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Innovation in motion

2017 QUARTERLY REVIEW SECOND QUARTER

North America's Railroad

CN reports Q2-2017 net income of C$1,031 million, or C$1.36 per diluted share

Continued strong volume growth leads to record revenues and 21 per cent increase in adjusted diluted earnings per share (EPS) (1)

MONTREAL, July 25, 2017 — CN (TSX: CNR) (NYSE: CNI) today reported its financial and operating results for the second quarter and six-month period ended June 30, 2017.

Second-quarter 2017 financial highlights

- Net income increased 20 per cent to C$1,031 million, while diluted EPS increased 24 per cent to C$1.36, compared with the second quarter of 2016.
- Adjusted net income increased 17 per cent to C$1,013 million, with adjusted diluted EPS increasing 21 per cent to C$1.34. (1)
- Operating income increased 16 per cent to C$1,495 million.
- Revenues increased by 17 per cent to a quarterly record of C$3,329 million. Carloadings increased 14 per cent, and revenue ton-miles increased 18 per cent.
- Operating expenses increased 18 per cent to C$1,834 million.
- Operating ratio of 55.1 per cent, an increase of 0.6 points over the prior-year quarter.
- Free cash flow (1) for second-quarter 2017 was C$811 million, up from C$585 million for the year-earlier quarter.

Luc Jobin, president and chief executive officer, said: "Once again, CN delivered solid quarterly performance with strong volume growth across most commodity groups, building on the momentum started in the fourth quarter of 2016. Our team of railroaders remained focused on balancing operational and service excellence while efficiently adjusting to the growing demand.

"The North American economic outlook continues to be positive, and we remain committed to delivering on our 2017 financial outlook. However, volume comparisons in the second half of the year will be more challenging, and the strengthening of the Canadian dollar will constitute a headwind."

Reaffirmed 2017 financial outlook (2)

CN aims to deliver 2017 adjusted diluted EPS in the range of C$4.95 to C$5.10 compared to last year's adjusted diluted EPS (1) of C$4.59.

Foreign currency impact on results

Although CN reports its earnings in Canadian dollars, a large portion of its revenues and expenses is denominated in U.S. dollars. The fluctuation of the Canadian dollar relative to the U.S. dollar affects the conversion of the Company's U.S.-dollar-denominated revenues and expenses. On a constant currency basis, (1) CN's net income for the second quarter of 2017 would have been lower by C$28 million, or C$0.04 per diluted share.

Second-quarter 2017 revenues, traffic volumes and expenses

Revenues for the second quarter of 2017 were C$3,329 million, an increase of 17 per cent, when compared to the same period in 2016. Revenues increased for metals and minerals (33 per cent), coal (33 per cent), grain and fertilizers (23 per cent), automotive (20 per cent), intermodal (17 per cent), petroleum and chemicals (12 per cent), and forest products (six per cent).

The increase in revenues was mainly attributable to higher volumes across several sectors, such as Canadian grain and fertilizers, overseas intermodal traffic, frac sand, coal and petroleum coke exports, crude oil, and finished vehicles. Also contributing to increased revenues were higher applicable fuel surcharge rates, freight rate increases, and the positive translation impact of a weaker Canadian dollar.

Carloadings for the quarter increased by 14 per cent to 1.4 million.

Revenue ton-miles (RTMs), measuring the relative weight and distance of rail freight transported by CN, increased by 18 per cent from the year-earlier quarter. Rail freight revenue per RTM decreased by 1 per cent over the year-earlier period, mainly driven by an increase in the average length of haul; partly offset by higher applicable fuel surcharge rates, freight rate increases, and the positive translation impact of a weaker Canadian dollar.

Operating expenses for the second quarter increased by 18 per cent to C$1,834 million, mainly due to higher fuel costs, increased purchased services and material costs, and higher labor and fringe benefits expense resulting from increased volumes, as well as increased casualty and other expense, and the negative translation impact of a weaker Canadian dollar.

(1) Non-GAAP Measures

CN reports its financial results in accordance with United States generally accepted accounting principles (GAAP). CN also uses non-GAAP measures in this news release that do not have any standardized meaning prescribed by GAAP, including adjusted performance measures, constant currency, and free cash flow. These non-GAAP measures may not be comparable to similar measures presented by other companies. For further details of these non-GAAP measures, including a reconciliation to the most directly comparable GAAP financial measures, refer to the attached supplementary schedule, Non-GAAP Measures.

CN's full-year adjusted EPS outlook (2) excludes the expected impact of certain income and expense items, as well as those items noted in the reconciliation tables provided in the attached supplementary schedule, Non-GAAP Measures. However, management cannot individually quantify on a forward-looking basis the impact of these items on its EPS because these items, which could be significant, are difficult to predict and may be highly variable. As a result, CN does not provide a corresponding GAAP measure for, or reconciliation to, its adjusted EPS outlook.

(2) Forward-Looking Statements

Certain statements included in this news release constitute “forward-looking statements” within the meaning of the United States Private Securities Litigation Reform Act of 1995 and under Canadian securities laws. By their nature, forward-looking statements involve risks, uncertainties and assumptions. The Company cautions that its assumptions may not materialize and that current economic conditions render such assumptions, although reasonable at the time they were made, subject to greater uncertainty. Forward-looking statements may be identified by the use of terminology such as “believes,” “expects,” “anticipates,” “assumes,” “outlook,” “plans,” “targets,” or other similar words.

2017 key assumptions

CN has made a number of economic and market assumptions in preparing its 2017 outlook. The Company assumes that North American industrial production for the year will increase by approximately two per cent, and assumes U.S. housing starts in the range of 1.25 million units. The Company now assumes U.S. motor vehicle sales of approximately 17 million units (compared to its April 24, 2017 assumption of approximately 17.5 million units.) For the 2016/2017 crop year, the grain crops in both the United States and Canada were above their respective five-year averages. The Company assumes that the 2017/2018 grain crops in both Canada and the United States will be in line with their respective five-year averages. With these assumptions, CN assumes total RTMs in 2017 will increase by approximately 10 per cent versus 2016. CN expects continued pricing improvement above inflation. CN now assumes that in 2017 the value of the Canadian dollar in U.S. currency will be in the range of $0.75 to $0.80 (compared to its April 24, 2017 assumption in the range of $0.75), and that the average price of crude oil (West Texas Intermediate) will be in the range of US$40 to US$50 per barrel (compared to its April 24, 2017 assumption in the range of US$50 to US$60 per barrel.) In 2017, CN plans to invest approximately C$2.6 billion in its capital program, of which C$1.6 billion is targeted toward track infrastructure.

Forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company to be materially different from the outlook or any future results or performance implied by such statements. Accordingly, readers are advised not to place undue reliance on forward-looking statements. Important risk factors that could affect the forward-looking statements include, but are not limited to, the effects of general economic and business conditions; industry competition; inflation, currency and interest rate fluctuations; changes in fuel prices; legislative and/or regulatory developments; compliance with environmental laws and regulations; actions by regulators; increases in maintenance and operating costs; security threats; reliance on technology; trade restrictions; transportation of hazardous materials; various events which could disrupt operations, including natural events such as severe weather, droughts, floods and earthquakes; climate change; labor negotiations and disruptions; environmental claims; uncertainties of investigations, proceedings or other types of claims and litigation; risks and liabilities arising from derailments; timing and completion of capital programs; and other risks detailed from time to time in reports filed by CN with securities regulators in Canada and the United States. Reference should be made to Management's Discussion and Analysis (MD&A) in CN's annual and interim reports, Annual Information Form and Form 40-F, filed with Canadian and U.S. securities regulators and available on CN's website, for a description of major risk factors.

Forward-looking statements reflect information as of the date on which they are made. CN assumes no obligation to update or revise forward-looking statements to reflect future events, changes in circumstances, or changes in beliefs, unless required by applicable securities laws. In the event CN does update any forward-looking statement, no inference should be made that CN will make additional updates with respect to that statement, related matters, or any other forward-looking statement.

This earnings news release, as well as additional information, including the Financial Statements, Notes thereto and MD&A, is contained in CN's Quarterly Review available on the Company's website at www.cn.ca/financial-results and on SEDAR at www.sedar.com as well as on EDGAR at www.sec.gov.

CN is a true backbone of the economy whose team of approximately 23,000 railroaders transports more than C$250 billion worth of goods annually for a wide range of business sectors, ranging from resource products to manufactured products to consumer goods, across a rail network of approximately 20,000 route-miles spanning Canada and mid-America. CN – Canadian National Railway Company, along with its operating railway subsidiaries – serves the cities and ports of Vancouver, Prince Rupert, B.C., Montreal, Halifax, New Orleans, and Mobile, Ala., and the metropolitan areas of Toronto, Edmonton, Winnipeg, Calgary, Chicago, Memphis, Detroit, Duluth, Minn./Superior, Wis., and Jackson, Miss., with connections to all points in North America. For more information about CN, visit the Company's website at www.cn.ca.

