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Update on Transportation of Grain by Canadian Railways

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Report Highlights:
A new Order in Council set minimum weekly grain shipments for Canada's two rail companies from August 3 through November 29, 2014, at 536,250 MT. Significant concerns were expressed by many on the effect of these mandates on rail service in the United States and the possibility that they were going to be expended beyond the November 29, 2014 expiring date. There are strong indications from the Canadian government that the minimum volume mandates imposed on the Canadian railways Canadian National (CN) and Canadian Pacific (CP) will be suspended once they expire on November 29, 2014. Uncertainty remains on how the likely suspension of the mandates will affect service along other corridors, including south to the United States.

Update on Transportation of Grain by Canadian Railways

Mandated Minimum Volume Rail Service for Grains Likely to be Suspended:

A new Order in Council set minimum weekly grain shipments for Canada's two rail companies from August 3 through November 29, 2014, at 536,250 MT. This is a slight increase over the 500,000 MT minimum set in a March 8, 2014 an Order in Council. Failure by Canadian National (CN) and Canadian Pacific (CP) to comply with the minimum volume of grain movement could result in penalties of up to CDN$100,000 per violation. In order to satisfy these obligations, the railroads indicated they would be forced to reduce service levels on southbound shipments to the United States.

Significant concerns were expressed by many on the effect of these mandates on rail service in the United States and the possibility that they were going to be expended beyond the November 29, 2014 expiring date. There are strong indications from the Canadian government that the minimum volume mandates imposed on the Canadian railways Canadian National (CN) and Canadian Pacific (CP) will be suspended once they expire on November 29, 2014. In a recent interview, Canadian Minister of Agriculture Gerry Ritz stated that unless the government sees a significant and sudden pile-up of grain across the Western Canada, the minimum volume mandates will be removed as they will have served their purpose. The Minister is reported to have stated that only a complete failure by the railways to move grain will result in the mandates being extended.

It is uncertain how the likely suspension of the mandates will affect service along other corridors, including south to the United States. Industry discussions reveal that it is more likely the huge backlog of grain and public relations, rather than the threat of fines for non-compliance, that has concentrated the rail effort to the Western ports. To achieve maximum velocity, the railways have focused on maximizing usage of their most efficient corridors and directed grain companies on where the cars will be spotted. The expectation from industry is that the velocity of the trains will slow down if the railways begin servicing the eastern and southern corridors more completely. Service south to the United States will continue to be at a disadvantage as cycle times past Chicago are reportedly nearly twice what they are to go to the Western ports in Canada and will continue to face competition from the continued strong demand for rail service in Canada resulting from high carry-in stocks.

Current Conditions Improve Slightly Over Last Year:

Statistics and industry confirm that the situation this fall is somewhat different from the previous year and that most of the problems that remain are systemic problems to hopefully be addressed through the review of the Canada Transportation Act which is ongoing. While the lower production level in 2014/2015 has not been able to completely off-set the very high carry-in stocks, the distribution of stocks across the country and terminals should prevent the severe delays to load ships that occurred in late 2013 and early 2014 while grain companies waited for grain deliveries. Industry statistics show that vessel lineups in the Port of Vancouver are beginning to stabilize but remain higher than any other year for the same time period. This is a reflection of both record level exports and strained logistics under high stocks.

Railway Car Order Systems Changing:

Canadian railways are also making changes and planning to eliminate their open order systems. Canadian National (CN) will be limiting orders to two weeks and to a maximum of twice the car spots of the facility. CN, much to the dismay of the smaller shippers, has also stated that it will continue to allocate according to historical data. CN has stated that shortfalls will be given priority to the next week's available cars (roll to the following week).

Canadian Pacific (CP) is putting in place a `destination` train program that has a shuttle concept for companies that decided to contract this service. Some companies are in favor of this because it appears at least some accountability will be built into the program, which they have long-argued has been lacking in the shipper/railways relationship. Cars and power that are not in the program will be allocated through the normal manifest car allocation program.

There are a number of initiatives underway to attempt to transform the Canadian rail system and force it to build more capacity. The Canadian grain industry and all shippers are united in seeking a more clear definition of what constitutes an adequate level of service and have penalties that are big enough to ensure compliance. Several organizations including Pulse Canada and the Canada Grains Councils are working on ways to position Canada so that it will be able to take advantage of the increase in trade that is anticipated to occur as a result of the trade agreements that Canada has recently signed (the CETA with Europe and the South Korean Free Trade Deal). Canada's challenge will be how to adjust its rail service to account for increased demand and service industries built around a just-in-time business model.

Implementing regulations for the *Fair Rail for Grain Farmers Act*, released on August 1, 2014, extend the interswitching distances for shippers in western provinces from 30 to 160 km, set new reporting requirements by railway companies on movement of grains, clarify parameters for level of service arbitration, and provide for penalties for grain buyers for failure to take delivery of grain for which they have contracted. These changes do not address fully the systemic challenges that will be the focus of the Canadian Transportation Act review. Results of the Canadian Transportation Act review and the recommendations that will be put forward to Parliament in late 2015 are highly anticipated as it could have a significant impact on how well Canada will be able to take advantage of new trade opportunities.