ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with the Interim Consolidated Financial Statements and related notes for the three and six months ended June 30, 2016 in Item 1. Financial Statements, and other information in this report. Except where otherwise indicated, all financial information reflected herein is expressed in Canadian dollars.

For purposes of this report, all references herein to “CP,” “the Company,” “we,” “our” and “us” refer to CPRL, CPRL and its subsidiaries, CPRL and one or more of its subsidiaries, or one or more of CPRL's subsidiaries, as the context may require.

Available Information

CP makes available on or through its website www.cpr.ca free of charge, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports as soon as reasonably practicable after such reports are filed with or furnished to the Securities and Exchange Commission (“SEC”). Also, filings made pursuant to Section 16 of the Securities Exchange Act of 1934 (“Exchange Act”) with the SEC by our executive officers, directors and other reporting persons with respect to the Company's Common Shares are made available free of charge, through our website. Our website also contains charters for each of the committees of our Board of Directors, our corporate governance guidelines and our Code of Business Ethics. SEC filings made by CP are also accessible through the SEC’s website at www.sec.gov. The information on our website is not part of this quarterly report on Form 10-Q.

The Company has included the Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”) certifications regarding the Company's public disclosure required by Section 302 of the Sarbanes-Oxley Act of 2002 as an Exhibit to this report.

Executive Summary

Second Quarter of 2016 Results

Financial Performance - In the second quarter of 2016, CP reported Diluted earnings per share ("EPS") of $2.15 and Adjusted diluted EPS of $2.05, down 9% and 16% respectively, due in large part to a 12% drop in revenues. Revenue challenges in the quarter included lower-than-anticipated bulk volumes, devastating wildfires in northern Alberta and a strengthening Canadian dollar. The Company took action to adapt its cost structure as quickly as possible, but it was not able to fully mitigate the precipitous volume decline; as a result, second quarter operating ratio was up 110 basis points to 62.0%. Adjusted diluted EPS is defined and reconciled in Non-GAAP Measures and discussed further in Results of Operations of this Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Operating performance - CP’s continued focus on asset utilization and network investments resulted in improvements to a number of CP’s key operating metrics. The following metrics are discussed further in Performance Indicators of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

- Average train speed increased by 11% to 24.1 miles per hour;
- Average train weight increased by 3% to 8,540 tons;
- Average train length increased by 4% to 7,275 feet; and
- Average terminal dwell time improved by 3% to 6.5 hours.

Recent Developments

- On April 20, 2016, CP announced a new normal course issuer bid ("NCIB") to repurchase, for cancellation, up to 6.91 million of its Common Shares, which received Toronto Stock Exchange ("TSX") approval on April 28, 2016. As at June 30, 2016, CP had repurchased 5.13 million shares under the NCIB.

- Also on April 20, 2016, CP announced an increase to the Company's quarterly dividend to $0.50 per share from $0.35 per share.

- On April 20, 2016, the Company announced that Mr. Robert Johnson was appointed Executive Vice-President, Operations.

- On July 19, 2016, Dr. Anthony R. Melman resigned as a member of the Company’s Board of Directors.

Performance Indicators

The following table lists the key measures of the Company's operating performance:

	For the three months ended June 30			For the six months ended June 30		
	2016	2015[(1)]	% Change	**2016**	2015[(1)]	% Change
Operations Performance						
Gross ton-miles ("GTMs") (millions)	**57,460**	66,598	(14)	**119,432**	132,682	(10)
Train miles (thousands)	**7,291**	8,705	(16)	**15,155**	17,340	(13)
Average train weight – excluding local traffic (tons)	**8,540**	8,253	3	**8,518**	8,218	4
Average train length – excluding local traffic (feet)	**7,275**	6,989	4	**7,188**	6,881	4
Average terminal dwell (hours)	**6.5**	6.7	(3)	**6.7**	8.6	(22)
Average train speed (mph)	**24.1**	21.7	11	**23.7**	20.5	16
Fuel efficiency (U.S. gallons of locomotive fuel consumed / 1,000 GTMs)	**0.979**	0.993	(1)	**0.989**	1.020	(3)
Total employees (average)	**12,341**	14,195	(13)	**12,387**	14,280	(13)
Total employees (end of period)	**11,988**	14,071	(15)	**11,988**	14,071	(15)
Workforce (end of period)	**12,033**	14,128	(15)	**12,033**	14,128	(15)
Safety Indicators						
FRA personal injuries per 200,000 employee-hours	**1.30**	1.44	(10)	**1.37**	1.74	(21)
FRA train accidents per million train miles	**0.50**	1.35	(63)	**0.72**	1.41	(49)

(1) Certain figures have been revised to conform with current presentation or have been updated to reflect new information.

Operations Performance

Three months ended June 30, 2016 compared to the three months ended June 30, 2015

- **GTMs** are defined as the movement of total train weight over a distance of one mile. Total train weight comprises the weight of the freight cars, their contents, and any inactive locomotives. An increase in GTMs indicates additional workload. GTMs for the second quarter of 2016 were 57,460 million, a decrease of 14% compared with 66,598 million in the same period of 2015. This decrease was primarily due to a drop in volumes in the Crude, Potash and Canadian Grain lines of business.

- **Train miles** decreased by 16% for the second quarter of 2016 compared to the same period of 2015. This reflects the impact of lower volumes and continuous improvements in operating efficiency from longer, heavier trains.

- The **average train weight** is defined as the average gross weight of CP trains, both loaded and empty. This excludes trains in short-haul service, work trains used to move CP's track equipment and materials, and the haulage of other railways' trains on CP's network. Average train weight increased by 3% for the second quarter of 2016 compared to the same period of 2015. This increase was due to improvements made in operating plan efficiency.

- The **average train length** is defined as the sum of each car length multiplied by the distance travelled, divided by train miles. Local trains are excluded from this measure. Average train length increased by 4% for the second quarter of 2016 compared to the same period of 2015. Similar to benefits to the average train weight, this was also due to improvements made in operating plan efficiency.

- The **average terminal dwell** is defined as the average time a freight car resides within terminal boundaries expressed in hours. The timing starts with a train arriving in the terminal, a customer releasing the car to the Company, or a car arriving at interchange from another railway. The timing ends when the train leaves, a customer receives the car from CP, or the freight car is transferred to another railway. Freight cars are excluded if they are being stored at the terminal or used in track repairs. Average terminal dwell decreased by 3% in the second quarter of 2016 compared to the same period of 2015. This favourable decrease was primarily due to continued improvements in yard operating performance.

- The **average train speed** is defined as a measure of the line-haul movement from origin to destination including terminal dwell hours. It is calculated by dividing the total train miles travelled by the total train hours operated. This calculation does not include delay time related to customer or foreign railways and excludes the time and distance travelled by: i) trains used in or around CP's yards; ii) passenger trains; and iii) trains used for repairing track. Average train speed increased by 11% in the second quarter of 2016 compared to the same period of 2015. This favourable increase was primarily due to improved train design and operating plan execution.

- **Fuel efficiency** improved by 1% in the second quarter of 2016 compared to the same period of 2015. Improvements in fuel efficiency were a result of increased locomotive productivity, operational fluidity and execution of the Company's fuel conservation strategies.

Six months ended June 30, 2016 compared to the six months ended June 30, 2015

- **GTMs** for the first six months of 2016 were 119,432 million, a decrease of 10% compared with 132,682 million in the same period of 2015. This decrease was primarily due to a drop in volumes in the Crude, Export Potash and Coal lines of business.

- **Train miles** decreased by 13% for the first six months of 2016 compared to the same period of 2015. This reflects the impact of lower volumes and continuous improvements in operating efficiency from longer, heavier trains.

- **Average train weight** increased by 4% for the first six months of 2016 compared to the same period of 2015. This increase was due to improvements made in operating plan efficiency.

- **Average train length** increased by 4% for the first six months of 2016 from the same period of 2015. This favourable increase was also due to improvements made in operating plan efficiency.

- **Average terminal dwell** decreased by 22% in the first six months of 2016 compared to the same period of 2015. This favourable decrease was primarily due to continued improvements in yard operating performance.

- **Average train speed** increased by 16% in the first six months of 2016 compared to the same period of 2015. This favourable increase was primarily due to improved train design and operating plan execution.

- **Fuel efficiency** improved by 3% in the first six months of 2016 compared to the same period of 2015. Improvements in fuel efficiency were a result of increased locomotive productivity, operational fluidity and execution of the Company's fuel conservation strategies.

Total Employees and Workforce

An employee is defined by the Company as an individual currently engaged in full-time or part-time employment with CP. Employees could be engaged in a full-time, part-time or seasonal capacity. The average number of total employees decreased by 13% in the second quarter and first six months of 2016, compared to the same periods of 2015. This reduction was primarily due to lower volumes, improved operational efficiency and natural attrition.

The Company's workforce is defined as total employees, plus contractors and consultants. The Company's reduction of total workforce during 2016 has been consistent with the reduction in the number of total employees. As at June 30, 2016, the total workforce was 12,033, a decrease of 866 or 7%, when compared to 12,899 as at December 31, 2015. As at June 30, 2016, the total workforce decreased by 2,095 compared to June 30, 2015.

Safety Indicators

Safety is a key priority and core strategy for CP’s management, employees and Board of Directors. The Company’s two main safety indicators – personal injuries and train accidents – follow strict U.S. Federal Railroad Administration (“FRA”) reporting guidelines.

The FRA personal injury rate per 200,000 employee-hours is the number of personal injuries multiplied by 200,000 and divided by total employee hours. Personal injuries are defined as injuries that require employees to lose time away from work, modify their normal duties or obtain medical treatment beyond minor first aid. FRA employee-hours are the total hours worked, excluding vacation and sick time, by all employees, excluding contractors. The FRA personal injury rate per 200,000 employee-hours for CP was 1.30 in the second quarter of 2016, down from 1.44 in the same period of 2015. For the first six months of 2016, the FRA personal injury rate per 200,000 employee-hours for CP was 1.37, down from 1.74 in the same period of 2015. The FRA train accidents per million train miles was 0.50 in the second quarter of 2016, a decrease from 1.35 in the same period of 2015. For the first six months of 2016, FRA train accidents per million train miles was 0.72, a decrease from 1.41 in the same period of 2015.

Financial Highlights

(in millions, except per share data, percentages and ratios)	For the three months ended June 30		For the six months ended June 30	
	2016	2015	**2016**	2015
Financial Performance				
Revenues	**$ 1,450**	$ 1,651	**$ 3,041**	$ 3,316
Operating income	**551**	646	**1,204**	1,258
Net income	**328**	390	**868**	710
Adjusted income(1)	**312**	404	**696**	779
Basic earnings per share	**2.16**	2.38	**5.70**	4.32
Diluted earnings per share	**2.15**	2.36	**5.67**	4.28
Adjusted diluted earnings per share(1)	**2.05**	2.45	**4.55**	4.70
Dividends declared per share	**0.50**	0.35	**0.85**	0.70
Cash provided by operating activities	**512**	585	**730**	1,140
Free cash(1)	**137**	173	**66**	485
Operating ratio(2)	**62.0%**	60.9%	**60.4%**	62.1%

	As at June 30, 2016	As at December 31, 2015
Financial Position		
Total assets	**$ 19,068**	$ 19,637
Total long-term obligations(3)	**8,460**	9,012
Shareholders' equity	**4,691**	4,796

	For the twelve months ended June 30	
	2016	2015
Financial Ratios		
Return on invested capital ("ROIC")(1)	**14.7%**	15.0%
Adjusted ROIC(1)	**14.9%**	15.7%

(1) These measures have no standardized meanings prescribed by accounting principles generally accepted in the United States of America ("GAAP") and, therefore, may not be comparable to similar measures presented by other companies. These measures are defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

(2) Operating ratio is defined as operating expenses divided by revenues, further discussed in Results of Operations of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

(3) Excludes deferred income taxes: $3,512 million and $3,391 million; and other non-financial deferred liabilities of $960 and $991 million at June 30, 2016 and December 31, 2015, respectively.

