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

The following Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A") is intended to enhance a reader's understanding of the Company's results of operations and financial condition. The MD&A is provided as a supplement to, and should be read in conjunction with, the Company's Interim Consolidated Financial Statements and the related notes for the three months ended March 31, 2024 in Item 1. Financial Statements, other information in this report, and Item 8. Financial Statements and Supplementary Data of the Company's 2023 Annual Report on Form 10-K. Except where otherwise indicated, all financial information reflected herein is expressed in Canadian dollars.

In this Quarterly Report on Form 10-Q, unless the context indicates otherwise, references to "CPKC", "the Company", "our", or "us" are to Canadian Pacific Kansas City Limited ("CPKC") and its subsidiaries, which includes Kansas City Southern ("KCS") as a consolidated subsidiary on and from April 14, 2023 (the "Control Date"). Prior to April 14, 2023, the Company's 100% interest in KCS was reported as an equity-method investment.

Available Information

The Company makes available on or through its website www.cpkcr.com 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"). Our website also contains charters for our Board of Directors and each of its committees, our corporate governance guidelines and our Code of Business Ethics. SEC filings made by the Company 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's ("CEO") and Chief Financial Officer's certifications regarding the Company's public disclosure required by Section 302 of the Sarbanes-Oxley Act of 2002 as Exhibits to this report.

Executive Summary

First Quarter of 2024 Results

- *Financial performance* - In the first quarter of 2024, the Company reported Diluted earnings per share ("EPS") of $0.83, a decrease of 3% compared to the same period of 2023. Core adjusted combined diluted EPS was $0.93, an increase of 3% compared to the same period of 2023. The Company reported Operating ratio of 67.4%, a 400 basis point increase compared to the same period of 2023. Core adjusted combined operating ratio was 64.0%, a 50 basis point increase compared to the same period of 2023. Core adjusted combined diluted EPS and Core adjusted combined operating ratio are defined and reconciled in the Non-GAAP Measures of this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

  In the first quarter of 2024, net income from KCS was $280 million compared to KCS equity earnings of $204 million in the same period of 2023. The higher overall contribution from KCS was primarily due to a decrease in net interest expense as a result of the completion of the debt exchange in 2023 and lower FX loss. In the first quarter of 2024, KCS contributed $370 million to Operating income, which increased CPKC's operating ratio by 1.4%.

- *Total revenues* - Total revenues increased by 55% in the first quarter of 2024 to $3,520 million, compared to the same period of 2023. The increase was primarily due to the impact of the KCS acquisition and higher freight rates, partially offset by lower fuel prices.

Performance Indicators

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

	For the three months ended March 31		
	2024	2023	% Change
Operations Performance			
Gross ton-miles ("GTMs") (millions)	**95,809**	67,449	42
Train miles (thousands)	**11,995**	7,257	65
Fuel efficiency (U.S. gallons of locomotive fuel consumed / 1,000 GTMs)	**1.065**	0.973	9
Total employees (average)	**19,997**	12,935	55

These key measures are used by management in the planning process to facilitate decisions that continue to drive further productivity improvements in the Company's operations. These key measures reflect how effective the Company's management is at controlling costs and executing the Company's operating plan and strategy. Continued monitoring of these key measures enables the Company to take appropriate actions to deliver superior service and grow its business at low incremental cost.

A **GTM** is defined as the movement of one ton of train weight over one mile. GTMs are calculated by multiplying total train weight by the distance the train moved. Total train weight comprises the weight of the freight cars, their contents, and any inactive locomotives. An increase in GTMs indicates additional workload. The increase in GTMs in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes of U.S. grain, Intermodal, and crude. This increase was partially offset by lower volumes of Canadian grain and Metals, minerals and consumer products.

Train miles are defined as the sum of the distance moved by all trains operated on the network. Train miles provide a measure of the productive utilization of our network. A smaller increase in train miles relative to increases in volumes, as measured by RTMs, and/or workload, as measured by GTMs, indicates improved train productivity. The increase in train miles in the first quarter of 2024 reflects the impact of a 42% increase in workload (GTMs), and a 14% decrease in train weights, which was primarily due to the impact of the KCS acquisition.

Fuel efficiency is defined as U.S. gallons of locomotive fuel consumed per 1,000 GTMs. Fuel consumed includes gallons from freight, yard and commuter service but excludes fuel used in capital projects and other non-freight activities. An improvement in fuel efficiency indicates operational cost savings. The decrease in Fuel efficiency in the first quarter of 2024 was primarily due to the impact of the KCS acquisition as a result of the decrease in train weights.

An **employee** is defined as an individual currently engaged in full-time, part-time, or seasonal employment with the Company. The Company monitors employment and workforce levels in order to efficiently meet service and strategic requirements. The number of employees is a key driver to total compensation and benefits costs. The increase in the average number of total employees in the first quarter of 2024 was primarily due to the acquisition of KCS.

Financial Highlights

The following table presents selected financial data related to the Company's financial results as at, and for the three months ended, March 31, 2024 and the comparative figures in 2023. The financial highlights should be read in conjunction with Item 1. Financial Statements and this Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations.

	For the three months ended March 31	
(in millions, except per share data, percentages and ratios)	**2024**	2023
Financial Performance		
Total revenues	**$ 3,520**	$ 2,266
Operating income	**1,149**	829
Net income attributable to controlling shareholders	**775**	800
Basic EPS	**0.83**	0.86
Diluted EPS	**0.83**	0.86
Core adjusted combined diluted EPS(1)	**0.93**	0.90
Dividends declared per share	**0.19**	0.19
Financial Ratios		
Operating ratio(2)	**67.4%**	63.4%
Core adjusted combined operating ratio(1)	**64.0%**	63.5%

(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 the Non-GAAP Measures section.

(2) Operating ratio is defined as operating expenses divided by revenues.

Results of Operations

Operating Revenues

The Company's revenues are primarily derived from transporting freight. Changes in freight volumes generally contribute to corresponding changes in Freight revenues and certain variable expenses such as fuel, equipment rents, and crew costs. Non-freight revenues are generated from leasing of certain assets, interline switching, and other arrangements including contracts with passenger service operators, subsurface and mineral rights agreements, and logistical services.

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 3,427**	$ 2,217	$ 1,210	55
Non-freight revenues (in millions)	**93**	49	44	90
Total revenues (in millions)	**$ 3,520**	$ 2,266	$ 1,254	55
Carloads (in thousands)	**1,072.6**	679.5	393.1	58
Revenue ton-miles (in millions)	**51,838**	37,549	14,289	38
Freight revenue per carload (in dollars)	**$ 3,195**	$ 3,263	$ (68)	(2)
Freight revenue per revenue ton-mile (in cents)	**6.61**	5.90	0.71	12

Total Revenues
The increase in Freight revenues in the first quarter of 2024 was primarily due to the impact of the KCS acquisition of $1,215 million, higher freight rates, and higher volumes as measured by RTMs, partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue and the unfavourable impact of the change in FX. The increase in Non-freight revenues was primarily due to higher revenue from a fibre optic agreement and the impact of the KCS acquisition of $17 million.

RTMs
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. The increase in RTMs in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes of U.S. grain, Intermodal, and crude, partially offset by lower volumes of Canadian grain and Metals, minerals and consumer products. Carloads have increased more than RTMs due to the impact of the KCS acquisition as KCS has a shorter average length of haul.