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Selected Railroad Statistics – unaudited

	Three months ended June 30		Six months ended June 30	
	2017	2016	**2017**	2016
Financial measures				
Key financial performance indicators (1)				
Total revenues *($ millions)*	**3,329**	2,842	**6,535**	5,806
Rail freight revenues *($ millions)*	**3,111**	2,646	**6,186**	5,491
Operating income *($ millions)*	**1,495**	1,293	**2,798**	2,510
Net income *($ millions)*	**1,031**	858	**1,915**	1,650
Diluted earnings per share *($)*	**1.36**	1.10	**2.51**	2.10
Adjusted diluted earnings per share *($)* (2)	**1.34**	1.11	**2.48**	2.11
Free cash flow *($ millions)* (2)	**811**	585	**1,659**	1,169
Gross property additions *($ millions)*	**675**	670	**1,071**	1,139
Share repurchases *($ millions)*	**521**	533	**1,012**	1,053
Dividends per share *($)*	**0.4125**	0.3750	**0.8250**	0.7500
Financial position (1)				
Total assets *($ millions)*	**37,245**	36,094	**37,245**	36,094
Total liabilities *($ millions)*	**22,194**	21,281	**22,194**	21,281
Shareholders' equity *($ millions)*	**15,051**	14,813	**15,051**	14,813
Financial ratio				
Operating ratio *(%)*	**55.1**	54.5	**57.2**	56.8
Operational measures (3)				
Statistical operating data				
Gross ton miles (GTMs) *(millions)*	**117,195**	99,999	**233,430**	203,467
Revenue ton miles (RTMs) *(millions)*	**58,789**	49,717	**118,565**	101,973
Carloads *(thousands)*	**1,424**	1,249	**2,792**	2,504
Route miles *(includes Canada and the U.S.)*	**19,500**	19,600	**19,500**	19,600
Employees *(end of period)*	**23,089**	22,162	**23,089**	22,162
Employees *(average for the period)*	**22,858**	22,230	**22,627**	22,462
Key operating measures				
Rail freight revenue per RTM *(cents)*	**5.29**	5.32	**5.22**	5.38
Rail freight revenue per carload *($)*	**2,185**	2,118	**2,216**	2,193
GTMs per average number of employees *(thousands)*	**5,127**	4,498	**10,316**	9,058
Operating expenses per GTM *(cents)*	**1.56**	1.55	**1.60**	1.62
Labor and fringe benefits expense per GTM *(cents)*	**0.45**	0.47	**0.47**	0.52
Diesel fuel consumed *(US gallons in millions)*	**108.6**	93.6	**221.5**	197.3
Average fuel price *($/US gallon)*	**2.65**	2.30	**2.71**	2.18
GTMs per US gallon of fuel consumed	**1,079**	1,068	**1,054**	1,031
Terminal dwell *(hours)*	**14.6**	13.6	**15.0**	14.0
Train velocity *(miles per hour)*	**26.1**	27.6	**25.9**	27.5
Safety indicators (4)				
Injury frequency rate *(per 200,000 person hours)*	**1.54**	1.48	**1.71**	1.57
Accident rate *(per million train miles)*	**1.61**	1.57	**1.58**	1.33

(1) Amounts expressed in Canadian dollars and prepared in accordance with United States generally accepted accounting principles (GAAP), unless otherwise noted.

(2) See supplementary schedule entitled Non-GAAP Measures for an explanation of these non-GAAP measures.

(3) Statistical operating data, key operating measures and safety indicators are unaudited and based on estimated data available at such time and are subject to change as more complete information becomes available. Definitions of these indicators are provided on CN's website, www.cn.ca/glossary.

(4) Based on Federal Railroad Administration (FRA) reporting criteria.

Supplementary Information – unaudited

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change Fav (Unfav)	% Change at constant currency Fav (Unfav) (1)	**2017**	2016	% Change Fav (Unfav)	% Change at constant currency Fav (Unfav) (1)
Revenues *($ millions)* (2)								
Petroleum and chemicals	**549**	492	12%	8%	**1,133**	1,070	6%	6%
Metals and minerals	**389**	292	33%	29%	**750**	602	25%	24%
Forest products	**464**	439	6%	2%	**911**	901	1%	1%
Coal	**126**	95	33%	29%	**255**	188	36%	36%
Grain and fertilizers	**530**	432	23%	20%	**1,137**	954	19%	19%
Intermodal	**815**	697	17%	15%	**1,557**	1,390	12%	12%
Automotive	**238**	199	20%	16%	**443**	386	15%	15%
Total rail freight revenues	**3,111**	2,646	18%	15%	**6,186**	5,491	13%	13%
Other revenues	**218**	196	11%	8%	**349**	315	11%	10%
Total revenues	**3,329**	2,842	17%	14%	**6,535**	5,806	13%	12%
Revenue ton miles (RTMs) *(millions)* (3)								
Petroleum and chemicals	**11,027**	9,575	15%	15%	**22,855**	20,881	9%	9%
Metals and minerals	**6,887**	4,751	45%	45%	**13,330**	9,454	41%	41%
Forest products	**7,789**	7,807	-	-	**15,479**	15,736	(2%)	(2%)
Coal	**3,355**	2,686	25%	25%	**6,957**	4,934	41%	41%
Grain and fertilizers	**13,415**	10,353	30%	30%	**28,902**	22,883	26%	26%
Intermodal	**15,109**	13,519	12%	12%	**28,813**	26,182	10%	10%
Automotive	**1,207**	1,026	18%	18%	**2,229**	1,903	17%	17%
Total RTMs	**58,789**	49,717	18%	18%	**118,565**	101,973	16%	16%
Rail freight revenue / RTM *(cents)* (2) (3)								
Petroleum and chemicals	**4.98**	5.14	(3%)	(6%)	**4.96**	5.12	(3%)	(3%)
Metals and minerals	**5.65**	6.15	(8%)	(11%)	**5.63**	6.37	(12%)	(12%)
Forest products	**5.96**	5.62	6%	2%	**5.89**	5.73	3%	2%
Coal	**3.76**	3.54	6%	4%	**3.67**	3.81	(4%)	(4%)
Grain and fertilizers	**3.95**	4.17	(5%)	(7%)	**3.93**	4.17	(6%)	(6%)
Intermodal	**5.39**	5.16	4%	3%	**5.40**	5.31	2%	2%
Automotive	**19.72**	19.40	2%	(1%)	**19.87**	20.28	(2%)	(2%)
Total rail freight revenue / RTM	**5.29**	5.32	(1%)	(3%)	**5.22**	5.38	(3%)	(3%)
Carloads *(thousands)* (3)								
Petroleum and chemicals	**149**	141	6%	6%	**306**	294	4%	4%
Metals and minerals	**245**	186	32%	32%	**477**	364	31%	31%
Forest products	**108**	110	(2%)	(2%)	**215**	223	(4%)	(4%)
Coal	**71**	73	(3%)	(3%)	**144**	152	(5%)	(5%)
Grain and fertilizers	**149**	129	16%	16%	**313**	275	14%	14%
Intermodal	**628**	542	16%	16%	**1,196**	1,065	12%	12%
Automotive	**74**	68	9%	9%	**141**	131	8%	8%
Total carloads	**1,424**	1,249	14%	14%	**2,792**	2,504	12%	12%
Rail freight revenue / carload *($)* (2) (3)								
Petroleum and chemicals	**3,685**	3,489	6%	2%	**3,703**	3,639	2%	2%
Metals and minerals	**1,588**	1,570	1%	(2%)	**1,572**	1,654	(5%)	(5%)
Forest products	**4,296**	3,991	8%	4%	**4,237**	4,040	5%	5%
Coal	**1,775**	1,301	36%	33%	**1,771**	1,237	43%	43%
Grain and fertilizers	**3,557**	3,349	6%	4%	**3,633**	3,469	5%	5%
Intermodal	**1,298**	1,286	1%	(1%)	**1,302**	1,305	-	-
Automotive	**3,216**	2,926	10%	7%	**3,142**	2,947	7%	6%
Total rail freight revenue / carload	**2,185**	2,118	3%	1%	**2,216**	2,193	1%	1%

(1) See supplementary schedule entitled Non-GAAP Measures for an explanation of this non-GAAP measure.

(2) Amounts expressed in Canadian dollars.

(3) Statistical operating data and related key operating measures are based on estimated data available at such time and are subject to change as more complete information becomes available.

Non-GAAP Measures – unaudited

In this supplementary schedule, the word "Company" or "CN" means Canadian National Railway Company and, as the context requires, its wholly-owned subsidiaries. Financial information included in this schedule is expressed in Canadian dollars, unless otherwise noted.