Results of Operations

Three months ended June 30, 2016 compared to the three months ended June 30, 2015

Income

Operating income was $551 million in the second quarter of 2016, a decrease of $95 million, or 15%, from $646 million in the same period of 2015. This decrease was primarily due to lower volumes. The northern Alberta wildfires contributed to an estimated $29M decline in Operating income with a significant decrease in volumes, in addition to negatively impacting fuel input costs without triggering a commensurate offsetting impact to benchmark fuel recovery prices. Operating income for the second quarter of 2016 was also negatively impacted by the timing effect of the customary lag in adjustments to fuel surcharge program in periods of significant fuel price changes.

This decrease in operating income was partially offset by:

- efficiencies generated from improved operating performance and asset utilization;
- higher defined benefit pension plan income of $22 million; and
- the favourable impact of the change in foreign exchange ("FX") of $17 million.

Net income was $328 million in the second quarter of 2016, a decrease of $62 million, or 16%, from $390 million in the same period of 2015. This decrease was primarily due to lower Operating income and higher interest expense on new debt issued in 2015. This was partially offset by a decrease in Income tax expense due to lower taxable earnings along with a lower effective tax rate compared to 2015 and the favourable impact of FX translation on U.S. dollar-denominated debt.

Adjusted income, defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, was $312 million in the second quarter of 2016, a decrease of $92 million, or 23%, from $404 million in the same period of 2015. This decrease was due to the same factors discussed above for the decrease in Net income, except that Adjusted income excluded the favourable impact of FX translation on U.S. dollar-denominated debt.

Diluted Earnings per Share

Diluted earnings per share was $2.15 in the second quarter of 2016, a decrease of $0.21, or 9% from $2.36 in the same period of 2015. Adjusted diluted EPS, defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, was $2.05 in the second quarter of 2016, a decrease of $0.40, or 16%, from $2.45 in the same period of 2015. These decreases were primarily due to lower Net income and Adjusted income, respectively, partially offset by lower average outstanding shares due to the Company's share repurchase program.

Operating Ratio

The Operating ratio provides the percentage of revenues used to operate the railway. A lower percentage normally indicates higher efficiency in the operation of the railway. The Company's Operating ratio was 62.0% in the second quarter of 2016, 110 basis point higher from 60.9% in the same period of 2015. This increase was primarily due to lower volumes, partially offset by efficiencies generated from improved operating performance and asset utilization, and higher defined benefit pension plan income.

Return on Invested Capital (ROIC)

ROIC is a measure of how productively the Company uses its long-term capital investments, representing critical indicators of good operating and investment decisions made by management, and is an important performance criteria in determining certain elements of the Company's long-term incentive plan. ROIC was 14.7% for the twelve months ended June 30, 2016, a 30 basis point decrease compared to 15.0% for the twelve months ended June 30, 2015. Adjusted ROIC was 14.9% for the twelve months ended June 30, 2016, an 80 basis point decrease compared to 15.7% for the twelve months ended June 30, 2015. These decreases were largely due to lower volumes experienced during 2016. ROIC and Adjusted ROIC are defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Six months ended June 30, 2016 compared to the six months ended June 30, 2015

Income

Operating income was $1,204 million in the first six months of 2016, a decrease of $54 million, or 4%, from $1,258 million in the same period of 2015. This decrease was primarily due to lower volumes and higher wage and benefit inflation of 3%. The northern Alberta wildfires contributed to the significant decrease in volumes, in addition to negatively impacting fuel input costs without a commensurate impact to benchmark fuel recovery prices. This decrease was partially offset by:

- efficiencies generated from improved operating performance and asset utilization;
- the favourable impact of the change in FX of $71 million;
- higher defined benefit pension plan income of $55 million; and
- lower casualty expense of $12 million (excluding an unfavourable FX impact of $2 million).

Net income was $868 million in the first six months of 2016, an increase of $158 million, or 22%, from $710 million in the same period of 2015. This increase was primarily due to the favourable impact of FX translation on U.S. dollar-denominated debt and a decrease in Income tax expense due to lower taxable earnings along with lower effective tax rate compared to 2015. This increase was partially offset by lower operating income and higher interest expense on new debt issued in 2015.

Adjusted income, defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, was $696 million in the first six months of 2016, a decrease of $83 million, or 11%, from $779 million in the same period of 2015. This decrease was due to the factors discussed above for Operating income and Net income, excluding the favourable impact of FX translation on U.S. dollar-denominated debt.

Diluted Earnings per Share

Diluted earnings per share was $5.67 in the first six months of 2016, an increase of $1.39, or 32% from $4.28 in the same period of 2015. This increase was primarily due to higher Net income and lower average outstanding shares due to the Company's share repurchase program.

Adjusted diluted EPS was $4.55 in the first six months of 2016, a decrease of $0.15, or 3%, from $4.70 in the same period of 2015. This decrease was primarily due to lower Adjusted income, which excludes the gain on FX translation on U.S. dollar-denominated debt, partially offset by lower average outstanding shares due to the Company's share repurchase program.

Operating Ratio

The Company's Operating ratio was 60.4% in the first six months of 2016, a 170 basis point improvement from 62.1% in the same period of 2015. This improvement was primarily due to efficiencies generated from improved operating performance and asset utilization, and higher defined benefit pension plan income. This improvement was partially offset by lower volumes.

Impact of FX on Earnings

Fluctuations in FX affect the Company's results because U.S. dollar-denominated revenues and expenses are translated into Canadian dollars. U.S. dollar-denominated revenues and expenses increase (decrease) when the Canadian dollar weakens (strengthens) in relation to the U.S. dollar. The following tables indicate the average and periodic exchange rates when converting U.S. dollars to Canadian dollars for the three and six months ended June 30, 2016 and the comparative periods in 2015.

Canadian to U.S. dollar				
Average exchange rates		**2016**		2015
For the three months ended – June 30	**$**	**1.29**	$	1.23
For the six months ended – June 30	**$**	**1.34**	$	1.23

Canadian to U.S. dollar				
Exchange rates		**2016**		2015
Beginning of year – January 1	**$**	**1.38**	$	1.16
Beginning of quarter – April 1	**$**	**1.30**	$	1.27
End of quarter – June 30	**$**	**1.29**	$	1.25

In the second quarter of 2016, the impact of a stronger U.S. dollar resulted in an increase in total revenues of $40 million, an increase in total operating expenses of $23 million and an increase in interest expense of $3 million from the same period in 2015.

Similarly, in the first six months of 2016, the impact of a stronger U.S. dollar resulted in an increase in total revenues of $148 million, an increase in total operating expenses of $77 million and an increase in interest expense of $10 million from the same period in 2015.

The impact of FX on total revenues and operating expenses is discussed further in Item 3. Quantitative and Qualitative Disclosures About Market Risk, Foreign Exchange Risk.

Impact of Fuel Price on Earnings

Fluctuations in fuel prices affect the Company's results because fuel expense constitutes a significant portion of CP's operating costs. As fuel prices fluctuate, there will be a timing impact on earnings. The following table indicates the average fuel price for the three and six months ended June 30, 2016 and the comparative periods in 2015.

Average Fuel Price				
(U.S. dollars per U.S. gallon)		**2016**		2015
For the three months ended – June 30	**$**	**1.82**	$	2.30
For the six months ended – June 30	**$**	**1.64**	$	2.31

In the second quarter of 2016, the impact of lower fuel prices resulted in a decrease in total revenues of $53 million and a decrease in total operating expenses of $33 million from the same period in 2015. The results of the second quarter of 2016 were negatively impacted by the timing effect of the customary lag in adjustments to fuel recovery prices in periods of significant fuel price changes. A portion of the adverse impact, however, is not attributable to timing, as the wildfires in northern Alberta negatively impacted fuel input costs by an estimated $9 million without triggering a commensurate offsetting impact to benchmark fuel recovery prices.

Similarly, in the first six months of 2016, the impact of lower fuel prices resulted in a decrease in total revenues of $135 million and a decrease in total operating expenses of $100 million from the same period in 2015.

Impact of Share Price on Earnings

Fluctuations in the Common Share price affect the Company's operating expenses because share-based liabilities are fair valued. The following tables indicate the opening and closing CP Common Share Price on the TSX and the New York Stock Exchange for the three and six months ended June 30, 2016 and the comparative periods in 2015.

CP Common Share Price *Toronto Stock Exchange (in Canadian dollars)*		**2016**		2015
Opening Common Share Price, as at January 1	**$**	**176.73**	$	223.75
Ending Common Share Price, as at March 31	**$**	**172.55**	$	231.90
Ending Common Share Price, as at June 30	**$**	**166.33**	$	200.02
Change in Common Share Price for the three months ended June 30	**$**	**(6.22)**	$	(31.88)
Change in Common Share Price for the six months ended June 30	**$**	**(10.40)**	$	(23.73)

CP Common Share Price *New York Stock Exchange (in U.S. dollars)*		**2016**		2015
Opening Common Share Price, as at January 1	**$**	**127.60**	$	192.69
Ending Common Share Price, as at March 31	**$**	**132.69**	$	182.70
Ending Common Share Price, as at June 30	**$**	**128.79**	$	160.23
Change in Common Share Price for the three months ended June 30	**$**	**(3.90)**	$	(22.47)
Change in Common Share Price for the six months ended June 30	**$**	**1.19**	$	(32.46)

In the second quarter of 2016, the impact of the change in Common Share price resulted in a decrease in stock-based compensation expense of $3 million compared to a decrease of $25 million in the same period in 2015.

In the first six months of 2016, the impact of the change in Common Share price resulted in a decrease in stock-based compensation expense of $5 million compared to a decrease of $18 million in the same period in 2015.

The impact of share price on stock-based compensation is discussed further in Item 3. Quantitative and Qualitative Disclosures About Market Risk, Share Price Impact on Stock-Based Compensation.

Operating Revenues

The Company's revenues are primarily derived from transporting freight. Non-freight revenue is generated from leasing of certain assets, contracts with passenger service operators, switching fees, transload activities and logistical management services. Changes in freight volumes generally contribute to corresponding changes in freight revenues and certain variable expenses, such as fuel, equipment rents and crew costs.

						2016 vs. 2015		
For the three months ended June 30		**2016**		2015	% Change		Total Change	FX Impact[2]
Freight revenues (in millions)[1]	**$**	**1,406**	$	1,610	(13)	$	(204)	$ 40
Non-freight revenues (in millions)		**44**		41	7		3	—
Total revenues (in millions)	**$**	**1,450**	$	1,651	(12)	$	(201)	$ 40
Carloads (in thousands)		**614**		668	(8)		(54)	N/A
Revenue ton-miles (in millions)		**32,091**		36,281	(12)		(4,190)	N/A
Freight revenue per carload (dollars)	**$**	**2,291**	$	2,409	(5)	$	(118)	
Freight revenue per revenue ton-miles (cents)		**4.38**		4.44	(1)		(0.06)	

[1] Freight revenues include fuel surcharge revenues of $20 million in 2016, and $73 million in 2015.
[2] FX impact is a component of the Total Change.

- **Freight revenues** were $1,406 million in the second quarter of 2016, a decrease of $204 million, or 13% from $1,610 million in the same period of 2015. This decrease was primarily due to an overall decline in volumes. In particular, there was an estimated $20 million decline in revenues as a direct result of the northern Alberta wildfires. Additionally, revenues from other freight activities declined by $30 million primarily due to reductions in haulage and ancillary revenues. Lower fuel prices also reduced fuel surcharge revenue by $53 million. The favourable impact of the change in FX of $40 million partially offset these decreases.