Freight Revenue per RTM
Freight revenue per RTM is defined as freight revenue per revenue-producing ton of freight over a distance of one mile. This is an indicator of yield. The increase in freight revenue per RTM in the first quarter of 2024 was primarily due to the impact of the KCS acquisition and higher freight rates, partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue of $68 million and the unfavourable impact of the change in FX of $3 million.

Fuel Cost Adjustment Program
Freight revenues include fuel surcharge revenues associated with the Company's fuel cost adjustment program, which is designed to respond to fluctuations in fuel prices and help reduce exposure to changing fuel prices. The surcharge is applied to shippers through tariffs and by contract, within agreed-upon guidelines. This program includes recoveries of carbon taxes, levies, and obligations under cap-and-trade programs. Freight revenues included fuel surcharge revenues of $412 million in the first quarter of 2024, an increase of $100 million, or 32%, from $312 million in the same period of 2023. This increase was primarily due to the impact of the KCS acquisition and higher volumes, partially offset by lower fuel prices and the unfavourable impact from the timing of recoveries under the Company's fuel cost adjustment program.

Lines of Business

Grain

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 730**	$ 515	$ 215	42
Carloads (in thousands)	**132.3**	104.8	27.5	26
Revenue ton-miles (in millions)	**14,570**	10,014	4,556	45
Freight revenue per carload (in dollars)	**$ 5,518**	$ 4,914	$ 604	12
Freight revenue per revenue ton-mile (in cents)	**5.01**	5.14	(0.13)	(3)

The increase in Grain revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes of U.S. corn to the U.S. Pacific Northwest and Alberta, and higher freight rates. This increase was partially offset by lower volumes of Canadian grain to Vancouver, British Columbia ("B.C.") due to a smaller crop size for the 2023-2024 crop year and decreased freight revenue per RTM. Freight revenue per RTM decreased due to the unfavourable impact of lower fuel prices on fuel surcharge revenue and the unfavourable impact of the change in FX. RTMs increased more than carloads due to moving higher volumes of U.S. corn to the U.S. Pacific Northwest and Alberta, which have longer lengths of haul.

Coal

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 209**	$ 155	$ 54	35
Carloads (in thousands)	**108.2**	72.4	35.8	49
Revenue ton-miles (in millions)	**5,252**	3,925	1,327	34
Freight revenue per carload (in dollars)	**$ 1,932**	$ 2,141	$ (209)	(10)
Freight revenue per revenue ton-mile (in cents)	**3.98**	3.95	0.03	1

The increase in Coal revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, increased freight revenue per RTM, and higher volumes of Canadian coal to Vancouver. This increase was partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue, lower volumes of Canadian coal to Kamloops, B.C. as a result of extreme cold weather in January, and lower volumes of U.S. coal driven by reduced power prices which decreases demand for coal. Freight revenue per RTM increased due to higher freight rates.

Potash

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 137**	$ 132	$ 5	4
Carloads (in thousands)	**37.0**	36.9	0.1	—
Revenue ton-miles (in millions)	**4,110**	4,010	100	2
Freight revenue per carload (in dollars)	**$ 3,703**	$ 3,577	$ 126	4
Freight revenue per revenue ton-mile (in cents)	**3.33**	3.29	0.04	1

The increase in Potash revenue in the first quarter of 2024 was primarily due to higher volumes of domestic potash, higher volumes of export potash to Texas and Thunder Bay, Ontario, and increased freight revenue per RTM. This increase was partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue and lower volumes of export potash to Kamloops, B.C. Freight revenue per RTM increased due to higher freight rates.

Fertilizers and Sulphur

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 104**	$ 96	$ 8	8
Carloads (in thousands)	**17.2**	17.0	0.2	1
Revenue ton-miles (in millions)	**1,366**	1,340	26	2
Freight revenue per carload (in dollars)	**$ 6,047**	$ 5,647	$ 400	7
Freight revenue per revenue ton-mile (in cents)	**7.61**	7.16	0.45	6

The increase in Fertilizers and sulphur revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition and increased freight revenue per RTM. This increase was partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue and lower volumes of sulphur and wet fertilizers. Freight revenue per RTM increased due to higher freight rates.

Forest Products

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 202**	$ 103	$ 99	96
Carloads (in thousands)	**35.9**	17.7	18.2	103
Revenue ton-miles (in millions)	**2,244**	1,378	866	63
Freight revenue per carload (in dollars)	**$ 5,627**	$ 5,819	$ (192)	(3)
Freight revenue per revenue ton-mile (in cents)	**9.00**	7.47	1.53	20

The increase in Forest products revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes of lumber from B.C. and Alberta to the U.S. Midwest, and higher freight rates. This increase was partially offset by lower volumes of wood pulp from Ontario to the U.S. Midwest and the unfavourable impact of lower fuel prices on fuel surcharge revenue.

Energy, Chemicals and Plastics

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 702**	$ 366	$ 336	92
Carloads (in thousands)	**144.5**	75.2	69.3	92
Revenue ton-miles (in millions)	**9,719**	6,207	3,512	57
Freight revenue per carload (in dollars)	**$ 4,858**	$ 4,867	$ (9)	—
Freight revenue per revenue ton-mile (in cents)	**7.22**	5.90	1.32	22

The increase in Energy, chemicals and plastics revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes of fuel oil from Alberta to B.C., higher volumes of DRUbit™ crude to Port Arthur, Texas and conventional crude to Chicago, Illinois, higher volumes of plastics, and higher freight rates. This increase was partially offset by lower volumes of liquefied petroleum gas and diluents, the unfavourable impact of lower fuel prices on fuel surcharge revenue, and the unfavourable impact of the change in FX.

Metals, Minerals and Consumer Products

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 440**	$ 233	$ 207	89
Carloads (in thousands)	**129.7**	61.8	67.9	110
Revenue ton-miles (in millions)	**4,701**	2,911	1,790	61
Freight revenue per carload (in dollars)	**$ 3,392**	$ 3,770	$ (378)	(10)
Freight revenue per revenue ton-mile (in cents)	**9.36**	8.00	1.36	17

The increase in Metals, minerals and consumer products revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition and increased freight revenue per RTM. This increase was partially offset by lower volumes of frac sand to the Bakken and Permian Basin shale formations, lower volumes of steel, and lower volumes of food and consumer products, the unfavourable impact of lower fuel prices on fuel surcharge revenue, and the unfavourable impact of the change in FX. Freight revenue per RTM increased due to higher freight rates.

Automotive

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 265**	$ 125	$ 140	112
Carloads (in thousands)	**55.7**	28.7	27.0	94
Revenue ton-miles (in millions)	**997**	474	523	110
Freight revenue per carload (in dollars)	**$ 4,758**	$ 4,355	$ 403	9
Freight revenue per revenue ton-mile (in cents)	**26.58**	26.37	0.21	1

The increase in Automotive revenue in the first quarter of 2024 was primarily due to the impact of the KCS acquisition, higher volumes from Ontario to the U.S. Midwest and western Canada, from Chicago to various destinations in Canada, and from Vancouver to eastern Canada, and increased freight revenue per RTM. This increase was partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue. Freight revenue per RTM increased due to higher freight rates. RTMs increased more than carloads due to moving higher volumes from Ontario to B.C. and from Vancouver to eastern Canada, which have longer lengths of haul.