CN reports its financial results in accordance with United States generally accepted accounting principles (GAAP). The Company also uses non-GAAP measures that do not have any standardized meaning prescribed by GAAP, including adjusted performance measures, constant currency, free cash flow, and adjusted debt-to-adjusted EBITDA multiple. These non-GAAP measures may not be comparable to similar measures presented by other companies. From management's perspective, these non-GAAP measures are useful measures of performance and provide investors with supplementary information to assess the Company's results of operations and liquidity. These non-GAAP measures should not be considered in isolation or as a substitute for financial measures prepared in accordance with GAAP.

Adjusted performance measures

Management believes that adjusted net income and adjusted earnings per share are useful measures of performance that can facilitate period-to-period comparisons, as they exclude items that do not necessarily arise as part of CN's normal day-to-day operations and could distort the analysis of trends in business performance. Management uses these measures, which exclude certain income and expense items in its results that management believes are not reflective of CN's underlying business operations, to set performance goals and as a means to measure CN's performance. The exclusion of items in adjusted net income and adjusted earnings per share does not, however, imply that these items are necessarily non-recurring. These measures do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

For the three and six months ended June 30, 2017, the Company reported adjusted net income of $1,013 million, or $1.34 per diluted share, and $1,892 million, or $2.48 per diluted share, respectively. The adjusted figures for the three months ended June 30, 2017 exclude a deferred income tax recovery of $18 million ($0.02 per diluted share), resulting from the enactment of a lower provincial corporate income tax rate. The adjusted figures for the six months ended June 30, 2017 exclude a deferred income tax recovery of $18 million ($0.02 per diluted share) in the second quarter and $5 million ($0.01 per diluted share) in the first quarter, resulting from the enactment of lower provincial corporate income tax rates.

For the three and six months ended June 30, 2016, the Company reported adjusted net income of $865 million, or $1.11 per diluted share, and $1,657 million, or $2.11 per diluted share, respectively, which exclude a deferred income tax expense of $7 million ($0.01 per diluted share) in the second quarter, resulting from the enactment of a higher provincial corporate income tax rate.

The following table provides a reconciliation of net income and earnings per share, as reported for the three and six months ended June 30, 2017 and 2016, to the adjusted performance measures presented herein:

	Three months ended June 30		Six months ended June 30	
In millions, except per share data	**2017**	2016	**2017**	2016
Net income as reported	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Adjustment: Income tax expense (recovery)	**(18)**	7	**(23)**	7
Adjusted net income	**$ 1,013**	$ 865	**$ 1,892**	$ 1,657
Basic earnings per share as reported	**$ 1.36**	$ 1.10	**$ 2.52**	$ 2.11
Impact of adjustments, per share	**(0.02)**	0.01	**(0.03)**	0.01
Adjusted basic earnings per share	**$ 1.34**	$ 1.11	**$ 2.49**	$ 2.12
Diluted earnings per share as reported	**$ 1.36**	$ 1.10	**$ 2.51**	$ 2.10
Impact of adjustments, per share	**(0.02)**	0.01	**(0.03)**	0.01
Adjusted diluted earnings per share	**$ 1.34**	$ 1.11	**$ 2.48**	$ 2.11

Non-GAAP Measures – unaudited

Constant currency

Financial results at constant currency allow results to be viewed without the impact of fluctuations in foreign currency exchange rates, thereby facilitating period-to-period comparisons in the analysis of trends in business performance. Measures at constant currency are considered non-GAAP measures and do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies. Financial results at constant currency are obtained by translating the current period results denominated in US dollars at the foreign exchange rates of the comparable period in the prior year. The average foreign exchange rates were $1.35 and $1.33 per US$1.00, respectively, for the three and six months ended June 30, 2017, and $1.29 and $1.33 per US$1.00, respectively, for the three and six months ended June 30, 2016.

On a constant currency basis, the Company's net income for the three and six months ended June 30, 2017 would have been lower by $28 million ($0.04 per diluted share) and $6 million ($0.01 per diluted share), respectively.

Free cash flow

Management believes that free cash flow is a useful measure of liquidity as it demonstrates the Company's ability to generate cash for debt obligations and for discretionary uses such as payment of dividends, share repurchases, and strategic opportunities. The Company defines its free cash flow measure as the difference between net cash provided by operating activities and net cash used in investing activities; adjusted for the impact of major acquisitions, if any. Free cash flow does not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

The following table provides a reconciliation of net cash provided by operating activities as reported for the three and six months ended June 30, 2017 and 2016, to free cash flow:

	Three months ended June 30		Six months ended June 30	
In millions	**2017**	2016	**2017**	2016
Net cash provided by operating activities	**$ 1,505**	$ 1,271	**$ 2,761**	$ 2,336
Net cash used in investing activities (1)	**(694)**	(686)	**(1,102)**	(1,167)
Free cash flow	**$ 811**	$ 585	**$ 1,659**	$ 1,169

(1) As a result of the retrospective adoption of Accounting Standards Update 2016-18 in the first quarter of 2017, changes in restricted cash and cash equivalents are no longer classified as investing activities within the Consolidated Statements of Cash Flows and are no longer included as an adjustment in the Company's definition of free cash flow. There is no impact to free cash flow resulting from this reclassification.

Adjusted debt-to-adjusted EBITDA multiple

Management believes that the adjusted debt-to-adjusted earnings before interest, income taxes, depreciation and amortization (EBITDA) multiple is a useful credit measure because it reflects the Company's ability to service its debt and other long term obligations. The Company calculates the adjusted debt-to-adjusted EBITDA multiple as adjusted debt divided by adjusted EBITDA. These measures do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

The following table provides a reconciliation of debt and net income to the adjusted measures presented below, which have been used to calculate the adjusted debt-to-adjusted EBITDA multiple:

In millions, unless otherwise indicated	*As at and for the twelve months ended June 30,*	**2017**	2016
Debt		**$ 10,557**	$ 10,322
Adjustment: Present value of operating lease commitments [1]		**488**	561
Adjusted debt		**$ 11,045**	$ 10,883
Net income		**$ 3,905**	$ 3,598
Interest expense		**486**	469
Income tax expense		**1,303**	1,315
Depreciation and amortization		**1,271**	1,180
EBITDA		**6,965**	6,562
Adjustments:			
Other income		**(94)**	(31)
Deemed interest on operating leases		**22**	27
Adjusted EBITDA		**$ 6,893**	$ 6,558
Adjusted debt-to-adjusted EBITDA multiple *(times)*		**1.60**	1.66

(1) The operating lease commitments have been discounted using the Company's implicit interest rate for each of the periods presented.

Consolidated Statements of Income – unaudited

In millions, except per share data	Three months ended June 30		Six months ended June 30	
	2017	2016	**2017**	2016
Revenues	**$ 3,329**	$ 2,842	**$ 6,535**	$ 5,806
Operating expenses				
Labor and fringe benefits	**527**	469	**1,107**	1,059
Purchased services and material	**432**	377	**872**	785
Fuel	**329**	243	**671**	478
Depreciation and amortization	**326**	296	**649**	603
Equipment rents	**103**	92	**204**	187
Casualty and other	**117**	72	**234**	184
Total operating expenses	**1,834**	1,549	**3,737**	3,296
Operating income	**1,495**	1,293	**2,798**	2,510
Interest expense	**(123)**	(116)	**(245)**	(239)
Other income (loss)	**1**	(1)	**3**	4
Income before income taxes	**1,373**	1,176	**2,556**	2,275
Income tax expense *(Note 3)*	**(342)**	(318)	**(641)**	(625)
Net income	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Earnings per share *(Note 4)*				
Basic	**$ 1.36**	$ 1.10	**$ 2.52**	$ 2.11
Diluted	**$ 1.36**	$ 1.10	**$ 2.51**	$ 2.10
Weighted-average number of shares *(Note 4)*				
Basic	**756.1**	778.9	**758.7**	782.5
Diluted	**759.7**	782.0	**762.1**	785.6
Dividends declared per share	**$ 0.4125**	$ 0.3750	**$ 0.8250**	$ 0.7500

See accompanying notes to unaudited consolidated financial statements.

Consolidated Statements of Comprehensive Income – unaudited

In millions	Three months ended June 30		Six months ended June 30	
	2017	2016	**2017**	2016
Net income	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Other comprehensive income (loss) *(Note 8)*				
Net loss on foreign currency translation	**(66)**	(10)	**(89)**	(135)
Net change in pension and other postretirement benefit plans *(Note 6)*	**45**	39	**91**	88
Other comprehensive income (loss) before income taxes	**(21)**	29	**2**	(47)
Income tax expense	**(38)**	(17)	**(60)**	(99)
Other comprehensive income (loss)	**(59)**	12	**(58)**	(146)
Comprehensive income	**$ 972**	$ 870	**$ 1,857**	$ 1,504

See accompanying notes to unaudited consolidated financial statements.