- **RTMs** are defined as the movement of one revenue-producing ton of freight over a distance of one mile. RTMs measure the relative weight and distance of rail freight moved by the Company. RTMs for the second quarter of 2016 were 32,091 million, a decrease of 12% compared with 36,281 million in the same period of 2015. This decrease was primarily due to a drop in volumes in the Crude, Potash and Canadian Grain lines of business. Increased shipments in the Forest Products line of business partially offset the decrease in RTMs.

- **Non-freight revenues** were $44 million in the second quarter of 2016, an increase of $3 million, or 7% from $41 million in the same period of 2015. This increase was primarily due to higher revenues from logistics services and transload revenues following the acquisition of Steelcare Inc. in the third quarter of 2015.

			2016 vs. 2015		
For the six months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[2]
Freight revenues (in millions)[1]	**$ 2,954**	$ 3,240	(9)	$ (286)	$ 147
Non-freight revenues (in millions)	**87**	76	14	11	1
Total revenues (in millions)	**$ 3,041**	$ 3,316	(8)	$ (275)	$ 148
Carloads (in thousands)	**1,228**	1,310	(6)	(82)	N/A
Revenue ton-miles (in millions)	**66,426**	72,344	(8)	(5,918)	N/A
Freight revenue per carload (dollars)	**$ 2,405**	$ 2,473	(3)	$ (68)	
Freight revenue per revenue ton-miles (cents)	**4.45**	4.48	(1)	(0.03)	

[1] Freight revenues include fuel surcharge revenues of $42 million in 2016, and $177 million in 2015.
[2] FX impact is a component of the Total Change.

- **Freight revenues** were $2,954 million in the first six months of 2016, a decrease of $286 million, or 9% from $3,240 million in the same period of 2015. This decrease was primarily due to an overall decline in volumes and the impact of lower fuel prices on fuel surcharge revenue of $135 million. The favourable impact of the change in FX of $147 million partially offset this decrease.

- **RTMs** for the first six months of 2016 were 66,426 million, a decrease of 8% compared with 72,344 million in the same period of 2015. This decrease was primarily due to a drop in volumes in the Crude, Potash, Coal and Metals, Minerals & Consumer Products lines of business.

- **Non-freight revenues** were $87 million in the first six months of 2016, an increase of $11 million, or 14% from $76 million in the same period of 2015. This increase was primarily due to higher transload revenues following the acquisition of Steelcare Inc. in the third quarter of 2015, and from logistics services and leasing revenues.

Lines of Business

Canadian Grain

			2016 vs. 2015		
For the three months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[1]
Freight revenues (in millions)	**$ 201**	$ 255	(21)	$ (54)	$ 3
Carloads (in thousands)	**64**	72	(11)	(8)	N/A
Revenue ton-miles (in millions)	**5,727**	6,622	(14)	(895)	N/A
Freight revenue per carload (dollars)	**$ 3,153**	$ 3,546	(11)	$ (393)	
Freight revenue per revenue ton-mile (cents)	**3.51**	3.86	(9)	(0.35)	

[1] FX impact is a component of the Total Change.

Canadian grain revenue was $201 million in the second quarter of 2016, a decrease of $54 million, or 21% from $255 million in the same period of 2015. This decrease was primarily due to a decline in volumes and lower freight rates that reflect the decrease in the Maximum Revenue Entitlement for Canadian regulated grain in crop year 2015/2016. The favourable impact of the change in FX partially offset this decrease.

For the six months ended June 30		2016		2015	% Change		2016 vs. 2015 Total Change		FX Impact[1]
Freight revenues (in millions)	$	**455**	$	511	(11)	$	(56)	$	11
Carloads (in thousands)		**130**		133	(2)		(3)		N/A
Revenue ton-miles (in millions)		**12,668**		13,027	(3)		(359)		N/A
Freight revenue per carload (dollars)	$	**3,513**	$	3,852	(9)	$	(339)		
Freight revenue per revenue ton-mile (cents)		**3.60**		3.92	(8)		(0.32)		

(1) FX impact is a component of the Total Change.

Canadian grain revenue was $455 million in the first six months of 2016, a decrease of $56 million, or 11% from $511 million in the same period of 2015. This decrease was primarily due to lower freight rates that reflect the decrease in the Maximum Revenue Entitlement for Canadian regulated grain in crop year 2015/2016 and a decline in volumes. This decrease was partially offset by the favourable impact of the change in FX.

U.S. Grain

For the three months ended June 30		2016		2015	% Change		2016 vs. 2015 Total Change		FX Impact[1]
Freight revenues (in millions)	$	**101**	$	106	(5)	$	(5)	$	5
Carloads (in thousands)		**35**		33	6		2		N/A
Revenue ton-miles (in millions)		**2,242**		2,184	3		58		N/A
Freight revenue per carload (dollars)	$	**2,946**	$	3,187	(8)	$	(241)		
Freight revenue per revenue ton-mile (cents)		**4.51**		4.85	(7)		(0.34)		

(1) FX impact is a component of the Total Change.

U.S. grain revenue was $101 million in the second quarter of 2016, a decrease of $5 million, or 5% from $106 million in the same period of 2015. The decrease was primarily due to lower freight rates and lower fuel surcharge revenue, partially offset by the favourable impact of the change in FX and higher volumes.

For the six months ended June 30		2016		2015	% Change		2016 vs. 2015 Total Change		FX Impact[1]
Freight revenues (in millions)	$	**214**	$	243	(12)	$	(29)	$	22
Carloads (in thousands)		**69**		73	(5)		(4)		N/A
Revenue ton-miles (in millions)		**4,556**		5,128	(11)		(572)		N/A
Freight revenue per carload (dollars)	$	**3,109**	$	3,308	(6)	$	(199)		
Freight revenue per revenue ton-mile (cents)		**4.71**		4.74	(1)		(0.03)		

(1) FX impact is a component of the Total Change.

U.S. grain revenue was $214 million in the first six months of 2016, a decrease of $29 million, or 12% from $243 million in the same period of 2015. The decrease was primarily due to a decline in volumes and lower fuel surcharge revenue. The favourable impact of the change in FX partially offset this decrease.

Coal

For the three months ended June 30		2016		2015	% Change		2016 vs. 2015 Total Change		FX Impact[1]
Freight revenues (in millions)	$	**149**	$	167	(11)	$	(18)	$	2
Carloads (in thousands)		**75**		84	(11)		(9)		N/A
Revenue ton-miles (in millions)		**5,394**		5,894	(8)		(500)		N/A
Freight revenue per carload (dollars)	$	**2,001**	$	1,996	—	$	5		
Freight revenue per revenue ton-mile (cents)		**2.76**		2.83	(2)		(0.07)		

(1) FX impact is a component of the Total Change.

Coal revenue was $149 million in the second quarter of 2016, a decrease of $18 million, or 11% from $167 million in the same period of 2015. This decrease was primarily due to a decline in volumes and lower fuel surcharge revenue. Higher freight rates and the favourable impact of the change in FX partially offset this decrease.

			2016 vs. 2015		
For the six months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[(1)]
Freight revenues (in millions)	**$ 294**	$ 327	(10)	$ (33)	$ 5
Carloads (in thousands)	**147**	166	(11)	(19)	N/A
Revenue ton-miles (in millions)	**10,742**	11,598	(7)	(856)	N/A
Freight revenue per carload (dollars)	**$ 2,001**	$ 1,968	2	$ 33	
Freight revenue per revenue ton-mile (cents)	**2.73**	2.82	(3)	(0.09)	

(1) FX impact is a component of the Total Change.

Coal revenue was $294 million in the first six months of 2016, a decrease of $33 million, or 10% from $327 million in the same period of 2015. As in the second quarter, this decrease was primarily due to a decline in volumes and lower fuel surcharge revenue. Higher freight rates and the favourable impact of the change in FX partially offset this decrease.

Potash

			2016 vs. 2015		
For the three months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[(1)]
Freight revenues (in millions)	**$ 79**	$ 106	(25)	$ (27)	$ 2
Carloads (in thousands)	**28**	37	(24)	(9)	N/A
Revenue ton-miles (in millions)	**3,497**	4,514	(23)	(1,017)	N/A
Freight revenue per carload (dollars)	**$ 2,800**	$ 2,854	(2)	$ (54)	
Freight revenue per revenue ton-mile (cents)	**2.27**	2.34	(3)	(0.07)	

(1) FX impact is a component of the Total Change.

Potash revenue was $79 million in the second quarter of 2016, a decrease of $27 million, or 25% from $106 million in the same period of 2015. This decrease was primarily due to a decline in Export Potash volumes and lower fuel surcharge revenue, partially offset by the favourable impact of the change in FX.

			2016 vs. 2015		
For the six months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[(1)]
Freight revenues (in millions)	**$ 161**	$ 199	(19)	$ (38)	$ 8
Carloads (in thousands)	**55**	68	(19)	(13)	N/A
Revenue ton-miles (in millions)	**6,682**	8,189	(18)	(1,507)	N/A
Freight revenue per carload (dollars)	**$ 2,928**	$ 2,933	—	$ (5)	
Freight revenue per revenue ton-mile (cents)	**2.42**	2.43	—	(0.01)	

(1) FX impact is a component of the Total Change.

Potash revenue was $161 million in the first six months of 2016, a decrease of $38 million, or 19% from $199 million in the same period of 2015. As in the second quarter, this decrease was primarily due to a decline in Export Potash volumes and lower fuel surcharge revenue, partially offset by the favourable impact of the change in FX.

Fertilizers and Sulphur

For the three months ended June 30	2016	2015	% Change	Total Change (2016 vs. 2015)	FX Impact[1] (2016 vs. 2015)
Freight revenues (in millions)	**$ 73**	$ 67	9	$ 6	$ 2
Carloads (in thousands)	**15**	15	—	—	N/A
Revenue ton-miles (in millions)	**1,019**	935	9	84	N/A
Freight revenue per carload (dollars)	**$ 4,981**	$ 4,508	10	$ 473	
Freight revenue per revenue ton-mile (cents)	**7.16**	7.12	1	0.04	

(1) FX impact is a component of the Total Change.

Fertilizers and sulphur revenue was $73 million in the second quarter of 2016, an increase of $6 million, or 9% from $67 million in the same period of 2015. This increase was primarily due to a shift in mix of traffic to more fertilizers, which generally has a higher freight rate than sulphur, and the favourable impact of the change in FX. Lower fuel surcharge revenue partially offset this increase.

For the six months ended June 30	2016	2015	% Change	Total Change (2016 vs. 2015)	FX Impact[1] (2016 vs. 2015)
Freight revenues (in millions)	**$ 154**	$ 138	12	$ 16	$ 7
Carloads (in thousands)	**31**	32	(3)	(1)	N/A
Revenue ton-miles (in millions)	**2,186**	2,050	7	136	N/A
Freight revenue per carload (dollars)	**$ 4,987**	$ 4,381	14	$ 606	
Freight revenue per revenue ton-mile (cents)	**7.04**	6.73	5	0.31	

(1) FX impact is a component of the Total Change.

Fertilizers and sulphur revenue was $154 million in the first six months of 2016, an increase of $16 million, or 12% from $138 million in the same period of 2015. This increase was primarily due to higher volumes, a shift in mix of traffic to more fertilizers with higher freight rate than sulphur, and the favourable impact of the change in FX. Lower fuel surcharge revenue was a partial offset.

Forest Products

For the three months ended June 30	2016	2015	% Change	Total Change (2016 vs. 2015)	FX Impact[1] (2016 vs. 2015)
Freight revenues (in millions)	**$ 70**	$ 61	15	$ 9	$ 2
Carloads (in thousands)	**17**	15	13	2	N/A
Revenue ton-miles (in millions)	**1,245**	1,061	17	184	N/A
Freight revenue per carload (dollars)	**$ 4,055**	$ 3,902	4	$ 153	
Freight revenue per revenue ton-mile (cents)	**5.59**	5.73	(2)	(0.14)	

(1) FX impact is a component of the Total Change.

