we have the integrated operating plan that's now running for the combined entity.

We've provided operational visibility to Mark and the team so that they can understand how the entire network is running and we've also provided the information needed for the finance team to do their work and have their data. And that was our first step. We have a longer road map, we will talk a little bit about it at Investor Day as well, but the big real one platform systems integration, whether it's what we're doing with SAP, what we're doing with our operating systems is more in that two plus year timeframe. But in between, we will have incremental releases of different tools. Our carbon calculator as an example, isn't integrated today, we see that coming in Q2 of this year as one piece. So we have a long road map and a very comprehensive plan and we're taking that measured approach so that we live up to the promises we made to the STB.

<Q – Ken Hoexter>: So with that -- just to clarify that process for SAP or something like that, does that change your timeframe on synergies, I know Nadeem just threw out maybe some of that might be longer.

<A – James Clements>: No, absolutely not. As an example, when you talk about the operating side, the visibility we have created we did it on day one so that Mark and team would have the ability to start asking those questions, drilling down into the operation and converting the opportunities that they can see. So we've given them those tools on day one and they'll just get better and better and they will be part of that ramp on the synergies.

<A – Nadeem Velani>: And Ken, just to clarify, when I say it's going to be longer I mean when we first assessed this we gave a three-year view of when we were going to achieve our synergies and I'd say that we kind of did a split of a third, a third, a third. We think the pie is -- we've consistently said, we think the pie is bigger. I'm just saying that we're not going to get the bigger pie in that three years. So this isn't going to be a three-year story. This is going to be an extended story and a larger one of delivering greater synergies. And to Keith's point, we're not going to put our network at risk by trying to do everything all at once. We're going to take a measured approach and provide the best service in the industry that we're used to providing and do that and take on business in a sustainable profitable way.

<Q – Ken Hoexter>: Great. Keith, James, Nadeem thanks for the tine. Appreciate it.

<Operator >: We have reached our allotted time for Q&A. I would like to now turn the call back over to Mr. Keith Creel.

<A – Keith Creel>: Okay, well thanks for joining us today. Let me, just close by saying this, I think this is critically important. We just closed and combined two proud, iconic, CP's 142-year-plus chapters, combining with KCS' 136 years. The story is not over, it's just beginning. We are 11 days into a forever story. I think that's the best way to look at it. We uniquely and only and solely bring three nations together, it's never been done before. I would suggest it will never be done again and we're about creating the most relevant rail network in North America to create those nations. So again the next three years are extremely exciting, but it's what's beyond that that excites me the most. We look forward to talking more about that in June. Have a great day.

<Operator >: This concludes todays conference call, you may now disconnect.