Intermodal

For the three months ended March 31	**2024**	2023	Total Change	% Change
Freight revenues (in millions)	**$ 638**	$ 492	$ 146	30
Carloads (in thousands)	**412.1**	265.0	147.1	56
Revenue ton-miles (in millions)	**8,879**	7,290	1,589	22
Freight revenue per carload (in dollars)	**$ 1,548**	$ 1,857	$ (309)	(17)
Freight revenue per revenue ton-mile (in cents)	**7.19**	6.75	0.44	7

The increase in Intermodal revenue in the first quarter of 2024 was primarily due to the impact of KCS acquisition, higher international intermodal volumes to and from the Port of Vancouver, higher domestic intermodal wholesale volumes, and higher freight rates. This increase was partially offset by the unfavourable impact of lower fuel prices on fuel surcharge revenue.

Operating Expenses

For the three months ended March 31 (in millions of Canadian dollars)	**2024**	2023	Total Change	% Change
Compensation and benefits	**$ 690**	$ 438	$ 252	58
Fuel	**458**	326	132	40
Materials	**94**	72	22	31
Equipment rents	**82**	30	52	173
Depreciation and amortization	**467**	225	242	108
Purchased services and other	**580**	346	234	68
Total operating expenses	**$ 2,371**	$ 1,437	$ 934	65

Compensation and Benefits

Compensation and benefits expense includes employee wages, salaries, fringe benefits, and stock-based compensation. The increase in Compensation and benefits expense in the first quarter of 2024 was primarily due to:
- the impact of the KCS acquisition of $212 million;
- the impact of wage and benefit inflation;
- increased stock-based compensation of $20 million primarily driven by the change in share price; and
- higher acquisition-related costs incurred by CPKC, excluding KCS's acquisition-related costs, including stock-based compensation of $4 million.

This increase was partially offset by retroactive payments on ratification of collective bargaining agreements in the prior year and lower training costs.

Fuel

Fuel expense consists mainly of fuel used by locomotives and includes provincial, state, and federal fuel taxes. The increase in Fuel expense in the first quarter of 2024 was primarily due to:
- the impact of the KCS acquisition of $158 million;
- an increase in workload, as measured by GTMs; and
- a decrease in fuel efficiency due to running shorter and lighter trains.

This increase was partially offset by the favourable impact of lower fuel prices of $27 million.

Materials

Materials expense includes the cost of materials used for the maintenance of track, locomotives, freight cars, and buildings, as well as software sustainment. The increase in Materials expense in the first quarter of 2024 was primarily due to the impact of the KCS acquisition of $29 million, partially offset by a decrease in track and freight car maintenance.

Equipment Rents

Equipment rents expense includes the cost associated with using other railways' freight cars, intermodal equipment, and locomotives, net of recoveries received from other railways for the use of the Company's equipment. The increase in Equipment rents expense in the first quarter of 2024 was primarily due to the impact of the KCS acquisition of $32 million and reduced recoveries from other railway's use of the Company's locomotives.

Depreciation and Amortization

Depreciation and amortization expense is the charge associated with the use of track and roadway, rolling stock, buildings, and other depreciable assets, including assets related to the Company's concession with the Mexican government, as well as amortization of finite life intangible assets. The increase in Depreciation and amortization expense in the first quarter of 2024 was primarily due to the impact of the KCS acquisition of $224 million, including additional depreciation of $59 million and amortization of $20 million attributed to fair value adjustments to properties and intangible assets with finite lives recognized upon the acquisition of KCS, and a higher depreciable asset base.

Purchased Services and Other

Purchased services and other expense encompasses a wide range of third-party costs, including expenses for joint facilities, personal injuries and damage claims, environmental remediation, property taxes, contractor and consulting fees, and insurance. The increase in Purchased services and other expense in the first quarter of 2024 was primarily due to:
- the impact of the KCS acquisition of $207 million;
- higher terminal service costs;
- an increase in casualty incidents and higher personal injury costs;
- an increase in bad debt expense;
- the impact of cost inflation; and
- an increase in acquisition-related costs.

The increase was partially offset by a one-time fee of $34 million (U.S. $25 million) received in connection with the Company's agreement to waive a departing executive's non-competition agreement with respect to their employment with Norfolk Southern Corporation.

Other Income Statement Items

Equity Earnings of Kansas City Southern

On April 14, 2023, the Company assumed control of KCS, and subsequently ceased recognizing equity earnings of KCS.

The Company recognized $204 million (U.S. $151 million) of equity earnings of KCS in the three months ended March 31, 2023. This amount was net of amortization of basis differences of $42 million (U.S. $31 million) associated with KCS purchase accounting, and was net of acquisition-related costs (net of tax) incurred by KCS. These basis differences related to depreciable property, plant and equipment, intangible assets with definite lives, and long-term debt, and were amortized over the related assets' remaining useful lives and the remaining terms to maturity of the debt instruments. Acquisition-related costs (net of tax) incurred by KCS in the first quarter of 2023 were $10 million (U.S. $7 million). KCS U.S. dollar historical results were translated at the average FX rate for the first three months ended March 31, 2023 of $1.00 USD= $1.35 CAD.

Other (Income) Expense

Other (income) expense consists of gains and losses from the change in FX on cash and working capital, the impact of foreign currency forwards, financing costs, shareholder costs, equity earnings, and other non-operating expenditures. Other income was $2 million in the first quarter of 2024, a change of $4 million, or 200%, compared to an expense of $2 million in the same period of 2023. This change was primarily due to a decrease in net acquisition-related costs of $3 million driven by the KCS Debt exchange.

Other Components of Net Periodic Benefit Recovery

Other components of net periodic benefit recovery are related to the Company's pension and other post-retirement and post-employment benefit plans. It includes interest cost on benefit obligation, expected return on plan assets, recognized net actuarial loss, and amortization of prior service costs. Other components of net periodic benefit recovery was $88 million in the first quarter of 2024, an increase of $2 million, or 2%, compared to the same period of 2023. The increase was due to a decrease in interest cost on benefit obligation of $3 million and an increase in expected return on plan assets of $3 million, partially offset by an increase in recognized net actuarial loss of $2 million and an increase in amortization of prior service costs of $2 million.

Net Interest Expense

Net interest expense includes interest on long-term debt and finance leases. Net interest expense was $206 million in the first quarter of 2024, an increase of $52 million, or 34%, from $154 million in the same period of 2023. The increase was primarily due to:

- interest of $37 million incurred on debt previously issued by KCS and exchanged with Canadian Pacific Railway Company ("CPRC") following the acquisition of control;
- higher interest on commercial paper of $15 million as a result of higher borrowings along with higher interest rates; and
- the impact of the KCS Purchasing Accounting of $5 million.

This increase was partially offset by lower interest costs of $4 million following the repayment of maturing long-term debt.

Income Tax Expense

Income tax expense was $259 million in the first quarter of 2024, an increase of $96 million, or 59%, from $163 million in the same period of 2023. The increase was primarily due to the impact of the KCS acquisition of $94 million, net of deferred tax recoveries on the amortization of business acquisition fair value adjustments of $22 million, and an outside basis deferred tax recovery of $23 million, recorded in the first quarter of 2023, arising from the difference between the carrying amount of CPKC's investment in KCS for financial reporting and the underlying tax basis of this investment, partially offset by lower taxable earnings resulting in a decrease to current tax expense.