Forest products revenue was $70 million in the second quarter of 2016, an increase of $9 million, or 15% from $61 million in the same period of 2015. This increase was due to higher volumes and the favourable impact of the change in FX, partially offset by lower fuel surcharge revenue.

For the six months ended June 30	2016	2015	% Change	Total Change (2016 vs. 2015)	FX Impact[1] (2016 vs. 2015)
Freight revenues (in millions)	**$ 141**	$ 118	19	$ 23	$ 7
Carloads (in thousands)	**34**	30	13	4	N/A
Revenue ton-miles (in millions)	**2,402**	2,080	15	322	N/A
Freight revenue per carload (dollars)	**$ 4,135**	$ 3,880	7	$ 255	
Freight revenue per revenue ton-mile (cents)	**5.87**	5.69	3	0.18	

(1) FX impact is a component of the Total Change.

Forest products revenue was $141 million in the first six months of 2016, an increase of $23 million, or 19% from $118 million in the same period of 2015. This increase was due to higher volumes and the favourable impact of the change in FX. Lower fuel surcharge revenue partially offset this increase.

Chemicals and Plastics

			2016 vs. 2015		
For the three months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[1]
Freight revenues (in millions)	**$ 162**	$ 171	(5)	$ (9)	$ 7
Carloads (in thousands)	**49**	51	(4)	(2)	N/A
Revenue ton-miles (in millions)	**3,348**	3,423	(2)	(75)	N/A
Freight revenue per carload (dollars)	**$ 3,266**	$ 3,354	(3)	$ (88)	
Freight revenue per revenue ton-mile (cents)	**4.84**	4.99	(3)	(0.15)	

[1] FX impact is a component of the Total Change.

Chemicals and plastics revenue was $162 million in the second quarter of 2016, a decrease of $9 million, or 5% from $171 million in the same period of 2015. This decrease was primarily due to lower fuel surcharge revenue and a decline in volumes, partially offset by the favourable impact of the change in FX.

			2016 vs. 2015		
For the six months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[1]
Freight revenues (in millions)	**$ 356**	$ 349	2	$ 7	$ 25
Carloads (in thousands)	**103**	102	1	1	N/A
Revenue ton-miles (in millions)	**7,010**	6,993	—	17	N/A
Freight revenue per carload (dollars)	**$ 3,443**	$ 3,427	—	$ 16	
Freight revenue per revenue ton-mile (cents)	**5.08**	4.99	2	0.09	

[1] FX impact is a component of the Total Change.

Chemicals and plastics revenue was $356 million in the first six months of 2016, an increase of $7 million, or 2% from $349 million in the same period of 2015. This increase was primarily due to the favourable impact of the change in FX, partially offset by lower fuel surcharge revenue.

Crude

			2016 vs. 2015		
For the three months ended June 30	**2016**	2015	% Change	Total Change	FX Impact[1]
Freight revenues (in millions)	**$ 24**	$ 81	(70)	$ (57)	$ 4
Carloads (in thousands)	**7**	19	(63)	(12)	N/A
Revenue ton-miles (in millions)	**854**	2,796	(69)	(1,942)	N/A
Freight revenue per carload (dollars)	**$ 3,248**	$ 4,294	(24)	$ (1,046)	
Freight revenue per revenue ton-mile (cents)	**2.83**	2.92	(3)	(0.09)	

[1] FX impact is a component of the Total Change.

Crude revenue was $24 million in the second quarter of 2016, a decrease of $57 million, or 70% from $81 million in the same period of 2015. This decrease was primarily due to a decline in volumes as a result of the fall in crude oil prices and the northern Alberta wildfires, along with lower fuel surcharge revenue. The favourable impact of the change in FX partially offset this decrease.

For the six months ended June 30		2016		2015	% Change	2016 vs. 2015 Total Change	FX Impact[1]
Freight revenues (in millions)	$	**95**	$	179	(47)	$ (84)	$ 15
Carloads (in thousands)		**24**		41	(41)	(17)	N/A
Revenue ton-miles (in millions)		**3,314**		5,828	(43)	(2,514)	N/A
Freight revenue per carload (dollars)	$	**3,927**	$	4,404	(11)	$ (477)	
Freight revenue per revenue ton-mile (cents)		**2.87**		3.09	(7)	(0.22)	

[1] FX impact is a component of the Total Change.

Crude revenue was $95 million in the first six months of 2016, a decrease of $84 million, or 47% from $179 million in the same period of 2015. This decrease was primarily due to a decline in volumes as a result of the fall in crude oil prices, lower fuel surcharge revenue and traffic mix changes that lowered the average freight revenue per revenue ton-mile. The favourable impact of the change in FX partially offset this decrease.

Metals, Minerals and Consumer Products

For the three months ended June 30		2016		2015	% Change	2016 vs. 2015 Total Change	FX Impact[1]
Freight revenues (in millions)	$	**140**	$	160	(13)	$ (20)	$ 6
Carloads (in thousands)		**50**		54	(7)	(4)	N/A
Revenue ton-miles (in millions)		**2,089**		2,172	(4)	(83)	N/A
Freight revenue per carload (dollars)	$	**2,800**	$	2,946	(5)	$ (146)	
Freight revenue per revenue ton-mile (cents)		**6.68**		7.37	(9)	(0.69)	

[1] FX impact is a component of the Total Change.

Metals, minerals and consumer products revenue was $140 million in the second quarter of 2016, a decrease of $20 million, or 13% from $160 million in the same period of 2015. This decrease was primarily due to traffic mix changes that lowered the average freight rate, reduced fuel surcharge revenue and a decline in volumes. The favourable impact of the change in FX partially offset this decrease.

For the six months ended June 30		2016		2015	% Change	2016 vs. 2015 Total Change	FX Impact[1]
Freight revenues (in millions)	$	**273**	$	319	(14)	$ (46)	$ 22
Carloads (in thousands)		**95**		109	(13)	(14)	N/A
Revenue ton-miles (in millions)		**3,896**		4,455	(13)	(559)	N/A
Freight revenue per carload (dollars)	$	**2,884**	$	2,911	(1)	$ (27)	
Freight revenue per revenue ton-mile (cents)		**7.00**		7.15	(2)	(0.15)	

[1] FX impact is a component of the Total Change.

Metals, minerals and consumer products revenue was $273 million in the first six months of 2016, a decrease of $46 million, or 14% from $319 million in the same period of 2015. This decrease was primarily due to a decline in volumes, traffic mix changes that lowered the average freight rate and reduced fuel surcharge revenue. The favourable impact of the change in FX partially offset this decrease.

Automotive

For the three months ended June 30	2016	2015	% Change	Total Change	FX Impact[(1)]
			2016 vs. 2015		
Freight revenues (in millions)	**$ 93**	$ 91	2	$ 2	$ 4
Carloads (in thousands)	**35**	36	(3)	(1)	N/A
Revenue ton-miles (in millions)	**495**	496	—	(1)	N/A
Freight revenue per carload (dollars)	**$ 2,629**	$ 2,541	3	$ 88	
Freight revenue per revenue ton-mile (cents)	**18.79**	18.37	2	0.42	

(1) FX impact is a component of the Total Change.

Automotive revenue was $93 million in the second quarter of 2016, an increase of $2 million, or 2% from $91 million in the same period of 2015. This increase was primarily due to the favourable impact of the change in FX and an increase in the average freight rate, partially offset by lower fuel surcharge revenue.

For the six months ended June 30	2016	2015	% Change	Total Change	FX Impact[(1)]
			2016 vs. 2015		
Freight revenues (in millions)	**$ 184**	$ 173	6	$ 11	$ 12
Carloads (in thousands)	**68**	66	3	2	N/A
Revenue ton-miles (in millions)	**912**	915	—	(3)	N/A
Freight revenue per carload (dollars)	**$ 2,689**	$ 2,610	3	$ 79	
Freight revenue per revenue ton-mile (cents)	**20.15**	18.89	7	1.26	

(1) FX impact is a component of the Total Change.

Automotive revenue was $184 million in the first six months of 2016, an increase of $11 million, or 6% from $173 million in the same period of 2015. This increase was primarily due to increased volumes of higher rated short-haul traffic and the favourable impact of the change in FX, partially offset by lower fuel surcharge revenue.

Domestic Intermodal

For the three months ended June 30	2016	2015	% Change	Total Change	FX Impact[(1)]
			2016 vs. 2015		
Freight revenues (in millions)	**$ 177**	$ 192	(8)	$ (15)	$ 1
Carloads (in thousands)	**106**	106	—	—	N/A
Revenue ton-miles (in millions)	**2,996**	3,063	(2)	(67)	N/A
Freight revenue per carload (dollars)	**$ 1,668**	$ 1,812	(8)	$ (144)	
Freight revenue per revenue ton-mile (cents)	**5.91**	6.26	(6)	(0.35)	

(1) FX impact is a component of the Total Change.

Domestic intermodal revenue was $177 million in the second quarter of 2016, a decrease of $15 million, or 8% from $192 million in the same period of 2015. This decrease was primarily due to lower fuel surcharge revenue and a decline in volumes, partially offset by the favourable impact of the change in FX.

For the six months ended June 30	2016	2015	% Change	Total Change	FX Impact[(1)]
			2016 vs. 2015		
Freight revenues (in millions)	**$ 348**	$ 386	(10)	$ (38)	$ 4
Carloads (in thousands)	**204**	209	(2)	(5)	N/A
Revenue ton-miles (in millions)	**5,843**	6,087	(4)	(244)	N/A
Freight revenue per carload (dollars)	**$ 1,701**	$ 1,852	(8)	$ (151)	
Freight revenue per revenue ton-mile (cents)	**5.95**	6.35	(6)	(0.40)	

(1) FX impact is a component of the Total Change.

Domestic intermodal revenue was $348 million in the first six months of 2016, a decrease of $38 million, or 10% from $386 million in the same period of 2015. As in the second quarter, this decrease was primarily due to lower fuel surcharge revenue and a decline in volumes, partially offset by the favourable impact of the change in FX.

International Intermodal

For the three months ended June 30		2016		2015	% Change	Total Change		FX Impact[1]
					2016 vs. 2015			
Freight revenues (in millions)	**$**	**137**	$	153	(10) $	(16)	$	2
Carloads (in thousands)		**133**		146	(9)	(13)		N/A
Revenue ton-miles (in millions)		**3,185**		3,121	2	64		N/A
Freight revenue per carload (dollars)	**$**	**1,034**	$	1,047	(1) $	(13)		
Freight revenue per revenue ton-mile (cents)		**4.31**		4.90	(12)	(0.59)		

[1] FX impact is a component of the Total Change.

International intermodal revenue was $137 million in the second quarter of 2016, a decrease of $16 million, or 10% from $153 million in the same period of 2015. This decrease was primarily due to traffic mix changes that lowered the average freight rate as a result of fewer revenue generating moves of empty customer containers and lower fuel surcharge revenue. The favourable impact of the change in FX partially offset this decrease.

For the six months ended June 30		2016		2015	% Change	Total Change		FX Impact[1]
					2016 vs. 2015			
Freight revenues (in millions)	**$**	**279**	$	298	(6) $	(19)	$	9
Carloads (in thousands)		**268**		281	(5)	(13)		N/A
Revenue ton-miles (in millions)		**6,215**		5,994	4	221		N/A
Freight revenue per carload (dollars)	**$**	**1,042**	$	1,058	(2) $	(16)		
Freight revenue per revenue ton-mile (cents)		**4.49**		4.97	(10)	(0.48)		

[1] FX impact is a component of the Total Change.

International intermodal revenue was $279 million in the first six months of 2016, a decrease of $19 million, or 6% from $298 million in the same period of 2015. This decrease was primarily due to traffic mix changes that lowered the average freight rate as a result of fewer revenue generating moves of empty customer containers and lower fuel surcharge revenue. Higher volumes and the favourable impact of the change in FX partially offset this decrease.

