Transcript

Q1 2024 Earnings Call

April 24, 2024

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
Chris de Bruyn – VP, Capital Markets

MANAGEMENT DISCUSSION SECTION

Operator

Good morning. My name is James, and I will be your conference operator today. At this time, I'd like to welcome everyone to CPKC's First Quarter 2024 Earnings 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'd now like to introduce Chris de Bruyn, Vice President, Capital Markets, to begin the conference.

Chris de Bruyn

Thank you, James. Good morning, everyone, and thank you for joining us today.

Before we begin, I want to remind you this presentation contains forward-looking information. Actual results may differ materially.

The risks, uncertainties and other factors that could influence actual results are described on Slide 2, in the press release and in the MD&A filed with Canadian and U.S. regulators.

This presentation also contains Non-GAAP measures outlined on Slide 3. Please note, in addition to our regular quarterly financials, there is supplemental Q1 combined revenue and operating performance data available at investor.cpkcr.com, which some of today's discussion will focus on.

With me here today is Keith Creel, our President and Chief Executive Officer; Nadeem Velani, our Executive Vice President and Chief Financial Officer; John Brooks, our Executive Vice President and Chief Marketing Officer; and Mark Redd, our Executive Vice President and Chief Operating Officer.

The formal remarks will be followed by Q&A. In the interest of time, we'd appreciate if you limit your questions to one. It is now my pleasure to introduce our President and CEO, Mr. Keith Creel.

Keith Creel

Good morning. Thanks, Chris. Listen, before we get to the results, I think it's only appropriate on behalf of our CPKC family to extend our heartfelt prayers and condolences to Jim Foote's family and friends. As many of you know, we lost him last week. Many of us in this industry have had the honor to serve with Jim during his multiple decades of service to this industry. I can tell you myself personally, I'm going to cherish the memories and the experiences. He was a wonderful man, a dedicated man, dedicated to this industry, dedicated to the railroads that he worked for and the people that he served with.

If you knew him, there are a couple of things that are undeniable about him. He loved his friends, he loved his family, and he loved the companies that he served and that he led in this industry. It's a man lost too soon. I can tell you he left it better. The memories and experiences will not be forgotten nor will Jim, nor will his impact on this industry. So all the best, again, to his family, prayers and condolences.

So with that said, I want to thank you for joining us on the call today so we get to share our results. As I always will, I want to start my comments thanking the 20,000 strong family of railroaders that enabled the results that we get to share today. As you're all aware, we just celebrated our one-year anniversary just last week of this historic combination.

We're here to celebrate actually today in Calgary another historic event. We're going to launch our Final Spike Steam Tour this afternoon. So super exciting day in Calgary after we get to share these results and do our AGM. We get to celebrate with our employees and start this historic and iconic trip across all three nations. So for the next probably 35, 40 days, we're going to get to spend time and thank the communities that we operate in and through all the way from Calgary down to Mexico City.

So I thank the employees, again, that have been specifically involved in enabling this creation, this vision we created two years ago with the culmination of the launch today. So thank you for that. And I hope many of you across this network will have a chance to participate in that.

So looking back at this last year of our forever story, I tell you, I can't be more pleased with the progress. We're delivering on the commitments we made to create competition. We're delivering a safe and efficient service, and we're expanding our service continually. We're creating new and expanded customer relationships over the new markets that we're creating, collaborating, that is only enabled because of this historic combination.

I'm pleased with the results we produced in the quarter. It's been a strong start to the year from an RTM and an operational perspective. Yes, it was a tough January, but I can tell you Mark and the operations team recovered quickly, and the volumes have exceeded the expectations that we provided during our Q4 earnings call.

So specific to the results the first quarter produced revenues of $3.5 billion which was an increase of 2%. An operating ratio of 64 which is about 50 bps increased versus last year, core EPS of $0.93 an increase of 3%, despite a challenging start from the year the volumes finished up 1% for the quarter.

On the operating performance I'm extremely pleased with how the network bounced back from the January challenges and the resiliency that the team displayed. The momentum that we created and carried in the quarter with strong gains across the network in speed, dwell, and locomotive productivity.

The improvements were pronounced in Mexico where we continue to see large improvements across our operating metrics. Several of the key metrics that we follow internally have improved significantly in Mexico this quarter. Car miles per car day, locomotive productivity both up over 20% year-over-year. Active cars online down 15%. Dwell down, productivity improving.

The gains we've made in Mexico, the improved velocity, they've allowed us to optimize our asset base. They've been able to park assets we've been able to redeploy as many as 60 locomotives in fact during the quarter to other parts of the network to address winter weather and serve stronger than expected demand. So huge credit to the operating team demonstrating the power of a true Precision Scheduled Railroading operating model. In fact, I think it's better said that CPKC is PSR prime. And importantly, these improvements continue to come at a time when in Mexico we're delivering an all-time high GTM performance.

So, management change, as you would have seen in March, we made a change to our leadership team in releasing John Orr from his commitments to CPKC. Again, I'd like to thank John for his contributions and the impactful leadership that he had as a leader. I believe it's your challenge to leave it better and John did that. He did that in his service to the KCS while the company was in trust, as well as to CPKC until his departure just last month.

We're fortunate to have an extremely talented and deep bench of PSR railroaders on our team so the decision to release John was not an easy one but it was made possible by the strength and the depth of the teams we actually have at CPKC. The plan was always for the Mexican operations to eventually report into Mark as our COO and with the strong performance in Mexico that I've mentioned the experienced team that we have in place it just simply made sense to accelerate that plan.

So credit to the entire operation team since John's departure, they haven't missed a beat. We're continuing to execute drive improvements and provide great customer service to our customers.