The effective tax rate in the first quarter of 2024 was 25.09% compared to 16.90% in the same period of 2023. The Core adjusted effective tax rate in the first quarter of 2024 was 25.00%, compared to 24.50% in the same period of 2023. The Company's 2024 Core adjusted effective tax rate is expected to be between 25.00% to 25.50%. The Core adjusted effective tax rate is a Non-GAAP measure, calculated as the effective tax rate adjusted for significant items as they are not considered indicative of future financial trends either by nature or amount nor provide comparability to past performance. The Company uses the Core adjusted effective tax rate to evaluate CPKC’s operating performance and for planning and forecasting future profitability. Core adjusted effective tax rate also excludes equity earnings of KCS (net of tax) and KCS purchase accounting to provide financial statement users with additional transparency by isolating the impact of KCS purchase accounting. This Non-GAAP measure does not have a standardized meaning and is not defined by GAAP and, therefore, may not be comparable to similar measures presented by other companies. Significant items and KCS purchase accounting are discussed further in Non-GAAP Measures of this Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations. The Company’s 2024 outlook for its Core adjusted effective 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 new events and developments. This is discussed further in Item 1A. Risk Factors of the Company's 2023 Annual Report on Form 10-K.

Impact of Foreign Exchange on Earnings and Foreign Exchange Risk

Although the Company is headquartered in Canada and reports in Canadian dollars, a significant portion of its revenues, expenses, assets and liabilities including debt are denominated in U.S. dollars and Mexican pesos. In addition, equity earnings of KCS earned in the prior year 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, commodity prices, and Canadian, U.S., and international monetary policies. Fluctuations in FX affect the Company’s results because revenues and expenses denominated in U.S. dollars and Mexican pesos 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. Mexican peso-denominated revenues and expenses increase (decrease) when the U.S. dollar weakens (strengthens) in relation to the Mexican peso.

In the first quarter of 2024, the U.S. dollar has remained flat at an average rate of $1.35 Canadian/U.S. dollar, compared to the first quarter of 2023.

On an annualized basis, the Company expects that every $0.01 weakening (or strengthening) of the Canadian dollar relative to the U.S. dollar, positively (or negatively) impacts Total revenues by approximately $75 million (December 31, 2023 – approximately $75 million), negatively (or positively) impacts Operating expenses by approximately $47 million (December 31, 2023 – approximately $46 million), and negatively (or positively) impacts Net interest expense by approximately $6 million (December 31, 2023 – approximately $5 million).

On an annualized basis, the Company expects that every Ps.0.10 strengthening (or weakening) of the Mexican peso relative to the Canadian dollar, positively (or negatively) impacts Total revenues by approximately $8 million (December 31, 2023 – approximately $7 million) and negatively (or positively) impacts Operating expenses by approximately $9 million (December 31, 2023 – approximately $7 million).

To manage its exposure to fluctuations in exchange rates between Canadian dollars, U.S. dollars, and or Mexican pesos, the Company may sell or purchase U.S. dollar or Mexican peso 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 and Mexican peso) make the goods transported by the Company more or less competitive in the world marketplace and may in turn positively or negatively affect revenues.

Impact of Fuel Price on Earnings

Fluctuations in fuel prices affect the Company’s results because fuel expense constitutes a significant portion of the Company's operating costs. As fuel prices fluctuate, there will be a timing impact on earnings due to the timing of recoveries from the Company's fuel cost adjustment program.

The impact of fuel price on earnings includes the impacts of carbon taxes, levies, and obligations under cap-and-trade programs recovered and paid, on revenues and expenses, respectively.

In the first quarter of 2024, the unfavourable impact of fuel prices on Operating income was $41 million. Lower fuel prices and the unfavourable impact from the timing of recoveries under the Company's fuel cost adjustment program resulted in a decrease in Total revenues of $68 million from the same period of 2023. Lower fuel prices resulted in a decrease in Total operating expenses of $27 million from the same period of 2023.

Impact of Share Price on Earnings and Stock-Based Compensation

Fluctuations in the Common Share price affect the Company's operating expenses because share-based liabilities are measured at fair value. The Company's Common Shares are listed on the Toronto Stock Exchange ("TSX") and the New York Stock Exchange ("NYSE") with ticker symbol "CP".

In the first quarter of 2024, the change in Common Share prices resulted in stock-based compensation expense of $21 million, an increase of $17 million, from $4 million in the same period of 2023.

Based on information available at March 31, 2024 and expectations for 2024 share-based grants, for every $1.00 change in share price, stock-based compensation expense has a corresponding change of approximately $1.7 million to $2.4 million (December 31, 2023 - approximately $1.6 million to $2.3 million). This excludes the impact of changes in Common Share price relative to the S&P/TSX 60 Index, S&P 500 Industrials Index, and to Class I railways, which may trigger different performance share unit payouts. Stock-based compensation may also be impacted by non-market performance conditions.

Additional information concerning stock-based compensation is included in Item 1. Financial Statements, Note 13 Stock-based compensation.

Liquidity and Capital Resources

The Company's primary sources of liquidity include its Cash and cash equivalents, commercial paper program and bilateral letter of credit facilities. The Company believes that these sources as well as cash flow generated through operations and existing debt capacity are adequate to meet its short-term and long-term cash requirements. The Company is not aware of any material trends, events, or uncertainties that would create any deficiencies in the Company's liquidity.

As at March 31, 2024, the Company had $519 million of Cash and cash equivalents compared to $464 million at December 31, 2023.

During the three months ended March 31, 2024, the Company repaid U.S.$48 million ($66 million) 5.41% Senior Secured Notes.

The Company has a commercial paper program that enables it to issue commercial paper in the form of unsecured promissory notes. The Company's existing commercial paper program is backed by a U.S. $2.2 billion revolving credit facility. As at March 31, 2024, the Company had total commercial paper borrowings outstanding of U.S. $650 million ($881 million) (December 31, 2023 - U.S. $800 million).

The Company has bilateral letter of credit facilities with six highly rated financial institutions to support its requirement to post letters of credit in the ordinary course of business. Under these agreements, 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 letter of credit issued. These agreements permit the Company to withdraw amounts posted as collateral at any time; therefore, the amounts posted as collateral are presented as “Cash and cash equivalents” on the Company’s Consolidated Balance Sheets. As at March 31, 2024, the Company did not have any collateral posted on its bilateral letter of credit facilities (December 31, 2023 - $nil) and had letters of credit drawn of $91 million (December 31, 2023 - $93 million) from a total available amount of $300 million.

Contractual Commitments

The Company’s material cash requirements from known contractual obligations and commitments to make future payments primarily consist of long-term debt and related interest, supplier purchases, capital commitments, leases, and other long term liabilities. As at March 31, 2024 debt and finance leases, interest obligations related to debt and finance leases, and letters of credit amount to $3,909 million, $788 million and $91 million within the next 12 months, respectively, with remaining amounts committed thereafter of $19,523 million, $16,742 million and $nil, respectively. Future capital commitments amount to $897 million within the next 12 months, and $1,465 million committed thereafter.

Supplier purchase agreements and other long-term liabilities amount to $261 million and $70 million within the next 12 months, respectively, with remaining amounts committed thereafter of $309 million and $645 million, respectively. Other long-term liabilities include expected cash payments for environmental remediation, post-retirement benefits, worker’s compensation benefits, long-term disability benefits, pension benefit payments for the Company’s non-registered supplemental pension plan, and certain other long-term liabilities. Pension payments are discussed further in Critical Accounting Estimates of Item 7. Management’s Discussion and Analysis of Financial Condition and Results of Operations of the Company's 2023 Annual Report on Form 10-K.