Operating Expenses

For the three months ended June 30 (in millions)		2016		2015	% Change	Total Change		FX Impact[1]
					2016 vs. 2015			
Compensation and benefits	**$**	**284**	$	308	(8) $	(24)	$	6
Fuel		**131**		185	(29)	(54)		8
Materials		**38**		45	(16)	(7)		—
Equipment rents		**44**		46	(4)	(2)		2
Depreciation and amortization		**161**		145	11	16		1
Purchased services and other		**241**		276	(13)	(35)		6
Total operating expenses	**$**	**899**	$	1,005	(11) $	(106)	$	23

[1] FX impact is a component of the Total Change.

Operating expenses were $899 million in the second quarter of 2016, a decrease of $106 million, or 11%, from $1,005 million in the same period of 2015. This decrease was primarily due to:

- lower volume variable expenses;
- efficiencies generated from improved operating performance and asset utilization;
- the favourable impact of $33 million from lower fuel prices; and
- higher defined benefit pension plan income of $22 million.

This decrease was partially offset by the unfavourable impact of the change in FX of $23 million.

For the six months ended June 30 (in millions)	2016	2015	2016 vs. 2015 % Change	2016 vs. 2015 Total Change	2016 vs. 2015 FX Impact[1]
Compensation and benefits	**$ 613**	$ 686	(11)	$ (73)	$ 18
Fuel	**256**	380	(33)	(124)	25
Materials	**94**	97	(3)	(3)	3
Equipment rents	**89**	88	1	1	5
Depreciation and amortization	**323**	291	11	32	5
Purchased services and other	**462**	516	(10)	(54)	21
Total operating expenses	**$ 1,837**	$ 2,058	(11)	$ (221)	$ 77

[1] FX impact is a component of the Total Change.

Operating expenses were $1,837 million in the first six months of 2016, a decrease of $221 million, or 11%, from $2,058 million in the same period of 2015. This decrease was primarily due to:

- the favourable impact of $100 million from lower fuel prices;
- lower volume variable expenses;
- efficiencies generated from improved operating performance and asset utilization; and
- higher defined benefit pension plan income of $55 million.

This decrease was partially offset by the unfavourable impact of the change in FX of $77 million.

Compensation and Benefits

Compensation and benefits expense includes employee wages, salaries, fringe benefits and stock-based compensation. Compensation and benefits expense was $284 million in the second quarter of 2016, a decrease of $24 million, or 8%, from $308 million in the same period of 2015. This decrease was primarily due to fewer employees and higher defined benefit pension plan income of $22 million.

This decrease was partially offset by:

- the impact of wage and benefit inflation of approximately 3%;
- the unfavourable impact of higher stock-based compensation of $7 million primarily driven by the smaller reduction in stock price compared to the same period in 2015; and
- the unfavourable impact of the change in FX of $6 million.

Compensation and benefits expense was $613 million in the first six months of 2016, a decrease of $73 million, or 11%, from $686 million in the same period of 2015. This decrease was primarily due to fewer employees and higher defined benefit pension plan income of $55 million. This decrease was partially offset by the impact of wage and benefit inflation of approximately 3% and the unfavourable impact of the change in FX of $18 million.

Fuel

Fuel expense consists mainly of fuel used by locomotives and includes provincial, state and federal fuel taxes. Fuel expense was $131 million in the second quarter of 2016, a decrease of $54 million, or 29%, from $185 million in the same period of 2015. This decrease was primarily due to:

- the favourable impact of $33 million from lower fuel prices;
- a reduction in workload, as measured by GTMs; and
- improvements in fuel efficiency of approximately 1%.

This decrease was partially offset by the unfavourable impact of the change in FX of $8 million.

Fuel expense was $256 million in the first six months of 2016, a decrease of $124 million, or 33%, from $380 million in the same period of 2015. This decrease was primarily due to:

- the favourable impact of $100 million from lower fuel prices;
- a reduction in workload, as measured by GTMs; and
- improvements in fuel efficiency of approximately 3%.

This decrease was partially offset by the unfavourable impact of the change in FX of $25 million.

Materials

Materials expense includes the cost of material used for track, locomotive, freight car and building maintenance and software sustainment. Materials expense was $38 million in the second quarter of 2016, a decrease of $7 million or 16%, from $45 million in the same period of 2015. This decrease was primarily due to lower volumes.

Materials expense was $94 million in the first six months of 2016, a decrease of $3 million or 3%, from $97 million in the same period of 2015. This decrease was primarily due to lower volumes, partially offset by the unfavourable impact of the change in FX of $3 million.

Equipment Rents

Equipment rents expense includes the cost associated with using other railways freight cars, intermodal equipment, and locomotives, net of rental income received from other railways for the use of CP's equipment. Equipment rents expense was $44 million in the second quarter of 2016, a decrease of $2 million or 4% from $46 million in the same period of 2015. This decrease was primarily due to the purchase or return of leased freight cars reducing rental expense by $3 million. This decrease was largely offset by the unfavourable impact of the change in FX of $2 million. Lower volumes resulted in an equal impact to CP's rental income and rental expense.

Equipment rents expense was $89 million in the first six months of 2016, an increase of $1 million or 1% from $88 million in the same period of 2015. This increase was primarily due to the return of subleased locomotives and freight cars reducing rental income by $5 million, and the unfavourable impact of the change in FX of $5 million. This increase was largely offset by the purchase or return of leased freight cars and intermodal equipment reducing rental expenses by $8 million.

Depreciation and Amortization

Depreciation and amortization expense represents the charge associated with the use of track and roadway, buildings, rolling stock, information systems and other depreciable assets. Depreciation and amortization expense was $161 million in the second quarter of 2016, an increase of $16 million, or 11%, from $145 million in the same period of 2015. This increase was primarily due to a higher depreciable asset base.

Depreciation and amortization expense was $323 million in the first six months of 2016, an increase of $32 million, or 11%, from $291 million in the same period of 2015. This increase was primarily due to a higher depreciable asset base and the unfavourable impact of the change in FX of $5 million.

Purchased Services and Other

			2016 vs. 2015	
For the three months ended June 30 (in millions)	**2016**	2015[(1)]	% Change	Total change
Support and facilities	**$ 77**	$ 73	5	$ 4
Track and operations	**56**	63	(11)	(7)
Intermodal	**44**	46	(4)	(2)
Equipment	**39**	52	(25)	(13)
Casualty	**14**	11	27	3
Property taxes	**29**	26	12	3
Other	**(16)**	6	(367)	(22)
Land sales	**(2)**	(1)	100	(1)
Total Purchased services and other	**$ 241**	$ 276	(13)	$ (35)

(1) Certain comparative figures have been reclassified within Purchased services and other to conform with 2016 presentation: previously Property taxes were included in Support and facilities, Track and operations and Other.

Purchased services and other expense encompasses a wide range of third-party costs, including expenses for joint facilities, personal injuries and damage, environmental remediation, property and other taxes, contractor and consulting fees, insurance, and gains on land sales. Purchased services and other expense was $241 million in the second quarter of 2016, a decrease of $35 million, or 13% from $276 million in the same period of 2015. This decrease was primarily due to:

- a $17 million gain on sale of surplus freight cars, reported in Other;
- lower third-party locomotive overhauls and maintenance costs, reported in Equipment;
- lower contractor services cost, reported in Track and operations and Support and facilities; and
- lower crew travel and accommodations costs, reported in Track and operations.

This decrease was partially offset by:

- the unfavourable impact of the change in FX of $6 million;
- higher casualty expenses of $3 million as a result of costlier mishaps, reported in Casualty; and
- higher property taxes of $2 million (excluding an unfavourable FX impact of $1 million).

			2016 vs. 2015	
For the six months ended June 30 (in millions)	**2016**	2015[(1)]	% Change	Total change
Support and facilities	**$ 161**	$ 149	8	$ 12
Track and operations	**112**	125	(10)	(13)
Intermodal	**88**	93	(5)	(5)
Equipment	**83**	103	(19)	(20)
Casualty	**34**	44	(23)	(10)
Property taxes	**59**	53	11	6
Other	**(20)**	11	(282)	(31)
Land sales	**(55)**	(62)	(11)	7
Total Purchased services and other	**$ 462**	$ 516	(10)	$ (54)

(1) Certain comparative figures have been reclassified within Purchased services and other to conform with 2016 presentation: previously Property taxes were included in Support and facilities, Track and operations and Other.

Purchased services and other expense was $462 million in the first six months of 2016, a decrease of $54 million, or 10% from $516 million in the same period of 2015. This decrease was primarily due to:

- a $17 million gain on sale of surplus freight cars, reported in Other;
- lower third-party freight car and locomotive maintenance costs, reported in Equipment;
- lower contractor services cost, reported in Track and operations and Support and facilities;
- lower crew travel and accommodations costs, reported in Track and operations;
- lower casualty expenses of $12 million (excluding an unfavourable FX impact of $2 million) as a result of lower personal injuries and lower incident costs, reported in Casualty; and
- lower intermodal expenses related to pickup and delivery service, reported in Intermodal.

This decrease was partially offset by:

- the unfavourable impact of the change in FX of $21 million;
- lower land sales of $7 million; and
- higher property taxes of $4 million (excluding an unfavourable FX impact of $2 million).

As part of optimizing its assets, the Company may identify and dispose of property used or formerly used in operating activities. In compliance with U.S. GAAP, the Company includes as part of operating expenses the gains and losses that arise on disposal of such long-lived assets. The following disposals have impacted Purchased services and other during the current and comparative periods:

- In the second quarter of 2016, the Company disposed of 1,000 surplus freight cars that had reached or were nearing the end of their useful life, in a non-monetary exchange for new freight cars. The Company recognized a gain on sale of $17 million from the transaction and the sale did not impact cash from investing activities.
- In the first quarter of 2016, the Company completed the sale of CP's Arbutus Corridor to the City of Vancouver for gross proceeds of $55 million and a gain on sale of $50 million. The agreement allows the Company to share in future proceeds on the eventual development and/or sale of certain parcels of the Arbutus Corridor.
- In the first quarter of 2015, the Company recorded a gain of $31 million following the sale of a building after resolution of legal proceedings, and the Company sold various sections of land in eastern Canada for transit purposes, recognizing gains totalling $60 million.

Other Income Statement Items

Other Income and Charges

Other income and charges consists of gains and losses from the change in FX on long-term debt and working capital, various costs related to financing activities, shareholder costs, equity income and other non-operating expenditures. Other income and charges was a gain of $9 million in the second quarter of 2016, compared to a gain of $5 million in the same period of 2015, a change of $4 million. This change was primarily due to a greater favourable impact of FX translation of $18 million on U.S. dollar-denominated debt during the second quarter of 2016 compared to $10 million in the same period of 2015, discussed further in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Other income and charges was a gain of $190 million in the first six months of 2016, compared to an expense of $68 million in the same period of 2015, a change of $258 million. This change was primarily due to a favourable impact of FX translation of $199 million on U.S. dollar-denominated debt in the first six months of 2016, compared to an unfavourable FX impact of $54 million in the same period of 2015.

Net Interest Expense

Net interest expense includes interest on long-term debt and capital leases. Net interest expense was $115 million in the second quarter of 2016, an increase of $31 million, or 37%, from $84 million in the same period of 2015. This increase was primarily due to an additional $34 million of interest on new debt issued after the second quarter in 2015 and the unfavourable impact of the change in FX of $3 million. This increase was partially offset by interest savings due to principal payments and higher capitalized interest.

Net interest expense was $239 million in the first six months of 2016, an increase of $70 million, or 41%, from $169 million in the same period of 2015. This increase was primarily due to an additional $67 million of interest on new debt issued after the second quarter in 2015 and the unfavourable impact of the change in FX of $10 million. This increase was also partially offset by interest savings due to principal payments and higher capitalized interest.