So in closing, I'm happy to start -- I'm happy with the start that we've had to the year, our performance so far in the second quarter as well. We're poised to be the most relevant rail network in North America uniting a continent, adding competition to the industry and delivering new options along with safe and efficient service to our customers.

So, with that said, I'm going to hand it over to Mark to speak to the operating performance. John's going to bring some color to the markets, and then Nadeem will close elaborating on the numbers before we open it up to questions. Over to you, Mark.

Mark Redd

All right. So, thank you, Keith, and good morning. I'm extremely proud of what the operating team produced this quarter. I'd like to thank them for their continued hard work delivering safe, reliable service.

Throughout the quarter, I spent a great deal of time on the network, and I'm pleased with the level of talent and dedication here at CPKC. I'd like to recognize the Shreveport terminal as well. They were named CPKC's 2023 Terminal of the Year. This terminal has been executing at an extremely high level, and having spent time earlier in my career at this terminal, I'm very pleased to recognize this team for their outstanding achievement.

I also spent time in Mexico this quarter. We have a strong, dedicated team of experienced railroaders, and as Keith noted, we're continuing to drive strong, sustainable improvements.

Now looking at the quarter, thanks to the team's collective efforts, we made a quick full recovery of extended cold weather in January, serving very strong volumes in the western corridor, and also extreme high-level record GTMs in Mexico, while posting strong year-over-year operating metrics.

And looking at the metrics this morning, locomotive productivity up 8%, average train speed up 13%, our dwell is 10% down, all demonstrates a fluid network. Our fuel efficiency declined 2%, largely due to the weather earlier in the quarter, but I expect this to improve throughout the year.

So looking at safety this morning, the FRA personal injury is up 3% year-over-year at a 1.15, FRA train accident still leading the industry at 0.89 up from 0.71 a year ago. While we strive for expected improvement each quarter, safety is a never-ending journey.

Our focus remains on building an aligned safety culture, which is key to maintaining CPKC's industry-leading safety record. Notably, we've rolled out HomeSafe across the KCS network, and we continue to do so in Mexico as well.

So as I look at Mexico, we're advancing some of the key initiatives that were identified last year to improve productivity and capacity. We're finding opportunities to streamline our operations during the quarter, where we're able to shut down switching operations at Venegas Yard.

We're also focused on improving cycle times, streamlining operations for bulk commodities and customers. This is an area where we've seen success so far, but we're also freeing up locomotives and equipment that we can use in other parts of the network so we can create more synergies and handle more growth.

Looking at capital, our plan remains focused on growth and safety. In the quarter, we in-serviced three more new sidings as part of our USD $275 million merger capital commitment. We've also in-serviced two sidings in Mexico to help with capacity and fluidity. If we look at the Laredo Bridge, 65% complete at this point, we remain on target to be closed out by the end of the year. All of these projects will support growth and further improvement in the network.

In summary, we've made a great start to the year, and the entire network is in great shape. We're in a good place from an asset and resource perspective, and the team is aligned on focusing providing service excellence to generate industry-leading growth.

And with that, I'll pass it over to John.

John Brooks

All right. Thank you, Mark. And good morning, everyone. So with a full year as a combined company under our belt, I'm extremely pleased with the progress we've made so far and all the opportunities I still see ahead of us. We've built on our momentum from Q4, and despite some of the early weather challenges we had to start the year, we have started the year strong, and we are gaining momentum.

Now looking at the results, on a combined basis, we delivered freight revenue growth of 1% on 1% RTM growth. This is slightly ahead of the flat-to-slightly-down outlook for RTMs that we provided to the market in January. Cents per RTM was flat year-over-year with strong pricing offset by a 3% fuel headwind along with negative mix.

Carloads on the quarter were down 3%, and I fully expect carloads to continue to lag RTMs. This is a result of our network unlocking longer lengths of haul as shippers take advantage of our seamless three-country franchise, delivering RTM growth, and average length of haul on the quarter up 8% versus last year.

In addition, we've also seen lower margin, short-haul intermodal business running between Mexico and the border shift off our network, opening up further capacity for growth in our strategic long-haul lanes.

Now taking a closer look at our first quarter revenue performance, I'll speak to the FX-adjusted results on a comparison versus CPKC had the combination occurred in 2023. Starting with bulk, grain revenues were up 2% on 1% RTM growth. U.S. Grain volumes grew 19% over prior year. Our franchise is benefiting from strong export corn shipments to the PNW and Alberta, along with more shipments of wheat and soybeans to Mexico, which is a new area of growth for CPKC.

Canadian grain volumes were down 15% year-over-year. Volumes decreased as a result of a weaker 2023 harvest in our draw territory. However, they still came in better than anticipated as on-farm supplies remained stronger given softer shipping in the fall peak. So while we may see better-than-expected volumes this summer, we still expect overall year-over-year compares in Canadian grain to be a headwind until we get to the new crop.

I also should note that the strong performance in our U.S. Grain franchise essentially offset the Canadian grain headwind, and this is a great example of how this combined network is adding resiliency within our book of business.

Moving on to potash, revenues were up 4% on a 2% volume growth. Despite a very slow start in January, we rebounded quickly and ended the quarter with growth driven by solid export and domestic shipments. We are well-positioned for solid potash growth in 2024 as demand remains steady and we lapped the comps from Canpotex's outage at their Portland terminal that occurred from April to December of last year.

Coal revenue and volume declined 7%. Cold weather in January negatively impacted Teck's production and exports, while lower natural gas prices weakened demand for U.S. Coal. We expect a good run with Teck as we look to claw back tonnage that didn't move in Q1.