Concession Duty

Under Kansas City Southern de México, S.A. de C.V. (also known as Canadian Pacific Kansas City Mexico) ("CPKCM")'s 50-year Concession, which could expire in 2047 unless extended, CPKCM pays annual concession duty expense of 1.25% of its gross revenues.

Guarantees

The Company accrues for all guarantees that it expects to pay. As at March 31, 2024, these accruals amounted to $11 million (December 31, 2023 - $8 million).

Operating Activities

Cash provided by operating activities was $1,015 million in the first quarter of 2024, an increase of $134 million, or 15%, compared to $881 million in the same period of 2023. The increase was primarily due to higher cash generating income, including the impact of the acquisition of KCS, compared to the same period of 2023. This was partially offset by the settlement of foreign currency forward contracts in the first quarter of 2024.

Investing Activities

Cash used in investing activities was $542 million in the first quarter of 2024, an increase of $141 million, or 35%, compared to $401 million in the same period of 2023. The increase was primarily due to higher capital additions, including the impact of the acquisition of KCS, compared to the same period of 2023.

Financing Activities

Cash used in financing activities was $431 million in the first quarter of 2024, a decrease of $214 million, or 33%, compared to $645 million in the same period of 2023. The decrease was primarily due to principal repayments of $66 million (U.S. $48 million) on the 5.41% Senior Secured Notes at maturity in the first quarter of 2024, compared to principal repayments of $479 million (U.S. $350 million) on the 4.450% 12.5-year at maturity in the same period of 2023. This decrease was partially offset by $205 million commercial paper repayments in the first quarter of 2024, compared to no repayments during the same period of 2023.

Credit Measures

Credit ratings provide information relating to the Company’s operations and liquidity, and affect the Company’s ability to obtain short-term and long-term financing and/or the cost of such financing. The applicable margin that applies to outstanding loans under the Company’s revolving credit facility is based on the credit rating assigned to the Company’s senior unsecured and unsubordinated debt.

If the Company’s credit ratings were to decline to below investment-grade levels, the Company could experience a significant increase in its interest cost for new debt along with a negative effect on its ability to readily issue new debt.

Credit ratings and outlooks are based on the rating agencies’ methodologies and can change from time to time to reflect their views of the Company. 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 March 31, 2024, the Company's credit ratings from Standard & Poor's Rating Services ("Standard & Poor's") remain unchanged from December 31, 2023. During the first quarter of 2024, Moody's Investor Service ("Moody's") upgraded the Company's outlook from stable to positive. The following table shows the ratings issued for the Company by the rating agencies noted as at March 31, 2024 and is being presented as it relates to the Company’s cost of funds and liquidity.

Credit ratings as at March 31, 2024[(1)]

Long-term debt		**Outlook**
Standard & Poor's	**BBB+**	stable
Moody's	**Baa2**	positive
Commercial paper program		
Standard & Poor's	**A-2**	N/A
Moody's	**P-2**	N/A

(1) Credit ratings are not recommendations to purchase, hold or sell securities and do not address the market price or suitability of a specific security for a particular investor. Credit ratings are based on the rating agencies' methodologies and may be subject to revision or withdrawal at any time by the rating agencies.

Supplemental Guarantor Financial Information

CPRC, a 100%-owned subsidiary of CPKC, is the issuer of certain securities which are fully and unconditionally guaranteed by CPKC on an unsecured basis. The other subsidiaries of CPRC do not guarantee the securities and are referred to below as the “Non-Guarantor Subsidiaries”. The following is a description of the terms and conditions of the guarantees with respect to securities for which CPRC is the issuer and CPKC provides a full and unconditional guarantee.

As of the date of filing this Form 10-Q, CPRC had U.S. $14,714 million principal amount of debt securities outstanding due through 2115 which includes the debt exchanged for KCS debt as described below; and U.S. $30 million and GBP £3 million in perpetual 4% consolidated debenture stock, for all of which CPKC is the guarantor subject to Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act"), as amended. As of the same date, CPRC also had $2,300 million principal amount of debt securities issued under Canadian Securities Law due through 2050 for which CPKC is the guarantor and not subject to the Exchange Act.

CPKC fully and unconditionally guarantees the payment of the principal (and premium, if any) and interest on the debt securities and consolidated debenture stock issued by CPRC, any sinking fund or analogous payments payable with respect to such securities, and any additional amounts payable when they become due, whether at maturity or otherwise. The guarantee is CPKC’s unsubordinated and unsecured obligation and ranks equally with all of CPKC’s other unsecured, unsubordinated obligations.

CPKC will be released and relieved of its obligations under the guarantees after obligations to the holders are satisfied in accordance with the terms of the respective instruments.

Pursuant to Rule 13-01 of the SEC's Regulation S-X, the Company provides summarized financial and non-financial information of CPRC in lieu of providing separate financial statements of CPRC.

More information on the securities under this guarantee structure can be found in Exhibit 22.1 List of Issuers and Guarantor Subsidiaries of this quarterly report.

Summarized Financial Information

The following tables present summarized financial information for CPRC (Subsidiary Issuer) and CPKC (Parent) on a combined basis after elimination of (i) intercompany transactions and balances among CPRC and CPKC; (ii) equity in earnings from and investments in the Non-Guarantor Subsidiaries; and (iii) intercompany dividend income.

Statements of Income

	CPRC (Subsidiary Issuer) and CPKC (Parent)	
(in millions of Canadian dollars)	**For the three months ended March 31, 2024**	For the year ended December 31, 2023
Total revenues	**$ 1,671**	$ 6,577
Total operating expenses	**1,102**	4,074
Operating income[(1)]	**569**	2,503
Less: Other[(2)]	**70**	468
Income before income tax expense	**499**	2,035
Net income	**$ 343**	$ 1,480

(1) Includes net lease costs incurred from non-guarantor subsidiaries for the three months ended March 31, 2024 and for the year ended December 31, 2023 of $115 million and $463 million, respectively.
(2) Includes Other (income) expense, Other components of net periodic benefit recovery, and Net interest expense.

Balance Sheets

	CPRC (Subsidiary Issuer) and CPKC (Parent)	
(in millions of Canadian dollars)	**As at March 31, 2024**	As at December 31, 2023
Assets		
Current assets	**$ 1,327**	$ 1,240
Properties	**12,483**	12,327
Other non-current assets	**3,657**	3,562
Liabilities		
Current liabilities	**$ 5,128**	$ 4,359
Long-term debt	**18,645**	19,169
Other non-current liabilities	**3,474**	3,412

Excluded from the Income Statements and Balance Sheets above are the following significant intercompany transactions and balances that CPRC and CPKC have with the Non-Guarantor Subsidiaries:

Transactions with Non-Guarantor Subsidiaries

	CPRC (Subsidiary Issuer) and CPKC (Parent)	
(in millions of Canadian dollars)	**For the three months ended March 31, 2024**	For the year ended December 31, 2023
Dividend income from non-guarantor subsidiaries	**$ 123**	$ 309
Capital contributions to non-guarantor subsidiaries	**—**	(4,324)