Income Tax Expense

Income tax expense was $117 million in the second quarter of 2016, a decrease of $60 million, or 34%, from $177 million in the same period of 2015. This decrease was due to lower taxable earnings along with a lower effective tax rate in 2016.

Income tax expense was $287 million in the first six months of 2016, a decrease of $24 million, or 8%, from $311 million in the same period of 2015. This decrease was also due to lower taxable earnings along with a lower effective tax rate in 2016.

The estimated annualized effective tax rate for the second quarter of 2016 excluding discrete items (FX translation of on U.S. dollar denominated debt) was 26.93%, compared to 27.50% during the same period of 2015. For the first six months of 2016, the estimated annualized effective tax rate was 27.25%, compared to 27.50% during the same period of 2015.

The effective tax rate in the second quarter of 2016, including discrete items was 26.40%, compared with 31.30% in the same period of 2015. The higher effective tax rate in the prior period was due to legislation enacted to increase the Alberta provincial corporate income tax rate, during the second quarter of 2015. As a result of this change, the Company recorded an income tax expense of $23 million in the second quarter of 2015 related to the revaluation of its deferred income tax balances as at January 1, 2015.

The effective tax rate in the first six months of 2016, including discrete items was 24.86%, compared with 30.51% in the same period of 2015. The lower effective tax rate in the current period was due to a tax expense related to FX translation gains on U.S. dollar-denominated debt in the first six months of 2016. This compares to the higher effective tax rate in the first six months of 2015 due to the Alberta provincial corporate income tax rate increase, discussed above, and a tax recovery related to FX translation losses on U.S dollar-denominated debt. The tax expense in the first six months of 2016 and the tax recovery in the first six months of 2015 related to the U.S. dollar-denominated debt were assessed at significantly lower rates than the estimated annualized effective tax rates of 27.25% and 27.50%, respectively.

The Company expects an annualized effective tax rate in 2016 of approximately 27.25%. The Company’s 2016 outlook for its normalized income tax rate is based on certain assumptions about events and developments that may or may not materialize or that may be offset entirely or partially by other events and developments, discussed further in Item 1A. Risk Factors of CP's 2015 Annual Report on Form 10-K.

Liquidity and Capital Resources

The Company believes adequate amounts of Cash and cash equivalents are available in the normal course of business to provide for ongoing operations, including the obligations identified in the tables in Contractual Commitments of this Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations. The Company is not aware of any trends or expected fluctuations in the Company's liquidity that would create any deficiencies. The Company's primary sources of liquidity include its Cash and cash equivalents, its bilateral letters of credit and its revolving credit facility.

As at June 30, 2016, the Company had $92 million of Cash and cash equivalents, U.S. $1.9 billion available under its revolving credit facility and up to $229 million available under its letters of credit facility (December 31, 2015 - $650 million of Cash and cash equivalents, U.S. $2.0 billion available under revolving credit facilities and up to $225 million under letters of credit facility).

As at June 30, 2016, the Company's U.S. $2.0 billion revolving credit facility, which includes a U.S. $1.0 billion five-year portion and U.S. $1.0 billion one-year plus one-year term-out portion, was undrawn. On June 28, 2016, the maturity date on the U.S. $1.0 billion one-year plus one-year term-out portion was extended to June 28, 2018, and the maturity date on the U.S. $1.0 billion five-year portion was extended to June 28, 2021.The Company did not draw from its revolving credit facility during the three months ended June 30, 2016. This facility was also undrawn as at December 31, 2015. The revolving credit facility agreement requires the Company not to exceed a maximum debt to earnings before interest, tax, depreciation, and amortization ratio. As at June 30, 2016, the Company was in compliance with the threshold stipulated in this financial covenant.

The Company has a commercial paper program which enables it to issue commercial paper up to a maximum aggregate principal amount of U.S. $1.0 billion in the form of unsecured promissory notes. The commercial paper is backed by the U.S. $1.0 billion one-year plus one-year term-out portion of the revolving credit facility. At June 30, 2016, total commercial paper borrowings were U.S. $135 million (December 31, 2015 - $nil), decreasing the amount available under the revolving credit facility to U.S. $1.9 billion at June 30, 2016. As at June 30, 2016, the Company does not intend to refinance outstanding commercial paper borrowings on a long-term basis.

As at June 30, 2016, under its bilateral letters of credit facility, the Company had letters of credit drawn of $371 million from a total available amount of $600 million. This compares to letters of credit drawn of $375 million from a total available amount of $600 million as at December 31, 2015. Under the bilateral letters of credit facility, the Company has the option to post collateral in the form of Cash or cash equivalents, equal at least to the face value of the letters of credit issued. Collateral provided may include highly liquid investments purchased three months or less from maturity and is stated at cost, which approximates market value. As at June 30, 2016, the Company had posted $nil in collateral on the bilateral letters of credit facility (December 31, 2015 - $nil). The Company can largely withdraw this collateral during any month.

The following discussion of operating, investing and financing activities describes the Company’s indicators of liquidity and capital resources and financial performance.

Operating Activities

Cash provided by operating activities was $512 million in the second quarter of 2016 compared to $585 million in the same period of 2015, a decrease of $73 million. The decrease in Cash provided by operating activities is primarily due to lower cash generating income in the second quarter of 2016 compared to the same period of 2015.

Cash provided by operating activities was $730 million in the first six months of 2016 compared to $1,140 million in the same period of 2015, a decrease of $410 million. The decrease in Cash provided by operating activities is primarily due to lower cash generating income, and an unfavourable change in working capital primarily as a result of higher income taxes paid and an increase in interest payments resulting from debt issued in 2015.

Investing Activities

Cash used in investing activities was $321 million in the second quarter of 2016, a decrease of $33 million from $354 million in the same period of 2015. For the first six months of 2016, cash used in investing activities was $539 million, a decrease of $6 million from $545 million in the same period of 2015. The decrease is primarily due to lower additions to properties during the second quarter and first six months of 2016.

Financing Activities

Cash used in financing activities was $669 million in the second quarter of 2016, an increase of $440 million from $229 million in the same period of 2015. The increase in cash used in financing activities is primarily due to higher purchases of CP Common Shares and lower net issuances of commercial paper compared to the same period of 2015. For the first six months of 2016, cash used in financing activities was $731 million, an increase of $90 million from $641 million in the same period of 2015. The increase in cash used in financing activities is primarily due to issuance of long-term debt in the first six months of 2015. This was partially offset by net issuance of commercial paper during the first six months of 2016 versus net repayment of commercial paper in the same period of 2015, and lower purchases of CP Common Shares.

Interest Coverage Ratio

For the twelve months ended June 30, 2016, the Company’s interest coverage ratio was 5.5, compared with 8.0 for the twelve months ended June 30, 2015. This decrease was primarily due to an increase in Net interest expense of $152 million based on the twelve month period ended June 30, 2016, compared to the same period of 2015, as well as a year over year decrease in Earnings before interest and taxes ("EBIT").

Excluding significant items from EBIT, Adjusted interest coverage ratio was 5.6 for the twelve months ended June 30, 2016, compared with 8.2 for the twelve months ended June 30, 2015. This decrease was primarily due to an increase in Net interest expense, as well as a year over year decrease in adjusted EBIT. Interest coverage ratio, Adjusted interest coverage ratio, EBIT, Adjusted EBIT, and significant items are defined and reconciled in Non-GAAP Measures of this Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations.

Credit Measures

Credit ratings provide information relating to the Company’s financing costs, liquidity and operations, which impacts the Company’s ability to obtain short-term and long-term financing and/or the cost of such financing.

A mid-investment grade credit rating is an important measure in assessing the Company's ability to maintain access to public financing and to minimize the cost of capital. It also affects the ability of the Company to engage in certain collateralized business activities on a cost-effective basis.

Credit ratings and outlooks are based on the rating agencies' methodologies and can change from time to time to reflect their views of CP. Their views are affected by numerous factors including, but not limited to, the Company's financial position and liquidity along with external factors beyond the Company's control.

As at June 30, 2016, CP's credit ratings from Standard & Poor's Rating Services ("Standard & Poor's"), Moody's Investor Service ("Moody's"), and Dominion Bond Rating Service Limited ("DBRS") remain unchanged from December 31, 2015. During the second quarter of 2016, Moody's changed the outlook on CP's Senior unsecured debt to negative from stable, and DBRS changed the outlook on CP's Unsecured debentures and Medium-term notes to negative from stable. Standard & Poor's affirmed a stable rating on CP's Long-term corporate credit, Senior secured debt and Senior unsecured debt.

The Company's goal is to maintain a degree of continuity and predictability for investors by meeting a minimum threshold. The Adjusted net debt to Adjusted earnings before interest, tax, depreciation and amortization ("EBITDA") ratio for the twelve months ended June 30, 2016 and June 30, 2015 was 2.9 and 2.3, respectively. This increase was primarily due to additional debt issued during the 2015 fiscal year, partially offset by the improved Adjusted income for the twelve months ended June 30, 2016. Adjusted net debt to Adjusted EBITDA ratio and Adjusted income are defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Free Cash

CP generated positive Free cash of $137 million in the second quarter of 2016, a decrease of $36 million from positive Free cash of $173 million in the same period of 2015. For the first six months of 2016, CP generated positive Free cash of $66 million, a decrease of $419 million from positive Free cash of $485 million in the same period of 2015. The decrease was primarily due to a decrease in cash provided by operating activities. Free cash is defined and reconciled in Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Free cash is affected by seasonal fluctuations and by other factors including the size of the Company's additions to properties. Capital additions were $330 million in the second quarter of 2016, $25 million lower than in the same period of 2015. In the first six months of 2016, capital additions were $608 million, $10 million lower than in the same period of 2015.

Share Capital

At July 18, 2016, the latest practicable date, there were 147,771,618 Common Shares and no preferred shares issued and outstanding, which consists of 15,113 holders of record of the Company's Common Shares. In addition, CP has a Management Stock Option Incentive Plan ("MSOIP"), under which key officers and employees are granted options to purchase CP shares. Each option granted can be exercised for one Common Share. At July 18, 2016, 2.7 million options were outstanding under the Company's MSOIP and stand-alone option agreements entered into with Mr. E. Hunter Harrison and Mr. Keith E. Creel. There are 1.5 million options available to be issued by the Company's MSOIP in the future.

CP has a Director's Stock Option Plan ("DSOP"), under which directors are granted options to purchase CP shares. There are no outstanding options under the DSOP, which has 0.3 million options available to be issued in the future.

An aggregate of 178,618 Common Shares of the Company beneficially owned or controlled by Mr. E. Hunter Harrison have been pledged as security for his personal line of credit. 153,100 of those Common Shares were pledged on December 30, 2014 and 25,518 of those Common Shares were pledged on June 3, 2016. Effective July 18, 2016, the Board of Directors of the Company approved an anti-pledging policy, which prohibits transactions after the effective date of policy that result in the holding of Common Shares or securities exercisable or convertible into Common Shares, in a margin account, or otherwise pledging such securities as collateral for a loan, subject only to Board approved exceptions where the person wishing to pledge indicates his or her financial capacity to repay the loan without resort to the pledged securities.

Non-GAAP Measures

The Company presents non-GAAP measures and cash flow information to provide a basis for evaluating underlying earnings and liquidity trends in the Company's business that can be compared with the results of operations in prior periods. In addition, these non-GAAP measures facilitate a multi-period assessment of long-term profitability allowing management and other external users of the Company's consolidated financial information to compare profitability on a long-term basis, including assessing future profitability, with that of the Company's peers.

These non-GAAP measures have no standardized meaning and are not defined by GAAP and, therefore, may not be comparable to similar measures presented by other companies. The presentation of these non-GAAP measures is not intended to be considered in isolation from, as a substitute for, or as superior to, the financial information presented in accordance with GAAP.