And moving on to merchandise: energy, chemicals, plastics, revenue and volume grew 2%. The volume growth in the quarter was driven by higher fuel oil, DRU shipments, and plastics. This strength was partially offset by multiple customer outages we faced resulting from the cold weather.

Looking at this portfolio, we are excited about the synergies that we are capturing, particularly with new wins in plastics, renewable diesel, and refined fuels, as we connect the markets between Alberta, the Gulf Coast, and Mexico.

Looking forward with customer production now stabilized at our facilities on our network, and the ongoing ramp up of synergy gains, we are set up for a solid year in ECP. Forest products revenues were down 4% on flat volumes. Forest products volumes were flat despite the broader economic headwinds we all face and softening in the paper space.

We had a record quarter in lumber driven by strong synergy conversions with new line haul solutions connecting Canadian producers with the strong demand in the Texas market.

The metals, minerals, and consumer products revenue was down 1% on a 5% volume decline. Volumes in the quarter were largely impacted by weakness in frac sand to the Bakken and Permian Basins. This is partially offset by ongoing strong demand from our steel production.

Automotive produced another record quarter with volumes up 8% and revenues up 10%. Despite this record performance, I was not pleased. Results came in well below our expectations due to numerous production holds for quality and parts availability. With those issues largely resolved, we expect to see growth in automotive continue to accelerate through Q2 and the rest of the year.

I'm also very excited to have our new Dallas auto compound opening in June located at our Wylie Terminal. This compound is part of our playbook that unlocks an entirely new supply chain model for the OEMs, giving them the service, reliability, and capacity certainty like they've never seen before.

I'm proud to report that this new compound is largely sold out, and will handle many of the top selling vehicles within the Texas market, including the vehicles built by our anchor tenant, General Motors.

On the intermodal side, revenue was down 1% on 7% volume growth. Starting with the international intermodal, volumes were up 14% on strong growth through both the ports of Vancouver and Lazaro. Strength through Vancouver was driven by a return of volumes after the work stoppage last summer and some impacts from the Red Sea and potential looming east coast labor disruptions.

Although these, stronger than forecasted volumes did drive some temporary congestion at the port, we successfully worked with our customers and the port to manage this excess volume. We are also encouraged by the ongoing trends at the port of Lazaro Cardenas. Through February, TEUs through this terminal grew by over 40% year-over-year.

In domestic intermodal, volumes were flat this quarter. Our Mexico Midwest Express cross-border service continues to perform extremely well with truck-like service across a safe, reliable border in Laredo. Growth on this flagship service has helped offset the shift in the short-haul business and since February, we have seen weekly volumes grow by over 24%.

We expect our density on this product to build through the year as we grow our volumes of reefer traffic between the U.S. and Mexico. And pending STB approval, we start up operations with CSX and Schneider from Texas and Mexico into the Southeast U.S.

So, in closing, Q1 volumes came in better than expected and we're off to a good start in Q2. Looking at the past seven months, we've seen year-over-year volume growth in each month, excluding January. While we still have a headwind from Canadian grain, and we continue to be very cautious on the macro environment, our line of sight to synergies, self-help opportunities, and a disciplined pricing approach remains a unique opportunity for CPKC. I'm pleased what we have accomplished for our first year as a combined company, and I look forward to sharing continued progress with you as we go forward.

With that, I'll pass it to Nadeem.

Nadeem Velani

All right. Thanks, John, and good morning.

So looking at the numbers, our reported operating ratio was 67.4%, and the core adjusted combined operating ratio came in at 64%.

Earnings per share was $0.83, and core adjusted combined earnings per share was $0.93, up 3% year-over-year. As a reminder, these core adjusted earnings exclude the non-cash impact of purchase accounting for the KCS merger, primarily related to D&A, along with interest expense and acquisition-related costs, which continue to gradually decline.

Similar to what we shared last quarter, our combined operating expenses illustrate the effects of the acquisition for the first quarter as if the acquisition closed on January 1, 2022. I will speak to FX adjusted combined operating results in these prepared remarks.

Now taking a closer look at our income statement, reported operating expenses provided on Slide 13 and combined operating expenses on Slide 14, where I will focus my comments.

Including adjustments, comp and benefits expense was $676 million. The increase was driven by wage and benefit inflation, along with a $23 million headwind from stock-based compensation, driven by the increase in share price over the course of the quarter. Stock comp amounted to a 70 basis point, or $0.01 headwind on the quarter. We also saw higher current service costs from our DB pension plan of $4 million due to a lower discount rate at year-end 2023.

Looking to the rest of 2024, we continue to expect average headcount to be roughly flat on a year-over-year basis. Fuel expense was $458 million, down 5%. The decline was primarily driven by a $28 million, or 6% decline in fuel price.

Overall, net fuel price was a $61 million drag to operating income in the quarter, or about an 80 basis point impact to the OR. This amounted to a $0.05 headwind as well to core adjusted combined earnings on the quarter.

Materials expense was down 5%. The decline in the quarter was driven primarily by timing of track and locomotive maintenance as activity schedules across the Legacy-CP and Legacy-KCS network are aligned.

Equipment rents were up $12 million, or 17%. The increase was due to a 2023 receivable, along with higher intermodal car hire as CPKC lanes shift to longer length of haul. This increase was partially offset by higher efficiency from improved cycle times and increased network velocity.

The depreciation expense was up 6% resulting from a higher asset base. Purchased services and other was up 2% year-over-year. Higher terminal service costs and increase in bad debt expense and cost inflation were partially offset by cost synergy savings from a combined insurance premiums and the recognition of a one-time non-competition waiver fee payment of CAD $34 million.

Moving below the line on Slide 15. Other income was $2 million, reflecting the impact of settled foreign currency hedges and higher equity earnings from increased container volumes through the Panama Canal Railway.

