RAILROAD WEEK IN REVIEW

August 2, 2024

"In the second quarter, the CPKC family delivered revenues of $3.8 billion, up 8%, strong volume growth, up 6%, an operating ratio of 61.8%, down 280 basis points versus last year, and EPS of $1.05, a 27% increase. We are extremely pleased with these results, and I can tell you that the numbers I just walked through do not happen by accident but through execution." CP President and CEO Keith Creel, July 30

Canadian Pacific on Tuesday posted its 2Q2024 earnings results. There are two sets of numbers: as reported GAAP numbers for today's combined KCS+CP and the "core-adjusted combined" or adjusted results.[1] I am using the former; the analyst community prefers to use the "adjusted" numbers. In other words, I'm doing what *is* rather that what *could have been* and *could be* going forward. Onward with the GAAP results.

CPKC quarterly freight revenue increased 14 percent to $C3.5 million on 1.1 million revenue units, up one percent. Double-digit carload (an intermodal box is a carload in this context) gains abound because of the footnoted accounting quirk. "Adjusted" revenue was up six points and units down four. The carload mix favors the carload sector with YTD double-digit volume gains in grain, energy/chems/plastics, and metals/minerals/consumer. Units ex coal and intermodal but including auto are 52 percent.

Operating income rose 34 percent to $C1.3 million as total expense was held to a five percent gain; the OR shed 542 bips to a highly respectable 64.8. Net income dropped 32 percent to $C905 million due to removal of a $C7 million merger-accounting credit a year ago. Cash flow from operations increased 29 percent to $C2.3 million, free cash flow after capex and divs jumped 56 percent to $C603,000. Retained earnings gained 18 percent to $C17.7 billion.

Out on the railroad, CPKC moved nine percent more GTMs on eight percent more fuel; KGTMs per gallon held at 1.03. RPU increased double-digits in grain, auto, and coal; system RPU was $C3,356, up 12 percent. On the call, Chief Marketing Officer John Brooks said, "Total grain revenues were up 17 percent; our franchise is benefiting from strong shipments of corn to the PNW, Mexico, and Alberta, along with increased shipments of soybeans and wheat to Mexico."

---

[1] "Interim Consolidated Financial Statements" include KCS as a consolidated subsidiary from April 14, 2023. For the period beginning on January 1, 2023 and ending on April 13, 2023, the Company's 100% interest in KCS was accounted for and reported as an equity-method investment. (See CP 2Q2024 Financials).

Potash revenues were up 24 percent on higher volumes for Canpotex to their Portland terminal. Energy, chemicals and plastics ("ECP") saw volume growth in the quarter driven by crude oil, LPG, plastics, renewable diesel, and refined fuels. Forest products were down a point in revenues on the same decline in volumes. Both STCCs fell, though "we are largely offsetting this headwind with synergy growth and extended line haul, shipping more lumber from Canadian producers down to our franchise in Texas and the Gulf markets."

Metals, minerals and consumer ("MMC") weathered weakness in frac sand and steel due to a labor event at an ArcelorMittal facility. Looking forward, says Brooks, "The volumes in the first half came in slightly better than we expected, and we're off to a strong start in Q3. While the big picture remains challenging in some areas, overall demand has stabilized and we continue to see strong differentiated growth from synergies, self-help initiatives and disciplined pricing."