Consolidated Balance Sheets – unaudited

In millions		June 30 2017		December 31 2016
Assets				
Current assets				
Cash and cash equivalents	$	**131**	$	176
Restricted cash and cash equivalents *(Note 5)*		**461**		496
Accounts receivable		**899**		875
Material and supplies		**453**		363
Other current assets		**213**		197
Total current assets		**2,157**		2,107
Properties		**33,656**		33,755
Pension asset		**1,160**		907
Intangible and other assets		**272**		288
Total assets	$	**37,245**	$	37,057
Liabilities and shareholders' equity				
Current liabilities				
Accounts payable and other	$	**1,733**	$	1,519
Current portion of long-term debt		**1,815**		1,489
Total current liabilities		**3,548**		3,008
Deferred income taxes		**8,630**		8,473
Other liabilities and deferred credits		**589**		593
Pension and other postretirement benefits		**685**		694
Long-term debt		**8,742**		9,448
Shareholders' equity				
Common shares		**3,785**		3,730
Common shares in Share Trusts *(Note 5)*		**(113)**		(137)
Additional paid-in capital		**222**		364
Accumulated other comprehensive loss *(Note 8)*		**(2,416)**		(2,358)
Retained earnings		**13,573**		13,242
Total shareholders' equity		**15,051**		14,841
Total liabilities and shareholders' equity	$	**37,245**	$	37,057

See accompanying notes to unaudited consolidated financial statements.

Consolidated Statements of Changes in Shareholders' Equity – unaudited

In millions	Number of common shares Outstanding	Number of common shares Share Trusts	Common shares	Common shares in Share Trusts	Additional paid-in capital	Accumulated other comprehensive loss	Retained earnings	Total shareholders' equity
Balance at December 31, 2016	762.0	1.8	$ 3,730	$ (137)	$ 364	$ (2,358)	$ 13,242	$ 14,841
Net income							1,915	1,915
Stock options exercised	0.5		31		(5)			26
Settlement of equity settled awards			77		(149)			(72)
Stock-based compensation expense					36		(2)	34
Share repurchase program *(Note 5)*	(10.6)		(53)				(959)	(1,012)
Share settlements by Share Trusts *(Note 5)*	0.3	(0.3)		24	(24)			-
Other comprehensive loss *(Note 8)*						(58)		(58)
Dividends							(623)	(623)
Balance at June 30, 2017	**752.2**	**1.5**	**$ 3,785**	**$ (113)**	**$ 222**	**$ (2,416)**	**$ 13,573**	**$ 15,051**

In millions	Number of common shares Outstanding	Number of common shares Share Trusts	Common shares	Common shares in Share Trusts	Additional paid-in capital	Accumulated other comprehensive loss	Retained earnings	Total shareholders' equity
Balance at December 31, 2015	787.2	1.4	$ 3,705	$ (100)	$ 475	$ (1,767)	$ 12,637	$ 14,950
Net income							1,650	1,650
Stock options exercised	0.4		18		(3)			15
Settlement of equity settled awards			68		(114)			(46)
Stock-based compensation expense					30		(3)	27
Share repurchase program *(Note 5)*	(14.6)		(69)				(984)	(1,053)
Share settlements by Share Trusts *(Note 5)*	0.3	(0.3)		23	(23)			-
Other comprehensive loss *(Note 8)*						(146)		(146)
Dividends							(584)	(584)
Balance at June 30, 2016	773.3	1.1	$ 3,722	$ (77)	$ 365	$ (1,913)	$ 12,716	$ 14,813

See accompanying notes to unaudited consolidated financial statements.

Consolidated Statements of Cash Flows – unaudited

	Three months ended June 30		Six months ended June 30	
In millions	**2017**	2016	**2017**	2016
Operating activities				
Net income	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Adjustments to reconcile net income to net cash provided by operating activities:				
Depreciation and amortization	**326**	296	**649**	603
Deferred income taxes	**134**	171	**279**	326
Changes in operating assets and liabilities:				
Accounts receivable	**(6)**	66	**(37)**	39
Material and supplies	**(44)**	(6)	**(94)**	(92)
Accounts payable and other	**102**	(73)	**241**	(81)
Other current assets	**4**	24	**(67)**	18
Pensions and other, net	**(42)**	(65)	**(125)**	(127)
Net cash provided by operating activities	**1,505**	1,271	**2,761**	2,336
Investing activities				
Property additions	**(675)**	(670)	**(1,071)**	(1,139)
Other, net	**(19)**	(16)	**(31)**	(28)
Net cash used in investing activities	**(694)**	(686)	**(1,102)**	(1,167)
Financing activities				
Issuance of debt *(Note 5)*	**-**	-	**-**	677
Repayment of debt	**(29)**	(387)	**(39)**	(498)
Net issuance (repayment) of commercial paper	**(112)**	622	**(23)**	322
Settlement of foreign exchange forward contracts on long-term debt	**7**	(23)	**4**	(24)
Issuance of common shares for stock options exercised	**13**	4	**26**	15
Withholding taxes remitted on the net settlement of equity settled awards *(Note 7)*	**-**	(11)	**(52)**	(36)
Repurchase of common shares *(Note 5)*	**(505)**	(532)	**(1,004)**	(1,044)
Purchase of common shares for settlement of equity settled awards	**(1)**	(10)	**(20)**	(10)
Dividends paid	**(310)**	(291)	**(623)**	(584)
Net cash used in financing activities	**(937)**	(628)	**(1,731)**	(1,182)
Effect of foreign exchange fluctuations on US dollar-denominated cash, cash equivalents, restricted cash, and restricted cash equivalents	**(6)**	3	**(8)**	7
Net decrease in cash, cash equivalents, restricted cash, and restricted cash equivalents (1)	**(132)**	(40)	**(80)**	(6)
Cash, cash equivalents, restricted cash, and restricted cash equivalents, beginning of period (1)	**724**	710	**672**	676
Cash, cash equivalents, restricted cash, and restricted cash equivalents, end of period (1)	**$ 592**	$ 670	**$ 592**	$ 670
Cash and cash equivalents, end of period	**131**	160	**131**	160
Restricted cash and cash equivalents, end of period	**461**	510	**461**	510
Cash, cash equivalents, restricted cash, and restricted cash equivalents, end of period (1)	**$ 592**	$ 670	**$ 592**	$ 670
Supplemental cash flow information				
Interest paid	**$ (110)**	$ (119)	**$ (244)**	$ (236)
Income taxes paid	**$ (169)**	$ (162)	**$ (333)**	$ (398)

(1) The Company adopted Accounting Standards Update 2016-18 in the first quarter of 2017 on a retrospective basis. Comparative balances have been reclassified to conform to the current presentation. See Note 2 – Recent accounting pronouncements for additional information.

See accompanying notes to unaudited consolidated financial statements.

1 – Basis of presentation

In these notes, the word "Company" or "CN" means, Canadian National Railway Company and, as the context requires, its wholly-owned subsidiaries.

The accompanying unaudited Interim Consolidated Financial Statements, expressed in Canadian dollars, have been prepared in accordance with United States generally accepted accounting principles (GAAP) for interim financial statements. Accordingly, they do not include all of the disclosures required by GAAP for complete financial statements. In management's opinion, all adjustments (consisting of normal recurring accruals) considered necessary for fair presentation have been included. Interim operating results are not necessarily indicative of the expected results for the full year.

These unaudited Interim Consolidated Financial Statements have been prepared using accounting policies consistent with those used in preparing CN's 2016 Annual Consolidated Financial Statements, except as disclosed in *Note 2 – Recent accounting pronouncements*, and should be read in conjunction with such statements and Notes thereto.

2 – Recent accounting pronouncements

The following recent Accounting Standards Update (ASU) issued by the Financial Accounting Standards Board (FASB) was adopted by the Company during the current period:

Standard	Description	Impact
ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash	Requires that a Statement of Cash Flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents.	The Company elected to early adopt the amendments of this ASU in the first quarter of 2017 on a retrospective basis. As a result of the adoption of this ASU, changes in restricted cash and cash equivalents are no longer classified as investing activities, and the Consolidated Statement of Cash Flows now explains the change during the period in the total of cash, cash equivalents, restricted cash, and restricted cash equivalents.

The following recent ASUs issued by FASB have an effective date after June 30, 2017 and have not been adopted by the Company:

Standard (1)	Description	Impact	Effective date (2)
ASU 2017-07 Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	Requires employers that sponsor defined benefit pension plans and/or other postretirement benefit plans to report the service cost component in the same line item or items as other compensation costs. The other components of net periodic benefit cost are required to be presented in the Statement of Income separately from the service cost component and outside a subtotal of income from operations. The new guidance allows only the service cost component to be eligible for capitalization. The guidance must be applied retrospectively for the presentation of the service cost component and other components of net periodic benefit cost in the Statement of Income and prospectively for the capitalization of the service cost component of net periodic benefit cost.	The amendments will affect the classification of the components of pension and postretirement benefit costs other than service cost which will be shown outside of income from operations in a separate caption in the Company's Consolidated Statements of Income. Had the ASU been applicable for the three and six months ended June 30, 2017, Operating income would have been reduced by approximately \$80 million and \$159 million, respectively (\$78 million and \$145 million for the three and six months ended June 30, 2016, respectively) with a corresponding increase presented in the new caption below Operating income with no impact on Net income as a result of the reclassification. The guidance allowing only the service cost component to be eligible for capitalization is not expected to have a significant impact on the Company's Consolidated Financial Statements. CN will adopt the requirements of the ASU effective January 1, 2018.	December 15, 2017. Early adoption is permitted.