Balances with Non-Guarantor Subsidiaries

(in millions of Canadian dollars)	CPRC (Subsidiary Issuer) and CPKC (Parent) As at March 31, 2024	As at December 31, 2023
Assets		
Accounts receivable, intercompany	**$ 452**	$ 455
Short-term advances to affiliates	**1,685**	1,788
Long-term advances to affiliates	**11,311**	7,072
Liabilities		
Accounts payable, intercompany	**$ 248**	$ 347
Short-term advances from affiliates	**2,563**	2,783
Long-term advances from affiliates	**3,968**	—

Share Capital

At April 23, 2024, the latest practicable date, there were 932,704,551 Common Shares and no preferred shares issued and outstanding, which consists of 13,600 holders of record of the Common Shares. In addition, the Company has a Management Stock Option Incentive Plan (“MSOIP”), under which key officers and employees are granted options to purchase the Common Shares. All number of options presented herein are shown on the basis of the number of shares subject to the options. At April 23, 2024, 6,653,686 options were outstanding under the MSOIP and stand-alone option agreements entered into with Mr. Keith Creel. There are 21,002,149 options available to be issued by the Company’s MSOIP in the future. The Company also has a Director's Stock Option Plan (“DSOP”), under which directors are granted options to purchase Common Shares. There are no outstanding options under the DSOP, which has 1,700,000 options available to be issued in the future.

Non-GAAP Measures

The Company presents Non-GAAP measures, including Core adjusted combined operating ratio and Core adjusted combined diluted earnings per share, to provide an additional basis for evaluating underlying earnings trends in the Company's current period's financial results that can be compared with the results of operations in prior period. Management believes these Non-GAAP measures facilitate a multi-period assessment of long-term profitability.

These Non-GAAP measures have no standardized meaning and are not defined 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. 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.

Non-GAAP Performance Measures

On April 14, 2023, Canadian Pacific Railway Limited obtained control of KCS and CPKC began consolidating KCS, which had been accounted for under the equity method of accounting between December 14, 2021 and April 13, 2023. On the Control Date, CPKC’s previously-held interest in KCS was remeasured to its Control Date fair value. CPKC presents Core adjusted combined operating ratio and Core adjusted combined diluted earnings per share to give effect to results after isolating and removing the impact of the acquisition of KCS on those results. These measures provide a comparison to prior period financial information, as adjusted to exclude certain significant items, and are used to evaluate CPKC’s operating performance and for planning and forecasting future business operations and future profitability.

Management believes the use of Non-GAAP measures provides meaningful supplemental information about our operating results because they exclude certain significant items that are not considered indicative of future financial trends either by nature or amount or provide improved comparability to past performance. As a result, these items are excluded for management's 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, acquisition-related costs, adjustments to provisions and settlements of Mexican taxes, KCS's gain on unwinding of interest rate hedges (net of CPKC's associated purchase accounting basis differences and tax), as recognized within "Equity earnings of Kansas City Southern" in the Company's Interim Consolidated Statements of Income, loss on derecognition of CPKC’s previously held equity method investment in KCS, discrete tax items, changes in the outside basis tax difference between the carrying amount of CPKC's equity investment in KCS and its tax basis of this investment, a deferred tax recovery related to the elimination of the deferred tax liability on the outside basis difference of the investment, changes in income tax rates, changes to an uncertain tax item, and certain items outside the control of management. Acquisition-related costs include legal, consulting, integration costs including third-party services and system migration, debt exchange transaction costs, community investments, fair value gain or loss on foreign exchange ("FX") forward contracts and interest rate hedges, FX gain on U.S. dollar-denominated cash on hand from the issuances of long-term debt to fund the KCS acquisition, restructuring, employee retention and synergy incentive costs, and transaction and integration costs incurred by KCS. These items may not be non-recurring and may include items that are settled in cash. Specifically, due to the magnitude of the acquisition, its significant impact to the Company’s business and complexity of integrating the acquired business and operations, the Company expects to incur acquisition-related costs beyond the year of acquisition. Management believes excluding these significant items from GAAP results provides an additional viewpoint which may give users a consistent understanding of CPKC's financial performance when performing a multi-period assessment including assessing the likelihood of future results. Accordingly, these Non-GAAP financial measures may provide additional insight to investors and other external users of CPKC's financial information.

In addition, Core adjusted combined operating ratio and Core adjusted combined diluted earnings per share exclude KCS purchase accounting. KCS purchase accounting represents the amortization of basis differences being the incremental depreciation and amortization in relation to fair value adjustments to properties and intangible assets, incremental amortization in relation to fair value adjustments to KCS’s investments, amortization of the change in fair value of debt of KCS assumed on the Control Date, and depreciation and amortization of fair value adjustments that are attributable to non-controlling interest, as recognized within "Depreciation and amortization", "Other (income) expense", "Net interest expense", and "Net loss attributable to non-controlling interest", respectively, in the Company's Interim Consolidated Statements of Income. During the periods that KCS was equity accounted for, from December 14, 2021 to April 13, 2023, KCS purchase accounting represents the amortization of basis differences, being the difference in value between the consideration paid to acquire KCS and the underlying carrying value of the net assets of KCS immediately prior to its acquisition by the Company, net of tax, as recognized within "Equity earnings of Kansas City Southern" in the Company's Interim Consolidated Statements of Income. All assets subject to KCS purchase accounting contribute to income generation and will continue to amortize over their estimated useful lives. Excluding KCS purchase accounting from GAAP results provides financial statement users with additional transparency by isolating the impact of KCS purchase accounting.

Reconciliation of GAAP Performance Measures to Non-GAAP Performance Measures

The following tables reconcile the most directly comparable measures presented in accordance with GAAP to the Non-GAAP measures:

Core Adjusted Combined Diluted Earnings per Share

Core adjusted combined diluted earnings per share is calculated using Net income attributable to controlling shareholders reported on a GAAP basis adjusted for significant items less KCS purchase accounting, divided by the weighted-average diluted number of Common Shares outstanding during the period as determined in accordance with GAAP. Between December 14, 2021 and April 13, 2023, KCS was accounted for in CPKC's diluted earnings per share reported on a GAAP basis using the equity method of accounting and on a consolidated basis beginning April 14, 2023. As the equity method of accounting and consolidation both provide the same diluted earnings per share for CPKC, no adjustment is required to pre-control diluted earnings per share to be comparable on a consolidated basis.

In the three months ended March 31, 2024, there were two significant items included in the Net income attributable to controlling shareholders as reported on a GAAP basis as follows:

- adjustments to provisions for Mexican taxes of $10 million ($10 million after deferred tax recovery) recognized in "Compensation and benefits", that unfavourably impacted Diluted EPS by 1 cent; and
- acquisition-related costs of $26 million in connection with the KCS acquisition ($20 million after current tax recovery of $6 million) including costs of $4 million recognized in "Compensation and benefits", $2 million recognized in "Materials", and $20 million recognized in "Purchased services and other", that unfavourably impacted Diluted EPS by 2 cents.

In the three months ended March 31, 2023, there were two significant items included in Net income attributable to controlling shareholders as reported on a GAAP basis as follows:

- a deferred tax recovery of $23 million on changes in the outside basis difference of the equity investment in KCS that favourably impacted Diluted EPS by 3 cents; and
- acquisition-related costs of $25 million ($21 million after current tax recovery of $4 million), including costs of $12 million recognized in "Purchased services and other", $3 million recognized in "Other (income) expense", and $10 million recognized in "Equity earnings of KCS", that unfavourably impacted Diluted EPS by 2 cents.