Adjusted Performance Measures

The Company uses Adjusted income and Adjusted diluted earnings per share to evaluate the Company's operating performance and for planning and forecasting future business operations and future profitability. These non-GAAP measures are presented in Financial Highlights and discussed further in other sections of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations. These non-GAAP measures provide meaningful supplemental information regarding operating results because they exclude certain significant items that are not considered indicative of future financial trends either by nature or amount. As a result, these items are excluded for management assessment of operational performance, allocation of resources and preparation of annual budgets. These significant items may include, but are not limited to, restructuring and asset impairment charges, individually significant gains and losses from sales of assets and certain items outside the control of management. These items may not be non-recurring. However, excluding these significant items from GAAP results allows for a consistent understanding of the Company's consolidated financial performance when performing a multi-period assessment including assessing the likelihood of future results. Accordingly, these non-GAAP financial measures may provide insight to investors and other external users of the Company's consolidated financial information.

In 2016, there was one significant item included in Net income:

- during the six months ended June 30, 2016, a net non-cash gain of $199 million ($172 million after deferred tax) due to FX translation of the Company's U.S. dollar-denominated debt as follows:
  - in the second quarter, an $18 million gain ($16 million after deferred tax); and
  - in the first quarter, a $181 million gain ($156 million after deferred tax).

In 2015, there were four significant items included in Net income:

- in the third quarter, a $68 million gain ($42 million after current tax) related to the sale of D&H South;
- in the third quarter, a $47 million charge ($35 million after deferred tax) related to the early redemption premium on notes;
- in the second quarter, a deferred income tax expense of $23 million as a result of the change in the Alberta provincial corporate income tax rate; and
- during the course of the year, a net non-cash loss of $297 million ($257 million after deferred tax) due to FX translation of the Company's U.S. dollar-denominated debt as follows:
  - in the fourth quarter, a $115 million loss ($100 million after deferred tax);
  - in the third quarter, a $128 million loss ($111 million after deferred tax);
  - in the second quarter, a $10 million gain ($9 million after deferred tax); and
  - in the first quarter, a $64 million loss ($55 million after deferred tax).

In 2014, there was one significant item included in Net income:

- in the fourth quarter, a $12 million net non-cash loss ($9 million after deferred tax) due to FX translation on the Company's U.S. dollar-denominated debt.

Reconciliation of Non-GAAP Measures to GAAP Measures

The following tables reconcile non-GAAP measures presented in Financial Highlights, and discussed further in other sections of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, to the most directly comparable measures presented in accordance with GAAP for the three and six months ended June 30, 2016 and 2015:

Adjusted income is calculated as Net income reported on a GAAP basis less significant items.

Net income	**For the three months ended June 30**		**For the six months ended June 30**	
(in millions)	**2016**	2015	**2016**	2015
Adjusted income	**$ 312**	$ 404	**$ 696**	$ 779
Add significant items:				
Impact of FX translation on U.S. dollar-denominated debt	**16**	9	**172**	(46)
Income tax rate change	**—**	(23)	**—**	(23)
Net income as reported	**$ 328**	$ 390	**$ 868**	$ 710

Adjusted diluted earnings per share is calculated using Adjusted income, as defined above, divided by the weighted-average diluted shares outstanding during the period as determined in accordance with GAAP.

Diluted earnings per share	**For the three months ended June 30**		**For the six months ended June 30**	
	2016	2015	**2016**	2015
Adjusted diluted earnings per share	**$ 2.05**	$ 2.45	**$ 4.55**	$ 4.70
Add significant items:				
Impact of FX translation on U.S. dollar-denominated debt	**0.10**	0.05	**1.12**	(0.28)
Income tax rate change	**—**	(0.14)	**—**	(0.14)
Diluted earnings per share as reported	**$ 2.15**	$ 2.36	**$ 5.67**	$ 4.28

ROIC and Adjusted ROIC

ROIC is calculated as Operating income less Other income and charges, tax affected at the Company's annualized effective tax rate, on a rolling twelve-month basis, divided by the sum of Total shareholders' equity, Long-term debt, Long-term debt maturing within one year and Short-term borrowing, as presented in the Company's Consolidated Financial Statements, averaged between the beginning and ending balance over a rolling twelve-month period. Adjusted ROIC excludes significant items reported in Operating income and Other income and charges in the Company's Consolidated Financial Statements, as these significant items are not considered indicative of future financial trends either by nature or amount. ROIC and Adjusted ROIC are all-encompassing performance measures that measure how productively the Company uses its long-term capital investments, representing critical indicators of good operating and investment decisions made by management and are important performance criteria in determining certain elements of the Company's long-term incentive plan. ROIC and Adjusted ROIC are presented in Financial Highlights and discussed further in Results of Operations of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Calculation of ROIC and Adjusted ROIC

(in millions, except for percentages)	**2016**	2015
Operating income for the twelve months ended June 30	**$ 2,634**	$ 2,587
Less:		
Other income and charges	**77**	84
Tax[(1)]	**709**	721
	$ 1,848	$ 1,782
Average for the twelve months of total shareholders' equity, long-term debt, long-term debt maturing within one year and short-term borrowing	**12,612**	11,889
ROIC	**14.7%**	15.0%

(1) Tax was calculated at the annualized effective tax rate of 27.73% for 2016 and 28.79% for 2015 for each of the above items for the periods presented.

(in millions, except for percentages)	**2016**	2015
Operating income for the twelve months ended June 30	**$ 2,634**	$ 2,587
Less significant items:		
Gain on sale of D&H South	**68**	—
Adjusted operating income for the twelve months ended June 30	**2,566**	2,587
Less:		
Other income and charges	**77**	84
Add significant items:		
Impact of FX translation on U.S. dollar-denominated debt	**44**	66
Early redemption premium on notes	**47**	—
Less: tax[(1)]	**705**	708
	$ 1,875	$ 1,861
Average for the twelve months of total shareholders' equity, long-term debt, long-term debt maturing within one year and short-term borrowing	**12,612**	11,889
Adjusted ROIC	**14.9%**	15.7%

(1) Tax was calculated at the adjusted annualized effective tax rate of 27.31% for 2016 and 27.57% for 2015 for each of the above items for the periods presented.

Free Cash

Free cash is calculated as Cash provided by operating activities, less Cash used in investing activities and Dividends paid, adjusted for changes in cash and cash equivalents balances resulting from FX fluctuations. Free cash is a measure that management considers to be an indicator of liquidity. Free cash is useful to investors and other external users of the consolidated financial information as it assists with the evaluation of the Company's ability to generate cash from its operations without incurring additional external financing. Positive Free cash indicates the amount of cash available for reinvestment in the business, or cash that can be returned to investors through increased dividends, stock repurchase programs, debt retirements or a combination of these. Conversely, negative Free cash indicates the amount of cash that must be raised from investors through new debt or equity issues, reduction in available cash balances or a combination of these. Free cash should be considered in addition to, rather than as a substitute for, Cash provided by operating activities. Free cash is presented in Financial Highlights and discussed further in Liquidity and Capital Resources of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Reconciliation of Cash Provided by Operating Activities to Free Cash

	For the three months ended June 30		For the six months ended June 30	
(in millions)	**2016**	2015	**2016**	2015
Cash provided by operating activities	**$ 512**	$ 585	**$ 730**	$ 1,140
Cash used in investing activities	**(321)**	(354)	**(539)**	(545)
Dividends paid	**(53)**	(57)	**(107)**	(115)
Effect of foreign currency fluctuations on U.S. dollar-denominated cash and cash equivalents	**(1)**	(1)	**(18)**	5
Free cash	**$ 137**	$ 173	**$ 66**	$ 485

Interest Coverage Ratio

Interest coverage ratio is measured, on a rolling twelve-month basis, as EBIT divided by Net interest expense. Interest coverage ratio is an indicator of liquidity used in assessing the Company's debt servicing capabilities. This ratio provides useful information on how the Company's debt servicing capabilities have changed, period over period and in comparison to the Company's peers. Additionally, investors, analysts, and lenders may use this measure to assess the Company's debt servicing capabilities. Interest coverage ratio is discussed further in Liquidity and Capital Resources of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Adjusted interest coverage ratio is calculated as Adjusted EBIT divided by Net interest expense. By excluding significant items which affect EBIT, Adjusted interest coverage ratio assists management in comparing the Company's performance over various reporting periods on a consistent basis. Adjusted interest coverage ratio is discussed further in Liquidity and Capital Resources of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Calculation of Interest Coverage Ratio and Adjusted Interest Coverage Ratio

	For the twelve months ended June 30	
(in millions, except for ratios)	**2016**	2015
EBIT	**$ 2,557**	$ 2,503
Adjusted EBIT	**2,580**	2,569
Net interest expense	**464**	312
Interest coverage ratio	**5.5**	8.0
Adjusted interest coverage ratio	**5.6**	8.2

Reconciliation of Adjusted earnings before interest, tax, depreciation and amortization and Earnings before interest and tax

Adjusted EBITDA is calculated as Adjusted EBIT plus Depreciation and amortization, adjusted for net periodic pension and other benefit cost and operating lease expense. EBIT is calculated as Operating income, less Other income and charges. Adjusted EBIT excludes significant items reported in Operating income and Other income and charges.

(in millions)	2016	2015
Adjusted EBITDA for the twelve months ended June 30	**$ 3,203**	$ 3,159
Add:		
Adjustment for net periodic pension and other benefit cost	**115**	112
Operating lease expense	**(111)**	(137)
Depreciation and amortization	**(627)**	(565)
Adjusted EBIT for the twelve months ended June 30	**2,580**	2,569
Add Significant items:		
Gain on sale of D&H South	**68**	—
Impact of FX translation on U.S. dollar-denominated debt	**(44)**	(66)
Early redemption premium on notes	**(47)**	—
EBIT for the twelve months ended June 30	**2,557**	2,503
Less:		
Net interest expense	**464**	312
Income tax expense	**583**	630
Net income as reported	**$ 1,510**	$ 1,561

Adjusted Net Debt to Adjusted EBITDA Ratio

Adjusted net debt is defined as Long-term debt, Long-term debt maturing within one year and Short-term borrowing as reported on the Company's Consolidated Balance Sheets adjusted for pension plans deficit, the net present value of operating leases, which is discounted by the Company's effective interest rate for each of the periods presented, and Cash and cash equivalents. Adjusted net debt to adjusted EBITDA ratio is calculated as Adjusted net debt divided by Adjusted EBITDA.

The Adjusted net debt to adjusted EBITDA ratio is one of the key metrics used by credit rating agencies in assessing the Company's financial capacities and constraints and determining the credit rating of the Company. By excluding the impact of certain items that are not considered by management in developing a minimum threshold, Adjusted net debt to Adjusted EBITDA ratio provides a metric that management uses to evaluate the Company's financial discipline with respect to capital markets credit sensitivities from management's perspective and communicates it publicly with investors, analysts and credit rating agencies. Adjusted net debt to Adjusted EBITDA ratio is discussed further in Liquidity and Capital Resources of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Calculation of Adjusted Net Debt to Adjusted EBITDA Ratio

(in millions, except for ratios)	2016	2015
Adjusted net debt as at June 30	**$ 9,133**	$ 7,216
Adjusted EBITDA for the twelve months ended June 30	**3,203**	3,159
Adjusted net debt to Adjusted EBITDA ratio	**2.9**	2.3

Reconciliation of Adjusted Net Debt to Long-term Debt

(in millions)	2016	2015
Adjusted net debt as at June 30	**$ 9,133**	$ 7,216
Add:		
Pension plans deficit	**(290)**	(291)
Net present value of operating leases[1]	**(354)**	(409)
Cash and cash equivalents	**92**	185
Long-term debt including long term debt maturing within one year as at June 30	**$ 8,581**	$ 6,701

[1] Operating leases were discounted at the Company's effective interest rate for each of the periods presented.