Standard [1]	Description	Impact	Effective date [2]
ASU 2016-02, Leases (Topic 842)	Requires the recognition of lease assets and lease liabilities on the Balance Sheet by lessees for most leases. The new standard also requires additional qualitative and quantitative disclosures about leases, significant judgments made in applying requirements, and the amounts recognized in the financial statements relating to leases. Lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using the modified retrospective approach.	The Company is evaluating the effects that the adoption of the ASU will have on its Consolidated Financial Statements and related disclosures, processes and internal controls. The Company is reviewing its lease contracts and expects that the majority of its operating leases with a term over twelve months will be recognized on the Company's Consolidated Balance Sheets. The Company expects that the ASU will have a significant impact on its Consolidated Balance Sheets with the most significant changes relating to the recognition of new right of use assets and lease liabilities for leases currently classified as operating leases. CN expects to adopt the requirements of the ASU effective January 1, 2019.	December 15, 2018. Early adoption is permitted.
ASU 2014-09, Revenue from Contracts with Customers (Topic 606) and related amendments	The basis of the new standard is that an entity recognizes revenue to represent the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additional financial statement presentations and disclosures will be required to assist users of financial statements understand the nature, amount, timing and uncertainty of revenues and cash flows arising from an entity's contracts. The guidance can be applied using either the retrospective or modified retrospective transition method.	The Company continues to make progress towards implementation of the ASU. With respect to freight contracts, in-depth reviews have been completed and the Company has confirmed that freight revenues will continue to be recognized over time based on the transit time of freight as it moves from origin to destination. The Company has also evaluated principal versus agent considerations, including assessing the nature of its promises to customers, and does not expect any significant changes to revenue recognition from this guidance. The Company continues to review freight contracts for terms that could represent additional performance obligations, and evaluate transaction price considerations. The Company is also finalizing its review of non-freight contracts to determine the impact of the ASU on its Consolidated Financial Statements. Additionally, the Company is evaluating the disclosure requirements, and changes to processes and internal controls necessary to meet the reporting and disclosure requirements. Based on the work already performed, the Company does not expect that the ASU will have a material impact on its Consolidated Financial Statements. The Company plans to adopt this ASU using the modified retrospective transition method, effective January 1, 2018.	December 15, 2017. Early adoption is permitted.

(1) Other recently issued ASUs required to be applied for periods beginning on or after June 30, 2017 have been evaluated by the Company and will not have a significant impact on the Company's Consolidated Financial Statements.

(2) Effective for annual and interim reporting periods beginning after the stated date.

3 – Income taxes

The Company recorded income tax expense of $342 million and $641 million for the three and six months ended June 30, 2017, respectively, compared to $318 and $625 million, respectively, for the same periods in 2016.

The six months ended June 30, 2017 figure included deferred income tax recoveries of $18 million recorded in the second quarter and $5 million recorded in the first quarter, both resulting from the enactment of lower provincial corporate income tax rates.

The six months ended June 30, 2016 figure included a deferred income tax expense of $7 million recorded in the second quarter, resulting from the enactment of a higher provincial corporate income tax rate.

4 – Earnings per share

	Three months ended June 30		Six months ended June 30	
In millions, except per share data	**2017**	2016	**2017**	2016
Net income	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Weighted-average basic shares outstanding	**756.1**	778.9	**758.7**	782.5
Dilutive effect of stock-based compensation	**3.6**	3.1	**3.4**	3.1
Weighted-average diluted shares outstanding	**759.7**	782.0	**762.1**	785.6
Basic earnings per share	**$ 1.36**	$ 1.10	**$ 2.52**	$ 2.11
Diluted earnings per share	**$ 1.36**	$ 1.10	**$ 2.51**	$ 2.10
Units excluded from the calculation as their inclusion would not have a dilutive effect:				
Stock options	**0.6**	1.6	**0.8**	1.6
Performance share units	**-**	0.4	**0.1**	0.4

5 – Financing activities

Revolving credit facility

The Company has an unsecured revolving credit facility with a consortium of lenders which is available for general corporate purposes including backstopping the Company's commercial paper programs. On March 15, 2017, the Company's revolving credit facility agreement was amended to extend the term of the credit facility by one year. The credit facility of $1.3 billion consists of a tranche for $420 million maturing on May 5, 2020 and a tranche for $880 million maturing on May 5, 2022. The credit facility agreement allows for an increase in the credit facility amount, up to a maximum of $1.8 billion, as well as the option to extend the term by an additional year at each anniversary date, subject to the consent of individual lenders. The agreement contains customary terms and conditions, which were substantially unchanged by the amendment. The credit facility provides for borrowings at various interest rates, including the Canadian prime rate, bankers' acceptance rates, the U.S. federal funds effective rate and the London Interbank Offered Rate (LIBOR), plus applicable margins, based on CN's debt credit ratings. The credit facility agreement has one financial covenant, which limits debt as a percentage of total capitalization, and with which the Company is in compliance.

As at June 30, 2017 and December 31, 2016, the Company had no outstanding borrowings under its revolving credit facility and there were no draws during the six months ended June 30, 2017.

Commercial paper

The Company has a commercial paper program in Canada and in the U.S. Both programs are backstopped by the Company's revolving credit facility, enabling it to issue commercial paper up to a maximum aggregate principal amount of $1.3 billion, or the US dollar equivalent, on a combined basis.

As at June 30, 2017 and December 31, 2016, the Company had total commercial paper borrowings of US$435 million ($564 million) and US$451 million ($605 million), respectively, at a weighted-average interest rate of 1.04% and 0.65%, respectively, presented in Current portion of long-term debt on the Consolidated Balance Sheets.

Accounts receivable securitization program

The Company has an agreement, expiring on February 1, 2019, to sell an undivided co-ownership interest in a revolving pool of accounts receivable to unrelated trusts for maximum cash proceeds of $450 million. As at June 30, 2017 and December 31, 2016, the Company had no proceeds received under the accounts receivable securitization program.

Bilateral letter of credit facilities

The Company has a series of committed and uncommitted bilateral letter of credit facility agreements. On March 15, 2017, the Company extended the maturity date of the committed bilateral letter of credit facility agreements to April 28, 2020. The agreements are held with various banks to support the Company's requirements to post letters of credit in the ordinary course of business. Under the agreements, the Company has the option from time to time to pledge collateral in the form of cash or cash equivalents, for a minimum term of one month, equal to at least the face value of the letters of credit issued.

As at June 30, 2017, the Company had outstanding letters of credit of $380 million ($451 million as at December 31, 2016) under the committed facilities from a total available amount of $441 million ($508 million as at December 31, 2016) and $124 million ($68 million as at December 31, 2016) under the uncommitted facilities.

As at June 30, 2017, included in Restricted cash and cash equivalents was $391 million ($426 million as at December 31, 2016) and $68 million ($68 million as at December 31, 2016) which were pledged as collateral under the committed and uncommitted bilateral letter of credit facilities, respectively.

Share repurchase program

The Company may repurchase shares pursuant to a Normal Course Issuer Bid (NCIB) at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange. Under its current NCIB, the Company may repurchase up to 33.0 million common shares between October 30, 2016 and October 29, 2017. As at June 30, 2017, the Company had repurchased 14.1 million common shares for $1,305 million under its current program.

The following table provides the information related to the share repurchase program for the three and six months ended June 30, 2017 and 2016:

	Three months ended June 30		Six months ended June 30	
In millions, except per share data	**2017**	2016	**2017**	2016
Number of common shares repurchased (1)	**5.2**	7.2	**10.6**	14.6
Weighted-average price per share (2)	**$ 99.38**	$ 73.80	**$ 94.98**	$ 72.20
Amount of repurchase (3)	**$ 521**	$ 533	**$ 1,012**	$ 1,053

(1) Includes repurchases of common shares pursuant to private agreements between the Company and arm's length third-party sellers.

(2) Includes brokerage fees where applicable.

(3) Includes settlements in subsequent periods.