Other components of net periodic benefit recovery was $88 million, reflecting the lower discount rate compared to 2023 and partially offsetting the headwind to comp and benefits.

Net interest expense was $206 million or $201 million on an adjusted basis. The decline was driven by a reduced debt balance. Income tax expense was $259 million or $289 million on a core adjusted combined basis. We still expect the CPKC core adjusted effective tax rate to be approximately 25% for the year.

Turning to Slide 16, we are generating strong cash flow with cash provided by operating activities of $1,015 million in Q1. Capital investments and safety and growth remain our priority. In this quarter, we reinvested $527 million in line with our plan to invest approximately $2.75 billion in 2024.

As Mark discussed, we are making strategic investments in safety and capacity, positioning our network to continue efficiently absorbing the growth that this merger has enabled. We generated $555 million in adjusted combined free cash flow on the quarter and continue to repay debt. We still expect to reach target leverage in late 2024 or early 2025, at which point we will evaluate shareholder returns with our Board.

I'm also very pleased to report that during the quarter, Moody's upgraded CPKC's credit rating outlook from stable to positive.

In review of the quarter, RTMs came in ahead of expectation that we communicated on the fourth quarter call, despite weather challenges earlier in the year. Our operations were resilient and we made progress on key growth investments across our network. We're also seeing the benefit of a lower inflation environment and disciplined pricing on our cost structure. This sets us up well for margin improvement as we move through the rest of the year. I am pleased with the start to the year and we expect to continue gaining momentum from here.

With that, let me pass it over to Keith.

Keith Creel

Thanks, guys. Let's open it up, operator, for questions.

Question & Answer

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<Operator >: Mr.Chappell, your line is open.

<Q – Jon Chappell>: Thank you. I guess that's me. Jon Chappell from Evercore. Mark or John, we've seen a real acceleration of Chinese imports into Mexico of late. The reasons, I guess, vary, and we won't get into that. But as it relates to what it means to Lazaro and what it means to the new services that you've created, are you seeing any impact from those yet? Is that moving mostly on truck? And I guess, is that a real big opportunity for you as you continue to see that new trade line open up?

<A – John Brooks>: Thanks, Jon. This is John. Yes. So, we saw a steady growth platform at Lazaro, really starting the back half of last year. And that trend has continued. I think I said we're up 40%. That was through February, but that's continued here in March and April. It is a pretty good mix, Jon, of truck and rail. And principally, that volume is, well -- at least primarily right now, more intra-Mexico than cross-border. But I can tell you, we do and we have a continued improving product out of Lazaro. I appreciate all the efforts of the state of Michoacan and the efforts at the port between Mark and the team down there to provide a good, safe product up into Mexico.

So I do believe you'll continue to see sort of that volume build on itself. And then we'll get into the exciting part of this chapter as we begin to see that density build into our cross-border business up into that Texas and Gulf market, which again, I believe we see a good opportunity there as we move into the second half of the year and into 2025 to grow that volume.

<A – Mark Redd >: And Jon, I would just add, remember we stay pretty close to each other me and John and we've got capacity, we've got room to move locomotives and people in place. So we can move whatever business we need out of Lazaro, with certainly communication with each other.

<Q – Jon Chappell>: Thanks, Mark.

<Operator >: Your next question comes from Brian Ossenbeck with JP Morgan.

<Q – Brian Ossenbeck>: Hey, good morning, thanks for taking the question. Keith just want to get your thoughts on the latest with the TCRC union negotiation. There's some comments made by CN last night, just want to get your perspective on it because at least from our standpoint, it sounds like there's quite a few moving parts in terms of changing, potentially to a or at least offering an hourly agreement and the unions, obviously, are I think pushing back on that at least from the time being. So wanted to get your thoughts on that.

And then John if you could just clarify what you meant about the Texas-Mexico into the Southeast pending STB approval, is that related to the MBNR, and through the Speedway? Thank you.

<A – Keith Creel>: I'll start with that when that's exactly what it is Brian, and as far as the application to the STB, we expect hopefully, we anticipate a favorable ruling based on the facts and the competition it represents and creates hopefully in the very near future.

I don't know if it'll happen next month or the following month. But when it does come when the decision comes we are prepared and ready within a month's time of the notice to take over operation of that piece of railway and to start the work and just a partnership with CSX to create a new Class I alternative to the Speedway that exists today to complement the service that we provide NS over the Speedway today. So very, very excited about the future of that.

The TCRC maybe I'll say tempered excitement or expectations. I'm a realist. I'm an optimist. I can tell you now that we've been negotiating with the TCRC for months, we were forced to file for conciliation. We were with the TCRC this week. We were with them not long ago.

The way I see it the positions have not changed a lot. We have two options on the table. We have a, what I call a status quo deal with only one what I would call a pay relative change not a work rule change tied to held away from Home-terminal pay, that's the only concession that we're asking for in exchange for fair and equitable wage increases, which other employees and other unions have realized the benefit of. The second is a progressive hourly deal. I can tell you that that progressive hourly deal in my assessment addresses what our employees want and need.

They want a better quality of life. They want higher wages, which certainly is understandable, those expectations, and in turn, our ability to be able to provide that, is found in the terms and conditions of that hourly agreement.

The customer wins, the employee wins, employee retention wins. It truly is a win-win scenario, but it takes change. It takes leaders that are willing to see the wisdom in it, the benefit in it, and at this point, that has not happened. Now, again, I'm going to be optimistic, but realistic, so where does that lead us? That leads us to a place, the third weekend of May, in fact, kind of the drop-dead time is going to be May the 19th at 00:01, and at that point, if we don't have an agreement, which I'm optimistic and hopeful we'll be able to reach one, but if we don't, which is what we're -- obviously hope for the best, but you have to make sure you plan for the worst as well.