KCS purchase accounting included in Net income attributable to controlling shareholders as reported on a GAAP basis was as follows:

2024:

- during the three months ended March 31, 2024, KCS purchase accounting of $84 million ($61 million after deferred tax recovery of $23 million), including costs of $79 million recognized in "Depreciation and amortization", $1 million recognized in "Purchased services and other" related to the amortization of equity investments, $5 million recognized in "Net interest expense", $1 million recognized in "Other (income) expense", and a recovery of $2 million recognized in "Net loss attributable to non-controlling interest", that unfavourably impacted Diluted EPS by 7 cents.

2023:
- during the three months ended March 31, 2023, KCS purchase accounting of $42 million recognized in "Equity earnings of KCS" that unfavourably impacted Diluted EPS by 5 cents.

	For the three months ended March 31	
	2024	2023
CPKC diluted earnings per share as reported	**$ 0.83**	$ 0.86
Less:		
Significant items (pre-tax):		
Adjustments to provisions and settlements of Mexican taxes	**(0.01)**	—
Acquisition-related costs	**(0.03)**	(0.03)
KCS purchase accounting	**(0.09)**	(0.05)
Add:		
Tax effect of adjustments[1]	**(0.03)**	(0.01)
Deferred tax recovery on the outside basis difference of the investment in KCS	**—**	(0.03)
Core adjusted combined diluted earnings per share[2]	**$ 0.93**	$ 0.90

(1) The tax effect of adjustments was calculated as the pre-tax effect of the significant items and KCS purchase accounting listed above multiplied by the applicable tax rate for the above items of 24.61% for the three months ended March 31, 2024, and 5.75% for the three months ended March 31, 2023, respectively. The applicable tax rates reflect the taxable jurisdictions and nature, being on account of capital or income, of the adjustments.

(2) The Company previously used the non-GAAP measure Core adjusted diluted earnings per share, which was calculated as diluted earnings per share adjusted for significant items less KCS purchase accounting. Core adjusted diluted earnings per share was $0.90 for the three months ended March 31, 2023, which is the same as the revised measure Core adjusted combined diluted earnings per share, as KCS was equity accounted for within CPKC's results.

Core Adjusted Combined Operating Ratio

Core adjusted combined operating ratio is calculated from reported GAAP revenue and operating expenses adjusted for (1) KCS operating income prior to the Control Date and giving effect to transaction accounting adjustments in a consistent manner with Regulation S-X Article 11 ("Article 11"), where applicable, (2) significant items (acquisition-related costs and adjustments to provisions and settlement of Mexican taxes) that are reported within Operating income, and (3) KCS purchase accounting recognized in "Depreciation and amortization" and "Purchased services and other".

This combined measure does not purport to represent what the actual consolidated results of operations would have been had the Company obtained control of KCS and consolidation actually occurred on January 1, 2022, nor is it indicative of future results. This information is based upon assumptions that CPKC believes reasonably reflect the impact to CPKC's historical financial information, on a supplemental basis, of obtaining control of KCS had it occurred as of January 1, 2022. This information does not include anticipated costs related to integration activities, cost savings or synergies that may be achieved by the combined company.

Significant items included in operating ratio on a combined basis were as follows:

2024:
- during the three months ended March 31, 2024, adjustments to provisions for Mexican taxes of $10 million recognized in "Compensation and benefits", that unfavourably impacted operating ratio by 0.3%; and
- during the three months ended March 31, 2024, acquisition-related costs were $26 million in connection with the KCS acquisition including costs of $4 million recognized in "Compensation and benefits", $2 million recognized in "Materials", and $20 million recognized in "Purchased services and other", that unfavourably impacted operating ratio by 0.8%.

2023:
- during the three months ended March 31, 2023, acquisition-related costs were $25 million in connection with the KCS acquisition, calculated in a manner consistent with Article 11, including costs of $11 million recognized in "Compensation and benefits" and $14 million recognized in "Purchased services and other", that unfavourably impacted operating ratio on a combined basis by 0.7%.

KCS purchase accounting included in operating ratio on a combined basis was as follows:

2024:
- during the three months ended March 31, 2024, KCS purchase accounting of $80 million including $79 million recognized in "Depreciation and amortization" and $1 million recognized in "Purchased services and other" related to the amortization of equity investments, that unfavourably impacted operating ratio by 2.3%.

2023:
- during the three months ended March 31, 2023, KCS purchase accounting of $80 million, calculated in a manner consistent with Article 11, recognized in "Depreciation and amortization", that unfavourably impacted operating ratio on a combined basis by 2.3%.

	For the three months ended March 31	
	2024	2023[3]
CPKC operating ratio as reported	**67.4 %**	63.4 %
Add:		
KCS operating income as reported prior to Control Date[1]	**— %**	0.8 %
Pro forma Article 11 transaction accounting adjustments[2]	**— %**	2.3 %
	67.4 %	66.5 %
Less:		
Adjustments to provisions and settlements of Mexican taxes	**0.3 %**	— %
Acquisition-related costs	**0.8 %**	0.7 %
KCS purchase accounting in Operating expenses	**2.3 %**	2.3 %
Core adjusted combined operating ratio	**64.0 %**	63.5 %

(1) KCS results were translated into Canadian dollars at the Bank of Canada monthly average rate for the three months ended March 31, 2023 of $1.35.

(2) Pro forma Article 11 transaction accounting adjustments represent adjustments made for the three months ended March 31, 2023 in a manner consistent with Article 11, and include depreciation and amortization of differences between the historic carrying values and the provisional fair values of KCS's tangible and intangible assets and investments prior to the Control Date that unfavourably impacted operating ratio by 2.3% and miscellaneous immaterial amounts that have been reclassified across revenue, operating expenses, and non-operating income or expense, consistent with CPKC's financial statement captions.

For more information about these pro forma transaction accounting adjustments for the three months ended March 31, 2023, please see Exhibit 99.1 “Selected Unaudited Combined Summary of Historical Financial Data” of CPKC’s Current Report on Form 8-K furnished with the Securities and Exchange Commission (“SEC”) on May 15, 2023.

(3) The Company previously used the Non-GAAP measure Adjusted operating ratio, which was defined as operating ratio excluding those significant items that are reported within Operating income. Adjusted operating ratio was 62.9% for the three months ended March 31, 2023, which was changed to the revised measure Core adjusted combined operating ratio. The change was due to the addition of KCS historical operating income less KCS acquisition-related costs (as defined above) prior to the Control Date. For the three months ended March 31, 2023, CPKC has presented the Non-GAAP measure of Core adjusted combined operating ratio, as defined above, to provide a comparison to prior period combined information calculated in a manner consistent with Article 11 as further adjusted to conform to CPKC’s core adjusted measures.

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 business acquisitions, goodwill and intangible assets, environmental liabilities, pensions and other benefits, property, plant and equipment, deferred income taxes, and personal injury and other claims liabilities. Additional information concerning critical accounting estimates is included in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations of the Company's 2023 Annual Report on Form 10-K.