Share Trusts

The Company's Employee Benefit Plan Trusts ("Share Trusts") purchase common shares on the open market, which are used to deliver common shares under the Share Units Plan (see *Note 7 – Stock-based compensation*). For the six months ended June 30, 2017 and 2016, there were no purchases of common shares by the Share Trusts. For the six months ended June 30, 2017, the Share Trusts disbursed 0.3 million common shares, which had a historical cost of $24 million, representing a weighted-average price per share of $77.99, for settlement under the Share Units Plan. For the six months ended June 30, 2016, the Share Trusts disbursed 0.3 million common shares, which had a historical cost of $23 million, representing a weighted-average price per share of $73.31, for settlement under the Share Units Plan. Additional information relating to the share purchases by Share Trusts is provided in *Note 13 – Share capital* to the Company's 2016 Annual Consolidated Financial Statements.

6 – Pensions and other postretirement benefits

The Company has various retirement benefit plans under which substantially all of its employees are entitled to benefits at retirement age, generally based on compensation and length of service and/or contributions. Additional information relating to the retirement benefit plans is provided in *Note 12 – Pensions and other postretirement benefits* to the Company's 2016 Annual Consolidated Financial Statements.

The following table provides the components of net periodic benefit cost (income) for defined benefit pension and other postretirement benefit (OPEB) plans for the three and six months ended June 30, 2017 and 2016:

	Three months ended June 30				Six months ended June 30			
	Pensions		OPEB		Pensions		OPEB	
In millions	**2017**	2016	**2017**	2016	**2017**	2016	**2017**	2016
Current service cost	**$ 33**	$ 30	**$ -**	$ -	**$ 67**	$ 65	**$ 1**	$ 1
Interest cost	**134**	136	**3**	2	**269**	272	**5**	4
Expected return on plan assets	**(262)**	(255)	**-**	-	**(524)**	(509)	**-**	-
Amortization of prior service cost	**1**	1	**-**	1	**2**	2	**-**	1
Amortization of net actuarial loss (gain)	**45**	39	**(1)**	(2)	**91**	88	**(2)**	(3)
Net periodic benefit cost (income) (1)	**$ (49)**	$ (49)	**$ 2**	$ 1	**$ (95)**	$ (82)	**$ 4**	$ 3

(1) In the second quarter of 2017 and 2016, the Company revised its estimate of full year Net periodic benefit cost (income) for pensions to reflect updated plan demographic information.

Pension contributions

Pension contributions for the six months ended June 30, 2017 and 2016 of $76 million and $88 million, respectively, primarily represent contributions to the Company's main pension plan, the CN Pension Plan, for the current service cost as determined under the Company's current actuarial valuations for funding purposes. In 2017, the Company expects to make total cash contributions of approximately $115 million for all of the Company's pension plans.

7 – Stock-based compensation

The Company has various stock-based compensation plans for eligible employees. A description of the major plans is provided in *Note 14 – Stock-based compensation* to the Company's 2016 Annual Consolidated Financial Statements.

	Three months ended June 30		Six months ended June 30	
In millions	**2017**	2016	**2017**	2016
Share Units Plan (1)				
Equity settled awards	**$ 11**	$ 9	**$ 20**	$ 20
Cash settled awards	**-**	1	**1**	4
Total Share Units Plan expense	**$ 11**	$ 10	**$ 21**	$ 24
Voluntary Incentive Deferral Plan (VIDP) (2)				
Cash settled awards	**$ 3**	$ (2)	**$ 6**	$ 1
Total VIDP expense (recovery)	**$ 3**	$ (2)	**$ 6**	$ 1
Stock option awards	**$ 4**	$ 2	**$ 7**	$ 5
Total stock-based compensation expense	**$ 18**	$ 10	**$ 34**	$ 30
Tax benefit recognized in income	**$ 4**	$ 3	**$ 8**	$ 7
Excess tax benefit recognized in income	**$ 2**	$ 2	**$ 11**	$ 2

(1) Performance share unit (PSU) awards are granted under the Share Units Plan.

(2) Deferred share unit (DSU) awards are granted under the Voluntary Incentive Deferral Plan.

Share Units Plan

	Equity settled				Cash settled
	PSUs-ROIC (1)		PSUs-TSR (2)		PSUs-ROIC (3)
	Units	Weighted-average grant date fair value	Units	Weighted-average grant date fair value	Units
	In millions		*In millions*		*In millions*
Outstanding at December 31, 2016	1.3	$ 49.82	0.3	$ 103.93	0.4
Granted	0.4	$ 53.19	0.1	$ 103.37	-
Settled (4) (5)	(0.4)	$ 66.84	-	N/A	(0.4)
Forfeited	(0.1)	$ 36.77	-	$ 96.51	-
Outstanding at June 30, 2017	**1.2**	**$ 46.30**	**0.4**	**$ 104.31**	**-**

(1) The grant date fair value of equity settled PSUs-ROIC granted in 2017 of $22 million is calculated using a lattice-based valuation model. As at June 30, 2017, total unrecognized compensation cost related to nonvested equity settled PSUs-ROIC outstanding was $26 million and is expected to be recognized over a weighted-average period of 1.7 years.

(2) The grant date fair value of equity settled PSUs-TSR granted in 2017 of $14 million is calculated using a Monte Carlo simulation model. As at June 30, 2017, total unrecognized compensation cost related to nonvested equity settled PSUs-TSR outstanding was $16 million and is expected to be recognized over a weighted-average period of 1.8 years.

(3) As at June 30, 2017, the liability for cash settled PSUs-ROIC was $nil ($45 million as at December 31, 2016).

(4) Equity settled PSUs-ROIC granted in 2014 met the minimum share price condition for settlement and attained a performance vesting factor of 150%. In the first quarter of 2017, these awards were settled, net of the remittance of the participants' withholding tax obligation of $30 million, by way of disbursement from the Share Trusts of 0.3 million common shares.

(5) Cash settled PSUs-ROIC granted in 2014 met the minimum share price condition for payout and attained a performance vesting factor of 150%. In the first quarter of 2017, the Company paid out $46 million for these awards.

Voluntary Incentive Deferral Plan

	Equity settled		Cash settled
	DSUs (1)		DSUs (2)
	Units	Weighted-average grant date fair value	Units
	In millions		*In millions*
Outstanding at December 31, 2016	1.5	$ 76.54	0.3
Granted	0.1	$ 93.85	-
Settled (3)	(0.5)	$ 76.54	-
Outstanding at June 30, 2017 (4)	**1.1**	**$ 77.49**	**0.3**

(1) The grant date fair value of equity settled DSUs granted in 2017 of $4 million is calculated using the Company's stock price on the grant date. As at June 30, 2017, the aggregate intrinsic value of equity settled DSUs outstanding amounted to $116 million.

(2) The fair value as at June 30, 2017 of cash settled DSUs is based on the intrinsic value. As at June 30, 2017, the liability for cash settled DSUs was $33 million ($35 million as at December 31, 2016). The closing stock price used to determine the liability was $105.22.

(3) For the six months ended June 30, 2017, the Company purchased 0.2 million common shares for the settlement of equity settled DSUs, net of the remittance of the participants' withholding tax obligation of $22 million.

(4) The number of units outstanding that were nonvested, unrecognized compensation cost and the remaining recognition period for cash and equity settled DSUs have not been quantified as they relate to a minimal number of units.

Stock option awards

	Options outstanding		
	Number of options	Weighted-average exercise price	
	In millions		
Outstanding at December 31, 2016 (1)	5.3	$	61.07
Granted (2)	0.9	$	91.94
Exercised	(0.5)	$	50.09
Outstanding at June 30, 2017 (1) (2) (3)	**5.7**	**$**	**65.81**
Exercisable at June 30, 2017 (1) (3)	**3.3**	**$**	**54.48**

(1) Stock options with a US dollar exercise price have been translated into Canadian dollars using the foreign exchange rate in effect at the balance sheet date.

(2) The grant date fair value of options granted in 2017 of $13 million ($14.37 per option) is calculated using the Black-Scholes option-pricing model. As at June 30, 2017, total unrecognized compensation cost related to nonvested options outstanding was $14 million and is expected to be recognized over a weighted-average period of 1.7 years.

(3) As at June 30, 2017, all stock options were in-the-money. The weighted-average term to expiration of options outstanding was 6.7 years and the weighted-average term to expiration of exercisable stock options was 5.2 years. As at June 30, 2017, the aggregate intrinsic value of in-the-money stock options outstanding amounted to $224 million and the aggregate intrinsic value of stock options exercisable amounted to $166 million.