If that were to occur, a strike notice or a lockout notice within 72 hours, so May 22 at 00:01 would be the earliest that a strike could actually come into existence, and the unique thing about this as well is CN is facing the same deadline that we're facing. Uniquely to our network, not only would it be our running trades employees that operate the trains that move across the network, it's also our dispatchers that dispatch not only the freight trains, but also dispatch the passenger trains in Vancouver that get the good folks in Vancouver from their homes to the city downtown core to go to work.

Same situation in Toronto with Metrolink, we dispatch those trains on our rail line, same situation in Montreal with those passengers. So this is truly something that I hope can be avoided. It's certainly not going to come at a good time for the country of Canada, but as I've told our customers and as I've told the government and I've told our employees, if we're going to have a strike, the uncertainty of that in and of itself is damaging.

For it to be prolonged, for it to occur, if it must occur later in the year when we have a harvest coming in, when the demands for our service and the needs of the country have never been greater, that is the absolute worst time for it to occur.

So as unfortunate as it is, I believe from a very realistic view, given my experience, having been at that negotiating table many, many times and I'll be at it again this time, that's how serious this is. I'm hopeful and I hope that we can avoid it, but this railroad will be prepared in the event that we can't, because we will not do a bad deal.

We've got to balance the needs of our shareholders, the balance of our customers and the balance of our fellow employees, not just the TCRC that we have negotiated with and came to negotiated agreements historically, just unfortunately we haven't been able to get there with this group. And again, I'm hoping with strong leadership that can change. I'll remain optimistic, but it just hasn't happened yet.

<Q – Brian Ossenbeck>: Thanks very much, Keith.

<A – Keith Creel>: Thank you.

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

<Q – Walter Spracklin>: Yes, thanks very much. Good morning, everyone. I want to go back to your volume guidance. When I look at what's happening in Vancouver, obviously a surge of containers coming into that port. You're poised to benefit significantly from that. John, you mentioned Mexico, Lazaro Cardenas up 40%. That's not a small number. It's catching its stride. Macro trends, in your prepared remarks, you indicated Q1 came in better than you expected and many would say we're perhaps, from a macro perspective, in a little bit better outlook here in April going into May than we were in January.

So just curious, when you look at your low single-digit volume guidance and so many kind of inflecting positive macro, but also more importantly, company-specific opportunity, just curious as to where you frame that low single-digit, is it just kind of just being overly conservative, or do you see upside to that guidance here for 2024?

<A – Keith Creel>: Walter, you've made some very good observations, and I think I'd frame it up as being responsibly conservative. There's some uncertainties out there. Certainly, we're in a good place. The network's running well, the demand is there, the synergies are coming, the new markets are being developed. We have a very unique story and a very unique opportunity.

But we also have a responsibility to look ahead. We've got a potential looming strike. I don't yet know what the macro's going to do the second half. We've got some assumptions in that which are conservative assumptions, so if it does better than what we assume, then sure there's some upside.

If the strike isn't as long as what we might think it'd be, or if we don't have a strike at all, then sure we've got some upside. Do we have a normal grain harvest, is it a bumper crop, or do we have, again, a situation where we face a potential drought? Those are the levers that we're really looking at, and once those become clear, then I'd be in a position to responsibly tell you, yes, we have upside.

And I guess I'll just close saying, we're in a good place. We've worked hard to get to this place. This team is prepared for any of those outcomes we've talked about. And in the end, come this summer, come the end of the second quarter, I think we'll be in a better position to tell you, yes, Walter, what you're seeing the potential of that is true. It's exciting. And until then, we're going to stay responsibly conservative and make sure we do our jobs and prepare for these challenges we have ahead of us and come out in a very, very strong position on the other side.

<Q – Walter Spracklin>: Responsibly conservative is good. I appreciate it. Thank you.

<Operator >: Your next question comes from Fadi Chamoun with BMO Capital Markets.

<Q – Fadi Chamoun>: Yes, good morning. Maybe just one follow-up question on this volume. In the second quarter, I mean, we're starting off strong. I'm thinking grain potentially could wind down a little bit as we move into the quarter. Is there a way for you to kind of give us some gauge on what second quarter kind of does the right framework for Q2 volume?

And really my main question on the pricing side, I mean, pricing environment is quite good, maybe unless you're competing with truck in some markets, but what is your thinking now with a year into this merger about the service-related pricing opportunity for CP? And is this something that will take time to kind of realize or are there triggers in terms of contract changes, renewals that you can kind of use to kind of drive a price improvement on the basis of the service level that you're delivering?

<A – Keith Creel>: Let me -- Fadi, I'm going to let John get into the color of the pricing, but let me tell you conceptually when it comes to price at this company, we're selling a valued service. It's not a commodity. There's value in it. There's a value proposition for the customer.

The level of service, the capacity we have on our railroad, the way we run the railroad, it's worth something in markets because it allows the reliability for our customers to win in their marketplace. So that's always going to be our story. It's a value proposition.

And as long as we do our job well, we never have to apologize for providing a very unique and valuable service. On the volume side, we're starting strong. This morning, I looked at it, we're up nine, over 9% on an RTM basis, and that's really what matters the most, not carloads, it's RTMs.

But again, looking at what's ahead, a potential strike, we're modeling again in a very responsible, conservative way for the quarter. I think we're somewhere around 3%, 2% to 3% for the quarter. And again, I've already talked about if some of those things don't happen, then that will change. But right now, that's where we're sticking our guidance to, and we're well on track to be able to achieve that.

So John, you want to provide a little color on the price?