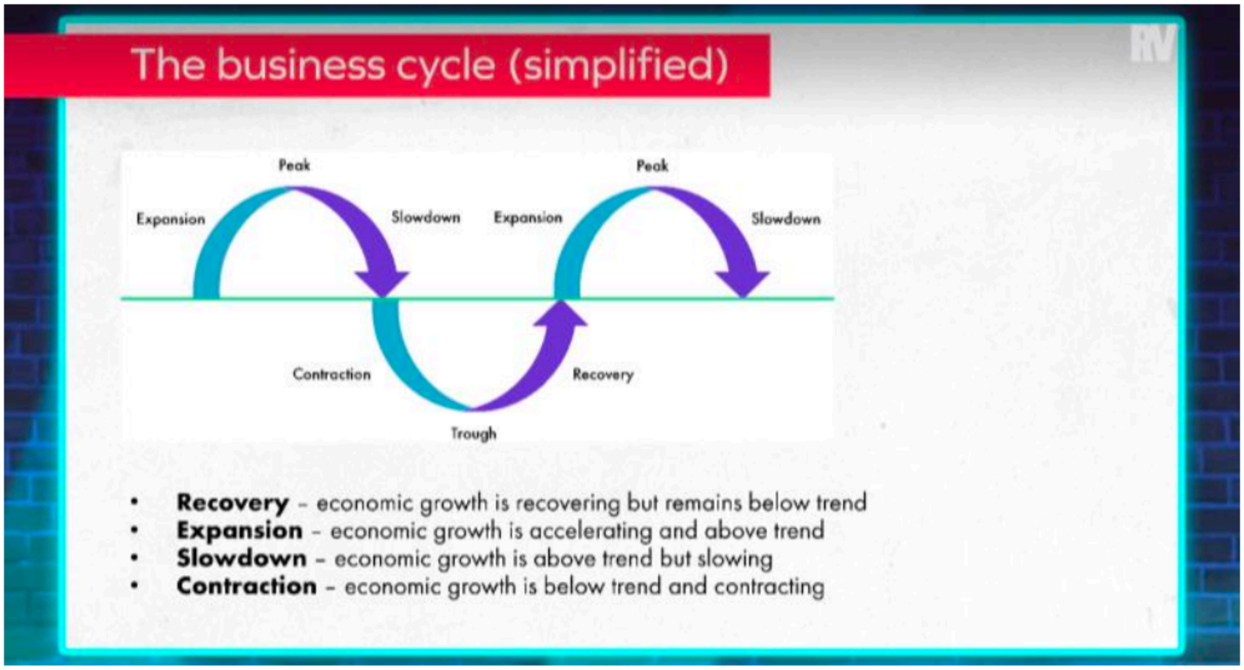
The day before the call we received the news that Pat Ottensmeyer, former KCS President and CEO, had passed away. He was only 67. I think Keith Creel's remarks before the earnings call were quite moving. "Pat's vision and leadership played a monumental role in the great history of Kansas City Southern as he helped reshape the railway industry.

"We've lost a truly remarkable leader and a cherished friend. We all knew him as a professional and a railroader and had nothing but respect and admiration for the material impact he made across so many aspects of our industry. And if you had the honor to have enjoyed a friendship with Pat as I did, words will never capture what a class gentleman and human being he was.

"Pat's legacy lives on. It can be seen in the work we do every day at CPKC. I'm also pleased to be hosting this call in Kansas City at our brand-new State of the Art US Operations Headquarters at new [ph] yard. This facility is just one small example of what would have never been possible without Pat's vision and strength as a leader. His contributions as a railroader and as a person will never be forgotten." Amen.

My inflation comments and observations seem to have a struck a chord with a number of WIR readers with shortline ownership and management experience. A charter reader who goes back to the very first WIRs more than two decade ago forwards this bit from Roth Capital Partners, an investment bank based in California with its global trading floor in Stamford, Connecticut:

"It has been a soft landing so far and markets priced to perfection have fully embraced the notion that growth will continue indefinitely. Yet, as we have discussed in the past, business cycles often have a transition period in which growth eases to trend after having been above trend earlier in the cycle, something that is often an oasis between expansion and contraction” See the downward pointing arrow on the left.



And so it’s beginning to look like the less than robust economic picture that each of the reporting railroads have reported thus far is likely to continue. The railroad stock charts continue to look promising, suggesting that institutional investors are beginning to see the light at the end of the tunnel— see the Trough-Recovery arrow above. I sure hope so.

The Railroad Week in Review, a compendium of railroad industry news, analysis, and comment, is sent as a PDF via e-mail 50 weeks a year. Individual subscriptions and subs for short lines with less than $12 million annual revenue are $175. Corporate subscriptions for Class I railroads and short line/ regional operators with more than $12 million annual revenue are $600 per year. To subscribe, click on the Week in Review tab at www.rblanchard.com. ***© 2024 Roy Blanchard***