Off-Balance Sheet Arrangements

Guarantees

At June 30, 2016, the Company had residual value guarantees on operating lease commitments of $26 million, compared to $28 million at December 31, 2015. The maximum amount that could be payable under these and all of the Company's other guarantees cannot be reasonably estimated due to the nature of certain guarantees. All or a portion of amounts paid under certain guarantees could be recoverable from other parties or through insurance. As at June 30, 2016, the fair value of these guarantees recognized as a liability was $6 million, compared to $4 million at December 31, 2015.

Contractual Commitments

The accompanying table indicates the Company's obligations and commitments to make future payments for contracts, such as debt, capital lease and commercial arrangements.

Contractual Commitments

At June 30, 2016

Payments due by period (in millions)		Total		2016		2017 & 2018		2019 & 2020		2021 & beyond
Contractual commitments										
Interest on long-term debt and capital lease	**$**	**12,317**	$	238	$	926	$	800	$	10,353
Long-term debt		**8,519**		184		780		540		7,015
Capital leases		**162**		2		9		10		141
Operating lease[1]		**469**		46		148		91		184
Supplier purchase		**1,309**		121		346		167		675
Other long-term liabilities[2]		**572**		54		116		110		292
Total contractual commitments	**$**	**23,348**	$	645	$	2,325	$	1,718	$	18,660

[1] Residual value guarantees on certain leased equipment with a maximum exposure of $26 million are not included in the minimum payments shown above, as management believes that CP will not be required to make payments under these residual guarantees.

[2] Includes expected cash payments for restructuring, environmental remediation, asset retirement obligations, post-retirement benefits, workers' compensation benefits, long-term disability benefits, pension benefit payments for the Company's non-registered supplemental pension plan and certain other long-term liabilities. Projected payments for post-retirement benefits, workers' compensation benefits and long-term disability benefits include the anticipated payments for years 2016 to 2025. Pension contributions for the Company's registered pension plans are not included due to the volatility in calculating them. Pension payments are discussed further in Critical Accounting Estimates of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

Certain Other Financial Commitments

In addition to the financial commitments mentioned previously in Off-Balance Sheet Arrangements and Contractual Commitments of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations, the Company is party to certain other financial commitments set forth in the table and discussed below.

At June 30, 2016

Amount of commitments per period (in millions)		Total		2016		2017 & 2018		2019 & 2020		2021 & beyond
Commitments										
Letters of credit	**$**	**371**	$	371	$	—	$	—	$	—
Capital commitments		**349**		246		74		15		14
Total commitments	**$**	**720**	$	617	$	74	$	15	$	14

Letters of Credit

Letters of credit are obtained mainly to provide security to third parties under the terms of various agreements, including workers' compensation and supplemental pension plan. CP is liable for these contractual amounts in the case of non-performance under these agreements. Letters of credit are accommodated through a revolving credit facility and the Company's bilateral letters of credit facility.

Capital Commitments

The Company remains committed to maintaining the current high level of plant quality and renewing the franchise. As part of this commitment, CP has entered into contracts with suppliers to make various capital purchases related to track programs. Payments for these commitments are due in 2016 through 2032. These expenditures are expected to be financed by cash generated from operations or by issuing new debt.

Critical Accounting Estimates

To prepare consolidated financial statements that conform with GAAP, the Company is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reported periods. Using the most current information available, the Company reviews estimates on an ongoing basis, including those related to environmental liabilities, pensions and other benefits, property, plant and equipment, deferred income taxes, legal and personal injury liabilities and goodwill.

The development, selection and disclosure of these estimates, and this MD&A, have been reviewed by the Board of Directors' Audit Committee, which is composed entirely of independent directors.

Pensions and Other Benefits

Pension Liabilities and Pension Assets

The Company included pension benefit liabilities of $280 million in Pension and other benefit liabilities and $10 million in Accounts payable and accrued liabilities on the Company's Interim Consolidated Balance Sheets at June 30, 2016. The Company also included post-retirement benefits accruals of $386 million in Pension and other benefit liabilities and $21 million in Accounts payable and accrued liabilities on the Company's Interim Consolidated Balance Sheets at June 30, 2016.

The Company included pension benefit assets of $1,565 million in Pension assets on the Company's Interim Consolidated Balance Sheets at June 30, 2016.

Pension Plan Contributions

The Company made contributions of $14 million to the defined benefit pension plans in the second quarter of 2016, compared with $20 million in the same period of 2015. In the first six months of 2016, the Company made contributions of $34 million to the defined benefit pension plans, compared with $41 million in the same period of 2015. The Company's main Canadian defined benefit pension plan accounts for 95% of CP's pension obligation and can produce significant volatility in pension funding requirements, given the pension fund's size, the many factors that drive the pension plan's funded status, and Canadian statutory pension funding requirements. The Company made voluntary prepayments of $600 million in 2011, $650 million in 2010 and $500 million in 2009 to the Company's main Canadian defined benefit pension plan. CP has applied $1,276 million of these voluntary prepayments to reduce its pension funding requirements in 2012–2015, leaving $474 million of the voluntary prepayments still available at December 31, 2015 to reduce CP's pension funding requirements in 2016 and future years. CP continues to have significant flexibility with respect to the rate at which the remaining voluntary prepayments are applied to reduce future years' pension contribution requirements, which allows CP to manage the volatility of future pension funding requirements. At this time, CP estimates it will apply $5 million of the remaining voluntary prepayments against its 2016 pension funding requirements.

CP estimates its aggregate pension contributions, including its defined benefit and defined contribution plan, to be in the range of $50 million to $60 million in 2016, and in the range of $50 million to $100 million per year from 2017 to 2019. These estimates reflect the Company's current intentions with respect to the rate at which CP will apply the remaining voluntary prepayments against contribution requirements in the next few years.

Future pension contributions will be highly dependent on the Company's actual experience with such variables as investment returns, interest rate fluctuations and demographic changes, on the rate at which previous years' voluntary prepayments are applied against pension contribution requirements, and on any changes in the regulatory environment. CP will continue to make contributions to the pension plans that, at a minimum, meet pension legislative requirements.

Deferred Income Taxes

A deferred income tax expense of $90 million was included in Income tax expense for the second quarter of 2016 compared to $74 million for the same period of 2015. For the first six months of 2016, deferred income tax expense of $183 million was included in Income tax expense compared to $106 million the same period of 2015.

The increase in deferred income tax expense in the second quarter of 2016 was primarily due to a change in the estimated timing of recognition of certain temporary differences that correspondingly decreased current tax expense, partially offset by lower pretax earnings compared to the same period of 2015. The increase in deferred income tax expense for the first six months of 2016 was attributable to the increase in the second quarter, as well as unrealized FX translation gains on U.S. dollar-denominated debt, which does not give rise to current tax expense.

At June 30, 2016, deferred income tax liabilities of $3,512 million were recorded as a long-term liability and are composed largely of temporary differences related to accounting for properties.

Legal and Personal Injury Liabilities

Provisions for incidents, claims and litigation charged to income, which were included in Purchase services and other expense, amounted to $13 million in the second quarter of 2016 compared with $9 million for the same period of 2015. For the first six months of 2016, these provisions amounted to $33 million compared with $35 million for the same period of 2015.

Forward-Looking Information

This MD&A and Quarterly Report on Form 10-Q contains certain forward-looking statements within the meaning of the United States Private Securities Litigation Reform Act of 1995 and other relevant securities legislation. These forward-looking statements include, but are not limited to, statements concerning the Company’s operations, anticipated financial performance, business prospects and strategies, including statements concerning the anticipation that cash flow from operations and various sources of financing will be sufficient to meet debt repayments and obligations in the foreseeable future and concerning anticipated capital programs, statements regarding future payments including income taxes and pension contributions, and capital expenditures. Forward-looking information typically contains statements with words such as “financial expectations”, “key assumptions”, “anticipate”, “believe”, “expect”, “plan”, “will”, “outlook”, “should” or similar words suggesting future outcomes.

Readers are cautioned not to place undue reliance on forward-looking information because it is possible that CP will not achieve predictions, forecasts, projections and other forms of forward-looking information. Current economic conditions render assumptions, although reasonable when made, subject to greater uncertainty. In addition, except as required by law, CP undertakes no obligation to update publicly or otherwise revise any forward-looking information, whether as a result of new information, future events or otherwise.

By its nature, forward-looking information involves numerous assumptions, inherent risks and uncertainties, including but not limited to the following factors: changes in business strategies; general North American and global economic, credit and business conditions; risks in agricultural production such as weather conditions and insect populations; the availability and price of energy commodities; the effects of competition and pricing pressures; industry capacity; shifts in market demand; inflation; changes in laws and regulations, including regulation of rates; changes in taxes and tax rates; potential increases in maintenance and operating costs; uncertainties of investigations, proceedings or other types of claims and litigation; labour disputes; risks and liabilities arising from derailments; transportation of dangerous goods; timing of completion of capital and maintenance projects; currency and interest rate fluctuations; effects of changes in market conditions on the financial position of pension plans and investments; and various events that could disrupt operations, including severe weather, droughts, floods, avalanches and earthquakes as well as security threats and the governmental response to them, and technological changes.

There are more specific factors that could cause actual results to differ materially from those described in the forward-looking statements contained in this MD&A. These more specific factors are identified and discussed in Item 1A. Risk Factors of CP's 2015 Annual Report on Form 10-K. Other risks are detailed from time to time in reports filed by CP with securities regulators in Canada and the United States.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes to market risk during the three and six months ended June 30, 2016 from the information provided in Item 7A. Quantitative and Qualitative Disclosure about Market Risk of CP's 2015 Annual Report on Form 10-K other than foreign exchange risk and share price impact on stock-based compensation discussed below:

Foreign Exchange Risk

Although CP conducts business primarily in Canada, a significant portion of its revenues, expenses, assets and liabilities including debt are denominated in U.S. dollars. The value of the Canadian dollar is affected by a number of domestic and international factors, including, without limitation, economic performance, and Canadian, U.S. and international monetary policies. Consequently, the Company's results are affected by fluctuations in the exchange rate between these currencies. On an annualized basis, a $0.01 weakening (or strengthening) of the Canadian dollar positively (or negatively) impacts Total revenues by approximately $26 million and negatively (or positively) impacts Operating expenses by approximately $13 million. To manage this exposure to fluctuations in exchange rates between Canadian and U.S. dollars, CP may sell or purchase U.S. dollar forwards at fixed rates in future periods. In addition, changes in the exchange rate between the Canadian dollar and other currencies (including the U.S. dollar) make the goods transported by the Company more or less competitive in the world marketplace and may in turn positively or negatively affect revenues.

FX translation on the Company's U.S. dollar-denominated long-term debt is also impacted by this risk. A weakening (or strengthening) of the Canadian dollar negatively (or positively) impacts Other income and charges in the Company's Consolidated Statements of Income. For further information, please refer to Item 8. Financial Statements and Supplementary Data, Note 20 Financial Instruments, in CP's 2015 Annual Report on Form 10-K.

Share Price Impact on Stock-Based Compensation

For every $1.00 change in share price, stock-based compensation expense has a corresponding change of approximately $0.5 million to $0.7 million based on information available at June 30, 2016. This excludes the impact of changes in share price relative to the S&P/TSX 60 index and relative to Class I railways, which may trigger different performance share unit payouts.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As of June 30, 2016, an evaluation was carried out under the supervision of and with the participation of CP's management, including its CEO and CFO, of the effectiveness of the design and operation of the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on that evaluation, the CEO and CFO concluded that these disclosure controls and procedures were effective as of June 30, 2016, to ensure that information required to be disclosed by the Company in reports that it files or submits under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified by the SEC rules and forms and (ii) accumulated and communicated to the Company’s management, including the CEO and CFO, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

During the second quarter of 2016, the Company has not identified any changes in internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.