8 – Accumulated other comprehensive loss

In millions		Foreign currency translation adjustments		Pension and other postretirement benefit plans		Derivative instruments		Total before tax		Income tax recovery (expense)		Total net of tax
Balance at March 31, 2017	$	(277)	$	(2,852)	$	7	$	(3,122)	$	765	$	(2,357)
Other comprehensive income (loss) before reclassifications:												
Foreign exchange loss on translation of net investment in foreign operations		(262)						(262)		-		(262)
Foreign exchange gain on translation of US dollar-denominated debt designated as a hedge of the net investment in U.S. subsidiaries (1)		196						196		(27)		169
Amounts reclassified from Accumulated other comprehensive loss:												
Amortization of net actuarial loss				44				44 (2)		(11) (3)		33
Amortization of prior service cost				1				1 (2)		-		1
Other comprehensive income (loss)		(66)		45		-		(21)		(38)		(59)
Balance at June 30, 2017	**$**	**(343)**	**$**	**(2,807)**	**$**	**7**	**$**	**(3,143)**	**$**	**727**	**$**	**(2,416)**

In millions		Foreign currency translation adjustments		Pension and other postretirement benefit plans		Derivative instruments		Total before tax		Income tax recovery (expense)		Total net of tax
Balance at December 31, 2016	$	(254)	$	(2,898)	$	7	$	(3,145)	$	787	$	(2,358)
Other comprehensive income (loss) before reclassifications:												
Foreign exchange loss on translation of net investment in foreign operations		(361)						(361)		-		(361)
Foreign exchange gain on translation of US dollar-denominated debt designated as a hedge of the net investment in U.S. subsidiaries (1)		272						272		(37)		235
Amounts reclassified from Accumulated other comprehensive loss:												
Amortization of net actuarial loss				89				89 (2)		(23) (3)		66
Amortization of prior service cost				2				2 (2)		-		2
Other comprehensive income (loss)		(89)		91		-		2		(60)		(58)
Balance at June 30, 2017	**$**	**(343)**	**$**	**(2,807)**	**$**	**7**	**$**	**(3,143)**	**$**	**727**	**$**	**(2,416)**

(1) The Company designates US dollar-denominated debt of the parent company as a foreign currency hedge of its net investment in U.S. subsidiaries. As a result, from the dates of designation, foreign exchange gains and losses on translation of the Company's US dollar-denominated debt are recorded in Accumulated other comprehensive loss, which minimizes volatility of earnings resulting from the conversion of US dollar-denominated debt into Canadian dollars.

(2) Reclassified to Labor and fringe benefits in the Consolidated Statements of Income and included in components of net periodic benefit cost. See Note 6 - Pensions and other postretirement benefits.

(3) Included in Income tax expense in the Consolidated Statements of Income.

In millions		Foreign currency translation adjustments		Pension and other postretirement benefit plans		Derivative instruments		Total before tax		Income tax recovery (expense)		Total net of tax
Balance at March 31, 2016	$	(334)	$	(2,155)	$	7	$	(2,482)	$	557	$	(1,925)
Other comprehensive income (loss) before reclassifications:												
Foreign exchange loss on translation of net investment in foreign operations		(53)						(53)		-		(53)
Foreign exchange gain on translation of US dollar-denominated debt designated as a hedge of the net investment in U.S. subsidiaries (1)		43						43		(6)		37
Amounts reclassified from Accumulated other comprehensive loss:												
Amortization of net actuarial loss				37				37 (2)		(10) (3)		27
Amortization of prior service cost				2				2 (2)		(1) (3)		1
Other comprehensive income (loss)		(10)		39		-		29		(17)		12
Balance at June 30, 2016	$	(344)	$	(2,116)	$	7	$	(2,453)	$	540	$	(1,913)

In millions		Foreign currency translation adjustments		Pension and other postretirement benefit plans		Derivative instruments		Total before tax		Income tax recovery (expense)		Total net of tax
Balance at December 31, 2015	$	(209)	$	(2,204)	$	7	$	(2,406)	$	639	$	(1,767)
Other comprehensive income (loss) before reclassifications:												
Foreign exchange loss on translation of net investment in foreign operations		(693)						(693)		-		(693)
Foreign exchange gain on translation of US dollar-denominated debt designated as a hedge of the net investment in U.S. subsidiaries (1)		558						558		(75)		483
Amounts reclassified from Accumulated other comprehensive loss:												
Amortization of net actuarial loss				85				85 (2)		(23) (3)		62
Amortization of prior service cost				3				3 (2)		(1) (3)		2
Other comprehensive income (loss)		(135)		88		-		(47)		(99)		(146)
Balance at June 30, 2016	$	(344)	$	(2,116)	$	7	$	(2,453)	$	540	$	(1,913)

(1) The Company designates US dollar-denominated debt of the parent company as a foreign currency hedge of its net investment in U.S. subsidiaries. As a result, from the dates of designation, foreign exchange gains and losses on translation of the Company's US dollar-denominated debt are recorded in Accumulated other comprehensive loss, which minimizes volatility of earnings resulting from the conversion of US dollar-denominated debt into Canadian dollars.

(2) Reclassified to Labor and fringe benefits in the Consolidated Statements of Income and included in components of net periodic benefit cost. See Note 6 - Pensions and other postretirement benefits.

(3) Included in Income tax expense in the Consolidated Statements of Income.

9 – Major commitments and contingencies

Purchase commitments

As at June 30, 2017, the Company had commitments to purchase wheels, railroad ties, rail, fuel, and other equipment and services, as well as outstanding information technology service contracts and licenses, at an aggregate cost of $1,478 million.

Contingencies

In the normal course of business, the Company becomes involved in various legal actions seeking compensatory and occasionally punitive damages, including actions brought on behalf of various purported classes of claimants and claims relating to employee and third-party personal injuries, occupational disease and property damage, arising out of harm to individuals or property allegedly caused by, but not limited to, derailments or other accidents.

As at June 30, 2017, the Company had aggregate reserves for personal injury and other claims of $299 million, of which $78 million was recorded as a current liability ($301 million as at December 31, 2016, of which $76 million was recorded as a current liability).

Although the Company considers such provisions to be adequate for all its outstanding and pending claims, the final outcome with respect to actions outstanding or pending as at June 30, 2017, or with respect to future claims, cannot be reasonably determined. When establishing provisions for contingent liabilities the Company considers, where a probable loss estimate cannot be made with reasonable certainty, a range of potential probable losses for each such matter, and records the amount it considers the most reasonable estimate within the range. However, when no amount within the range is a better estimate than any other amount, the minimum amount in the range is accrued. For matters where a loss is reasonably possible but not probable, a range of potential losses cannot be estimated due to various factors which may include the limited availability of facts, the lack of demand for specific damages and the fact that proceedings were at an early stage. Based on information currently available, the Company believes that the eventual outcome of the actions against the Company will not, individually or in the aggregate, have a material adverse effect on the Company's financial position. However, due to the inherent inability to predict with certainty unforeseeable future developments, there can be no assurance that the ultimate resolution of these actions will not have a material adverse effect on the Company's results of operations, financial position or liquidity.

Environmental matters

The Company's operations are subject to numerous federal, provincial, state, municipal and local environmental laws and regulations in Canada and the U.S. concerning, among other things, emissions into the air; discharges into waters; the generation, handling, storage, transportation, treatment and disposal of waste, hazardous substances, and other materials; decommissioning of underground and aboveground storage tanks; and soil and groundwater contamination. A risk of environmental liability is inherent in railroad and related transportation operations; real estate ownership, operation or control; and other commercial activities of the Company with respect to both current and past operations.

The Company has identified approximately 165 sites at which it is or may be liable for remediation costs, in some cases along with other potentially responsible parties, associated with alleged contamination and is subject to environmental clean-up and enforcement actions, including those imposed by the United States Federal *Comprehensive Environmental Response, Compensation and Liability Act* of 1980 (CERCLA), also known as the Superfund law, or analogous state laws. CERCLA and similar state laws, in addition to other similar Canadian and U.S. laws, generally impose joint and several liability for clean-up and enforcement costs on current and former owners and operators of a site, as well as those whose waste is disposed of at the site, without regard to fault or the legality of the original conduct. The Company has been notified that it is a potentially responsible party for study and clean-up costs at 6 sites governed by the Superfund law (and analogous state laws) for which investigation and remediation payments are or will be made or are yet to be determined and, in many instances, is one of several potentially responsible parties.

The ultimate cost of addressing these known contaminated sites cannot be definitively established given that the estimated environmental liability for any given site may vary depending on the nature and extent of the contamination; the nature of anticipated response actions, taking into account the available clean-up techniques; evolving regulatory standards governing environmental liability; and the number of potentially responsible parties and their financial viability. As a result, liabilities are recorded based on the results of a four-phase assessment conducted on a site-by-site basis. A liability is initially recorded when environmental assessments occur, remedial efforts are probable, and when the costs, based on a specific plan of action in terms of the technology to be used and the extent of the corrective action required, can be reasonably estimated. The Company estimates the costs related to a particular site using cost scenarios established by external consultants based on the extent of contamination and expected costs for remedial efforts. In the case of multiple parties, the Company accrues its allocable share of liability taking into account the Company's alleged responsibility, the number of potentially responsible parties and their ability to pay their respective share of the liability. Adjustments to initial estimates are recorded as additional information becomes available.

The Company's provision for specific environmental sites is undiscounted and includes costs for remediation and restoration of sites, as well as monitoring costs. Costs related to any unknown existing or future contamination will be accrued in the period in which they become probable and reasonably estimable.