<A – John Brooks>: Yes. So that's exactly, Fadi, it, in terms of I'm looking at the quarter in terms of volume. Certainly, hopeful there's upside in May and June, but with the strike and other things looming, we're going to stay responsibly cautious on that front. The grain business, you're right. It definitely has been a little better the last 30 days or so. But we're going to get into seeding here in May and certainly expect that to fall off. I just met with all the grain companies the last couple weeks and they're pretty optimistic that we might see, particularly if we get some rains here in May and early June, that we might actually see a pretty decent push this summer. So we're watching that closely and certainly that could provide some upside there.

You asked about the pricing. I'm super pleased with the execution and discipline that the team performed with in Q1. I saw it coming. We held in there and we delivered on the very top end of our efforts the last half of '23. It's carried into the quarter in '24 and we'll continue to be disciplined as we move forward.

I had previously said there were a number of, maybe legacy-KCS agreements that hadn't been repriced and were coming up for renewal this first half of the year. So we've been focused on those. We've been focused on those in the context of what Keith said, making sure we're getting the value for the service and capacity that we provide.

So I expect that to continue here in Q2. If I were to call out one area, where we've seen maybe softness versus others, it would be in the domestic intermodal front. I think that's pretty obvious though, relative to some of the overcapacity challenges in the truck market out there. But, there also might be some signs of life there as we push towards the second half of the year.

I'm really pleased with how we've seen our volumes grow on our Mexico Midwest Express train. I fully expected a slugfest here to start the year in terms of building that volume, and we've had some really nice wins. So if we can keep that trajectory going, again, there might be upside as we look to Q2 -- or the second half of the year, sorry.

<Q – Fadi Chamoun>: Thank you, I appreciate the color.

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

<A – Chris de Bruyn>: Operator, please go to the next question.

<Operator >: Certainly. Your next question will come from Ken Hoexter with Bank of America.

<Q – Ken Hoexter>: Great. I'll take Scott's question as well. Keith and team, great thoughts on Jim, always enjoyed our discussions, so thoughts there as well. John, you tossed out there real quick the intermodal noted some short haul lanes left. Is that from increased competition? And then, perhaps Keith or Nadeem, can you talk about the progress on synergy targets? Are there -- can you talk about the dollars at this point? And does that set you up, I guess normal sequential operating ratio performance would put you sub-60% into the second quarter. Can you talk to that level? Thanks.

<A – Keith Creel>: On the synergy question, Ken, we're exactly where we said we would be. We exited USD $350 million, we said we're going to double it on the revenue side. So we're certainly on track, in a good position. Same for the cost synergy side. So synergies are moving in line with what we said if not a little bit ahead. So we're very pleased in that space.

<A – John Brooks>: On the short haul stuff, Ken, honestly, it's stuff that we're completely fine with it exiting our railroad. To be quite candid with you, it's business that principally ran between stations in Mexico and the border. It consumed a lot of capacity at our terminals in Mexico and certainly our border crossing.

So the fact that a lot of that traffic has moved over to the FXE has frankly just opened up the ability for us to grow the long haul. I talked about our average length of haul being up, I think 8% year-over-year. Our intermodal average length of haul is up 12%. And that's -- we're utilizing the capacity with our customers that want the premium ride and a seamless connection at the border up into the upper Midwest into Canada. So I expect that trend to continue.

<A – Keith Creel>: Feeds right into that value proposition model, Ken. It's a good thing, not a bad thing.

<A – Nadeem Velani>: And Ken, we'll obviously see sequential improvement in the OR and year-over-year improvements. Without giving you a Q2 number, I'd say that it's going to be somewhat dependent on what happens with the labor situation. We talked about some of the grain impact in Q2, that we might see that the grain volumes start to decline in Canada as seeding takes place and we start running out of grain in Canada, so it depends. I'm not going to give you a number. I'd just say that we'll continue to see improvements and year-over-year improvement.

<Q – Ken Hoexter>: Great. Thanks for the time guys, appreciate it.

<Operator >: Your next question comes from Steve Hansen with Raymond James.

<Q – Steve Hansen>: Good morning guys. I wanted to circle back on the length of haul issue because it's been quite marked of an increase, not just in intermodal but in ECP as well. And John, do you want to maybe just comment on the longevity of that trend? I presume it's the Edmonton to the Gulf volumes that are helping extend that length, but just any broader commentary around the durability of this broader length of haul theme? Thanks.

<A – John Brooks>: Yes, Steve. So the mix was quite interesting in Q1. I spoke about the certainly the short haul domestic intermodal that shifted away from the railroad. We definitely saw volumes decline in our U.S. coal business which are also very short haul business. But on top of that we layered on strength in international, strength in grain, strength in potash, some of those longer haul plus the synergies, the growth in the MMX and in the ECP area that you alluded to which is largely Alberta down to the Gulf and even into Mexico.

I do believe this is, we're just seeing a natural progression of what this railroad looks like in the future and just maybe got a little accented in Q1 more than we anticipated. I expect that to moderate and normalize.

The other thing I will point out because I think it's important if you guys think about mix is we have really forecasted a strong automotive Q1 with all the business wins and some of the pent-up demand. And certainly we outperformed and we set a record in that quarter, but I'll just remind you it did fall very short of our expectations. So there was a lot of good length of haul there and high cents per RTM traffic that didn't materialize in Q1 that certainly we're seeing ramp up here in Q2.

<A – Keith Creel>: I think I'll add a little bit of color to that John because I see it a little bit differently. When you say normalize, I don't think we're going to normalize until we've fully built out our closed loop automotive supply chain.