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

Forward-Looking Statements

This Management's Discussion and Analysis of Financial Condition and Results of Operations 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 forward-looking information within the meaning of other relevant securities legislation, including applicable securities laws in Canada (collectively referred to herein as "forward-looking statements"). Forward-looking statements typically include words such as “financial expectations”, “key assumptions”, “anticipate”, “believe”, “expect”, "project", "estimate", "forecast", “plan”, "intend", "target", “will”, “outlook”, "guidance", “should” or similar words suggesting future outcomes. All statements other than statements of historical fact may be forward-looking statements. To the extent that the Company has provided forecasts or targets using Non-GAAP financial measures, the Company may not be able to provide a reconciliation to a GAAP measure without unreasonable efforts, due to unknown variables and uncertainty related to future results.

This Management's Discussion and Analysis of Financial Condition and Results of Operations and Quarterly Report on Form 10-Q includes forward-looking statements relating, but not limited to, statements concerning the Company’s expected impacts resulting from changes in the U.S. dollar and Mexican peso exchange rates relative to the Canadian dollar, and the effective tax rate, as well as 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, and statements regarding future payments including income taxes.

The forward-looking statements contained in this Management’s Discussion and Analysis of Financial Condition and Results of Operations and Quarterly Report on Form 10-Q are based on current expectations, estimates, projections and assumptions, having regard to the Company's experience and its perception of historical trends, and includes, but is not limited to, expectations, estimates, projections and assumptions relating to: change in business strategies; North American and global economic growth; commodity demand growth; sustainable industrial and agricultural production; commodity prices and interest rates; foreign exchange rates (as specified herein); effective tax rates (as specified herein); performance of our assets and equipment; sufficiency of our budgeted capital expenditures in carrying out our business plan; geopolitical conditions; applicable laws, regulations and government policies; the availability and cost of labour, services and infrastructure; labour disruptions; and the satisfaction by third parties of their obligations to the Company. Although the Company believes the expectations, estimates, projections and assumptions reflected in the forward-looking statements presented herein are reasonable as of the date hereof, there can be no assurance that they will prove to be correct. Current conditions, economic and otherwise, render assumptions, although reasonable when made, subject to greater uncertainty.

With respect to the KCS business combination, there can be no guarantee of the satisfaction of the conditions imposed by the STB in its March 15, 2023 final decision, successful integration of KCS or that the combined company will realize the anticipated benefits of the business combination, whether financial, strategic or otherwise, and this may be exacerbated by changes to the economic, political and global environment in which the merged company will operate.

Undue reliance should not be placed on forward-looking statements as actual results may differ materially from those expressed or implied by forward-looking statements. By their nature, forward-looking statements involve numerous inherent risks and uncertainties that could cause actual results to differ materially from the forward-looking statements, including but not limited to the following factors: changes in business strategies; general North American and global economic, credit and business conditions; risks associated with 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; changes in commodity prices; uncertainty surrounding timing and volumes of commodities being shipped via the Company; inflation; geopolitical instability; changes in laws, regulations and government policies, including regulation of rates; changes in taxes and tax rates; potential increases in maintenance and operating costs; changes in fuel prices; 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 and discount rates on the financial position of pension plans and investments; trade restrictions or other changes to international trade arrangements; climate change; various events that could disrupt operations, including severe weather, such as droughts, floods, avalanches, volcanism and earthquakes, and cybersecurity attacks, as well as security threats and governmental response to them, and technological changes; and the outbreak of a pandemic or contagious disease and the resulting effects on economic conditions, the demand environment for logistics requirements and energy prices, restrictions imposed by public health authorities or governments, fiscal and monetary policy responses by governments and financial institutions, and disruptions to global supply chains. The foregoing list of factors is not exhaustive.

There are more specific factors that could cause actual results to differ materially from those described in the forward-looking statements contained in this Management's Discussion and Analysis of Financial Condition and Results of Operations and Quarterly Report on Form 10-Q. These more specific factors are identified and discussed in Item 1A. Risk Factors of the Company's 2023 Annual Report on Form 10-K. Other risks are detailed from time to time in reports filed by the Company with securities regulators in Canada and the United States.

The forward-looking statements contained in this Management’s Discussion and Analysis of Financial Condition and Results of Operations and Quarterly Report on Form 10-Q are made as of the date hereof. Except as required by law, the Company undertakes no obligation to update publicly or otherwise revise any forward-looking statements, or the foregoing assumptions and risks affecting such forward-looking statements, whether as a result of new information, future events or otherwise.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Information concerning market risk sensitive instruments is set forth under Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations – Impact of FX on Earnings and Foreign Exchange Risk and Impact of Share Price on Earnings and Stock-Based Compensation.

Interest Rate Risk

Debt financing forms part of the Company's capital structure. The debt agreements entered into expose the Company to increased interest costs on future fixed debt instruments and existing variable rate debt instruments, should market rates increase. As at March 31, 2024, a hypothetical one percentage point change in interest rates on the Company's floating rate debt obligations outstanding is not material. In addition, the present value of the Company’s assets and liabilities will also vary with interest rate changes. To manage interest rate exposure, the Company may enter into forward rate agreements such as treasury rate locks or bond locks that lock in rates for a future date, thereby protecting against interest rate increases. The Company may also enter into swap agreements whereby one party agrees to pay a fixed rate of interest while the other party pays a floating rate. Contingent on the direction of interest rates, the Company may incur higher costs depending on the contracted rate.

The fair value of the Company’s fixed rate debt may fluctuate with changes in market interest rates. A hypothetical one percentage point decrease in interest rates as at March 31, 2024 would result in an increase of approximately $1.8 billion to the fair value of the Company's debt as at March 31, 2024 (March 31, 2023 - approximately $1.5 billion). Fair values of the Company’s fixed rate debt are estimated by considering the impact of the hypothetical interest rates on quoted market prices and current borrowing rates, but do not consider other factors that could impact actual results.

Information concerning market risks is supplemented in Item 1. Financial Statements, Note 11 Financial instruments.

ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

As at March 31, 2024, an evaluation was carried out under the supervision of and with the participation of the Company'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 at March 31, 2024, 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 first quarter of 2024, 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.

PART II

ITEM 1. LEGAL PROCEEDINGS

For further details refer to Item 1. Financial Statements, Note 14 Contingencies.

SEC regulations require the disclosure of any proceeding under environmental laws to which a government authority is a party unless the registrant reasonably believes it will not result in sanctions over a certain threshold. The Company uses a threshold of U.S. $1 million for the purposes of determining proceedings requiring disclosure.

From time to time, the Company or its subsidiaries may be subject to information requests from U.S. State or Federal environmental regulatory authorities inquiring as to the Company's compliance or remediation practices in the U.S. In September 2020, the Company received an initial request for information from the U.S. Environmental Protection Agency ("EPA") inquiring into the Company's compliance with the mobile source provisions of the Clean Air Act ("CAA"). The Company has been providing information in response to the EPA's initial and follow-up requests, and the EPA has issued Notices of Violations, which preliminarily identify certain categories of alleged non-compliance with civil provisions of the CAA pertaining to locomotives and locomotive engines. In December 2022, the U.S. Department of Justice ("DOJ") sent a communication requesting a meeting with the Company to discuss potentially resolving any alleged noncompliance which included an initial draft consent decree from the DOJ. That initial meeting occurred in January 2023 and communications are ongoing. Neither the EPA nor the DOJ has issued a final compendium of alleged violations, demand for corrective or mitigating actions, or articulated a preliminary civil penalty assessment, and it remains too early to provide a fulsome evaluation of the likely outcome with respect to either the nature of any alleged violations or the amount of any potential civil penalty. The Company will continue to fully cooperate and engage in discussions to resolve the matter.