We've got Wylie Terminal opening up end of the quarter. In June. That's going to allow vehicles that are produced and shipped out of Ontario today that currently length of haul ends in Chicago. That length of haul is going to end in Dallas, Texas for CPKC. It's going to create empty supply to go down to Mexico and lengths of haul that today perhaps stop at Laredo or Robstown are going to be going to Minneapolis/St. Paul or going to Canada.

So again, this thing is a multiple chapter story. We're not going to get it built out overnight. It's a two, three, four, five-year plan. That in and of itself that one business unit offers significant, I think, accretive incremental improvements to driving that length of haul.

<Q – Steve Hansen>: Great color there. Thanks.

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

<Q – Scott Group>: Hey. Great, sorry about that earlier, can you guys hear me?

<A – Keith Creel>: Absolutely. Good morning, Scott.

<Q – Scott Group>: You guys keep referring to a potential strike. It almost feels as if like your guidance assumes that we are going to have a strike or said differently, if we do have sort of a normal short-lived strike, do you still feel confident about doing double-digit earnings growth this year?

And then maybe just bigger picture, Keith, when I look at Q1 revenues up 2%, operating income is flat. Do you think, I guess, I know we've got some strike uncertainty, but going forward like it feels like we're at the point now where like the story is going to really start showing up in the model in terms of better revenue growth, meaningful margin improvements and significant earnings growth. Is that the right way to think about it that we're sort of we're there now and it's going to all start showing up in the model?

<A – Keith Creel>: I think we're at an inflection point. So as this thing starts to play out, Scott, I think you've got that captured accurately.

<A – Nadeem Velani>: And Scott, if we have kind of a strike that's not extended, I'm comfortable that we can still hit our double-digit EPS guidance for the year.

<Q – Scott Group>: Okay. Thank you, guys.

<Operator >: Your next question comes from Tom Wadewitz with UBS.

<Q – Tom Wadewitz>: Yes. Good morning. I guess a lot of things to -- you can ask about on the growth drivers. You've got a lot of things going on. How do you think about, you mentioned kind of a new service that we get approval from STB with Schneider. Would you think of that as being kind of new origination points or kind of new connectivity that gives you new volume? Or do you think some of it is service goes from Norfolk to CSX?

Or I guess how do we think about obviously, there's some noise going on with the agreement you have or the concessions that you got related to John Orr leaving. So I don't know if you could give some broader comments on kind of the opportunity and how much is new business and how much do you think might end up being shifting on that kind of Mexico and Meridian Speedway opportunity? Thank you.

<A – Keith Creel>: Okay, thanks. Let me say this. All this noise about the agreement over the Meridian Speedway is just that, it's much to do about nothing. At the end of the day, all we've done is take issues that were ripe for dispute off the table. We're going to have unfettered opportunity to compete in partnership with NS, to compete in partnership with CSX. This isn't about share shift. If there's any, it might be nominal.

There's some overlapping markets in the Southeast that perhaps they both serve. But what this is, is about growth. It opens up competition in new markets for CSX's customers and lanes that NS can't offer them that opportunity. And conversely with NS, they're no worse off. We've got 2 situations here where we can uniquely partner with both railroads. It's enabling investment to create an alternative route. The customer has a choice. Competition wins. Service wins.

The only true threat in this, unless you're afraid to compete, is truly the truck. That's where the competition is. That's where the growth is going to come from. It’s that I-20 that runs parallel to that Meridian Speedway that we're going to be competing against. This is truck-competitive business. So any and again, it's much to do about nothing. I think this is a win-win situation.

And again, I'll close saying the only other loser in this perhaps are the lawyers that would have been fighting on our behalf in the dispute with NS over some of those very ripe for dispute considerations that were eliminated with our agreement. And listen, if anybody wants to see the truth and see the facts, we filed with the STB the agreement, go look at it.

You'll see for yourself that exactly what we're saying, and in fact exactly what NS has said, is exactly what the truth is. It's much to do about nothing. Let's get over this and let's get to competing and being great partners with the NS and being great partners with the CSX. That's what our intention is to be.

<A – John Brooks>: Tom, I just would add to Keith's comments. I don't see shift. It's a truck lane either out of Mexico or Texas that we're focused on. And frankly, there is a significant -- with the terminal development we've got going on at Wylie that is non-intermodal focused, the automotive, the transload development we've got going on in Dallas market, the carload business opportunity in that lane that I think is untapped is a great growth story and that those markets are open up to both NS and CSX.

There's just never been for whatever reason the intense level that we will bring to the sales approach of growing that lane. And frankly, we've had so many other irons in the fire and areas of focus. We're now kind of shifting to how we grow that as part of this portfolio. And I see it all as additive.

<A – Keith Creel>: And I would say we're partnering with the right folks too. We're super excited about the partnership with Schneider, the same partnership that's allowing us to grow that great MMX service is I think going to meet or exceed this opportunity when we talk about this new gateway we're creating.

<Q – Tom Wadewitz>: Maybe just one brief follow-up, do you think it's more volume is Dallas origination or Texas origination or is more of the new business with CSX going to be Mexico origination?

<A – John Brooks>: Well, there is a lot of certainly Texas, Atlanta type traffic, Tom, it's truck and as you know that market is extremely tough right now with the truck capacity and spot rates. So it's hard for me to put a percentage on it. I would say maybe broadly speaking that might be a slightly bigger intermodal type market, but it's highly competitive and we're going to have to find those customers and those commodities that fit our model and are willing to pay for that servicing capacity.

I can tell you my team's focus and my focus with NS and CSX is going to be on Mexico. That's where we can generate a length of haul. We can leverage the great service Mark and team are providing down in that marketplace. And with all the industrial development going on down in Mexico, we've got over 40 projects kind of active right now that will represent significant volume growth opportunities in intermodal. Over the next two to three years, that will sort of fit right into that wheelhouse of that service into the Southeast U.S.

<A – Keith Creel>: I think the other complementary piece of that book, Tom, is all the automotive development plants that are being developed and that will soon open on specifically, in this case, the

CSX. So, as those supply chains get established, those parts that get moved from Mexico to the Southeast and parts from the Southeast to Mexico, that ecosystem for us to be able to have a competitive lane that takes right now the finished vehicles that are being produced today.

There are thousands of carloads, potential rail carloads of finished vehicles that are on that highway that are moving between the Southeast markets where they're produced for Glovis perhaps going into the Dallas markets. Those are ripe for opportunities; rail wins, the environment wins, competition wins. This is all a good story.

<Operator >: Your next question will come from Benoit Poirier with Desjardins Bank Securities.

<Q – Benoit Poirier>: Just to come back on the previous question with respect to, obviously, there's a lot of momentum at Lazaro with the 40% increase in volume. It looks like that the, there's China that is also bypassing the U.S., so sending stuff in Mexico.

I'm just wondering, how much is it the driver with respect to the overall volume increase? We've seen not too long ago that the Mexican government announced that it would apply some tariffs, on some imported goods, so they want to protect kind of the Mexican and the U.S. economy. Just wondering whether it's the kind of something to keep in mind? And just in terms of cargo diversion, have you seen some on the back of the labor issues? And if you could give an update on St. John, that would be great.

<A – John Brooks>: Yes. So Benoit, I'm not going to speculate on whether or not the Mexican government does something in terms of managing Chinese imports versus their own production. I do believe we have seen some of the surge relative to some of that business coming into Mexico today. But the fact of the matter is Lazaro has capacity, has low on-dock dwell.

And frankly, I think the steam ship lines, and beyond just maybe transpacific freight, South American freight, are recognizing Lazaro as an alternative. And is that because a looming East Coast and looking at that as an alternative to going through the Panama Canal, I think all that's part of the story.

And frankly, Benoit, we're out selling it hard. We believe it can become a complement to Vancouver and the West Coast of California and give shippers another option. And frankly, our partner, Hapag-Lloyd and their announcement with Maersk and the formation of Gemini as you look to 2025 with Maersk's relationship and doubling the capacity at Lazaro, I think presents again CPKC a tremendous opportunity with those companies.

I'd say our St. John volumes have sort of settled in and actually moderated here lately. I think we are seeing some impacts in East Coast imports relative to some of the trade challenges, I guess, that the world is facing in that port. Now that being said, we're watching close what's going to take place at the Port of Montreal in terms of a potential strike there. And if in fact we get a fall labor disruption on the U.S. East Coast, I think both of those -- we're keeping both of those stories topical with the steamship lines as St. John being an alternative if in fact we do have disruptions in that area.

<Q – Benoit Poirier>: Okay. That's very good color, John. Thank you very much.

<Operator >: Your next question comes from Ravi Shanker with Morgan Stanley.

<Q – Christyne McGarvey>: This is Christyne on for Ravi. Apologies for earlier. Can you guys hear me now?

<A – Chris de Bruyn>: Yes, we can.

<Q – Christyne McGarvey>: Great. Thanks for going back to us. Maybe taking a step back, I want to talk about the longer-term guidance and particularly kind of conversion of the $5 billion pipeline you guys have outlined. At the Investor Day, it definitely felt very idiosyncratic, still does, but it does feel like the macro maybe disguising some of the success you guys are having around converting that pipeline.

So maybe you can just remind us and parse out kind of the long-term guidance, how much you feel is idiosyncratic versus maybe meeting the macro backdrop to be more supportive in terms of unlocking the full potential of that pipeline?

<A – John Brooks>: Maybe just a couple of comments on there. In terms of what we laid out at Investor Day, I would say we're ahead of plan in terms of my expectations on delivering in frankly, all of those categories. Certainly, some maybe a little quicker than others. As a primary example is just talking about Lazaro. I do see that being maybe a little bit more back half of this year and 2025 story in terms of cross-border opportunities.

But that being said, I would say the area of automotive has really maybe presented itself as more of a pull-ahead opportunity for this network in the development of that closed-loop model that Keith spoke about and the benefits that the franchise provides the OEMs in that area.

I would say we were pretty adamant and clear around finishing 2023 at a USD $350 million revenue run rate. I remain very confident in, that we'll double that exiting 2024. And frankly, that will put us right in line or maybe even a little ahead of what we laid out at Investor Day with those areas. I think your call out around the macro not being very supportive, particularly maybe if you think about some of the intermodal and truck conducive type products is right. But we're trying not to worry about that. Control what we can control, create the product. And if we get a macro tailwind, it's just going to provide more upside to the story.

<Q – Christyne McGarvey>: Appreciate it. Thank you.

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

<A – Keith Creel>: Thank you. Listen, thank you for joining us again today and give us a chance to just give you an update. And I hope what you take away from this is, this company is in a strong position. We're in a strong position to achieve the guidance that we laid out in our multiyear plan. We're in a strong position to achieve the guidance that we've laid out for this year.

We've got to get through this potential work outage that's ahead of us. We've got to see what the macro does, but I can tell you, this is a very unique story. It's a unique network that's been created, that's unparalleled in this industry. We're one year old on a journey of our forever story, creating the most relevant rail network in North America.

I couldn't be more proud to work here and serve with these fine men and women that make this happen day in and day out, and we'll continue to work hard to meet and exceed our investors' expectations, our employees', commitments we made to them as well as our customers' commitments. I think that's a recipe for success, and I'm confident this team will achieve that, if not exceed that. Have a great day, and we'll talk to everyone soon.

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