On June 15, 2017, as part of a plea agreement, the Company agreed to disclose three offences under the Storage Tank Systems for Petroleum Products and Allied Petroleum Products Regulations arising out of the operation of its fueling facilities at the Bissell Yard in Edmonton. The fines related to these three offenses were (a) $250,000 for failing to remove a single-walled underground pipe; (b) $100,000 for failing to keep an up-to-date emergency plan at the location of the tank system; and (c) $150,000 for using a centrifugal pump in connection with an oil water separator.

As at June 30, 2017, the Company had aggregate accruals for environmental costs of $90 million, of which $49 million was recorded as a current liability ($86 million as at December 31, 2016, of which $50 million was recorded as a current liability). The Company anticipates that the majority of the liability at June 30, 2017 will be paid out over the next five years. Based on the information currently available, the Company considers its accruals to be adequate.

Guarantees and indemnifications

A description of the Company's guarantees and indemnifications is provided in *Note 16 – Major commitments and contingencies* to the Company's 2016 Annual Consolidated Financial Statements.

Guarantees

Guarantee of residual values of operating leases

The Company has guaranteed a portion of the residual values of certain of its assets under operating leases with expiry dates between 2017 and 2023, for the benefit of the lessor. If the fair value of the assets at the end of their respective lease term is less than the fair value, as estimated at the inception of the lease, then the Company must, under certain conditions, compensate the lessor for the shortfall. As at June 30, 2017, the maximum exposure in respect of these guarantees was $155 million ($161 million as at December 31, 2016). There are no recourse provisions to recover any amounts from third parties.

Other guarantees

As at June 30, 2017, the Company had outstanding letters of credit of $380 million ($451 million as at December 31, 2016) under the committed bilateral letter of credit facilities and $124 million ($68 million as at December 31, 2016) under the uncommitted bilateral letter of credit facilities, and surety and other bonds of $179 million ($169 million as at December 31, 2016), all issued by financial institutions with investment grade credit ratings to third parties to indemnify them in the event the Company does not perform its contractual obligations.

As at June 30, 2017, the maximum potential liability under these guarantee instruments was $683 million ($688 million as at December 31, 2016), of which $624 million ($629 million as at December 31, 2016) related to other employee benefit liabilities and workers' compensation and $59 million ($59 million as at December 31, 2016) related to other liabilities. The guarantee instruments expire at various dates between 2017 and 2019.

As at June 30, 2017, the Company had not recorded a liability with respect to guarantees and indemnifications as the Company did not expect to make any payments under its guarantees and indemnifications.

10 – Financial instruments

Derivative financial instruments

The Company uses derivative financial instruments from time to time in the management of its foreign currency and interest rate exposures. The Company has limited involvement with derivative financial instruments in the management of its risks and does not hold or issue them for trading or speculative purposes. As at June 30, 2017, the Company had outstanding foreign exchange forward contracts with a notional value of US$1,126 million (US$1,035 million as at December 31, 2016). Changes in the fair value of foreign exchange forward contracts, resulting from changes in foreign exchange rates, are recognized in Other income in the Consolidated Statement of Income as they occur.

For the three and six months ended June 30, 2017, the Company recorded a loss of $26 million and $41 million, respectively, related to foreign exchange forward contracts, compared to a loss of $2 million and $47 million, respectively, for the same periods in 2016. These losses were largely offset by the re-measurement of US dollar-denominated monetary assets and liabilities recorded in Other income.

As at June 30, 2017, Other current assets included an unrealized gain of $nil ($19 million as at December 31, 2016) and Accounts payable and other included an unrealized loss of $32 million ($1 million as at December 31, 2016), related to the fair value of outstanding foreign exchange forward contracts.

Fair value of financial instruments

The following table provides the valuation methods and assumptions used by the Company to estimate the fair value of financial instruments and their associated level within the fair value hierarchy:

Level 1 **Quoted prices for identical instruments in active markets**	The carrying amounts of Cash and cash equivalents and Restricted cash and cash equivalents approximate fair value. These financial instruments include highly liquid investments purchased three months or less from maturity, for which the fair value is determined by reference to quoted prices in active markets.
Level 2 **Significant inputs (other than quoted prices included in Level 1) are observable**	The carrying amounts of Accounts receivable, Other current assets, and Accounts payable and other approximate fair value. The fair value of these financial instruments is not determined using quoted prices, but rather from market observable information. The fair value of derivative financial instruments used to manage the Company's exposure to foreign currency risk and included in Other current assets and Accounts payable and other is measured by discounting future cash flows using a discount rate derived from market data for financial instruments subject to similar risks and maturities. The carrying amount of the Company's debt does not approximate fair value. The fair value is estimated based on quoted market prices for the same or similar debt instruments, as well as discounted cash flows using current interest rates for debt with similar terms, company rating, and remaining maturity. As at June 30, 2017, the Company's debt had a carrying amount of $10,557 million ($10,937 million as at December 31, 2016) and a fair value of $11,793 million ($12,084 million as at December 31, 2016).
Level 3 **Significant inputs are unobservable**	The carrying amounts of investments included in Intangible and other assets approximate fair value, with the exception of certain cost investments for which significant inputs are unobservable and fair value is estimated based on the Company's proportionate share of the underlying net assets. As at June 30, 2017, the Company's investments had a carrying amount of $71 million ($68 million as at December 31, 2016) and a fair value of $222 million ($220 million as at December 31, 2016).

Management's Discussion and Analysis

This Management's Discussion and Analysis (MD&A) dated July 25, 2017, relates to the consolidated financial position and results of operations of Canadian National Railway Company, together with its wholly-owned subsidiaries, collectively "CN" or the "Company," and should be read in conjunction with the Company's 2017 unaudited Interim Consolidated Financial Statements and Notes thereto. It should also be read in conjunction with the Company's 2016 audited Annual Consolidated Financial Statements and Notes thereto, and the 2016 Annual MD&A. All financial information reflected herein is expressed in Canadian dollars and prepared in accordance with United States generally accepted accounting principles (GAAP), unless otherwise noted.

CN's common shares are listed on the Toronto and New York stock exchanges. Additional information about CN filed with Canadian securities regulatory authorities and the United States Securities and Exchange Commission (SEC), including the Company's 2016 Annual Information Form and Form 40-F, may be found online on SEDAR at www.sedar.com, on EDGAR at www.sec.gov, and on the Company's website at www.cn.ca in the Investors section. Printed copies of such documents may be obtained by contacting the Corporate Secretary's Office.

Business profile

CN is engaged in the rail and related transportation business. CN's network, of approximately 20,000 route miles of track, spans Canada and mid-America, uniquely connecting three coasts: the Atlantic, the Pacific and the Gulf of Mexico. CN's extensive network and efficient connections to all Class I railroads provide CN customers access to all three North American Free Trade Agreement (NAFTA) nations. A true backbone of the economy, CN handles over $250 billion worth of goods annually and carries almost 300 million tons of cargo, serving exporters, importers, retailers, farmers and manufacturers.

CN's freight revenues are derived from seven commodity groups representing a diversified and balanced portfolio of goods transported between a wide range of origins and destinations. This product and geographic diversity better positions the Company to face economic fluctuations and enhances its potential for growth opportunities. For the year ended December 31, 2016, no individual commodity group accounted for more than 24% of total revenues and from a geographic standpoint, 17% of revenues relate to United States (U.S.) domestic traffic, 34% transborder traffic, 18% Canadian domestic traffic and 31% overseas traffic. The Company is the originating carrier for over 85%, and the originating and terminating carrier for over 65%, of traffic moving along its network, which allows it both to capitalize on service advantages and build on opportunities to efficiently use assets.

Strategy overview

A description of the Company's strategy is provided in the section entitled *Strategy overview* of the Company's 2016 Annual MD&A.

2017 Second quarter highlights

- CN attained record quarterly revenues, operating income, net income, and earnings per share.
- Net income increased by $173 million, or 20%, to $1,031 million in the second quarter of 2017, with diluted earnings per share rising 24% to $1.36.
- Adjusted net income (1) increased by $148 million, or 17%, to $1,013 million in the second quarter of 2017, with adjusted diluted earnings per share (1) rising 21% to $1.34.
- Operating income was $1,495 million in the second quarter of 2017, an increase of $202 million, or 16%, over the same quarter of 2016.
- CN's operating ratio was 55.1% in the second quarter of 2017, a 0.6-point increase from the second quarter of 2016.
- The Company generated free cash flow (2) of $811 million, a 39% increase over the same quarter in 2016.
- The Company repurchased 5.2 million common shares under its share repurchase program, returning $521 million to its shareholders.
- CN paid a quarterly dividend of $0.4125 per share, representing an increase of 10% when compared to 2016, amounting to $310 million.

(1) See the section of this MD&A entitled Adjusted performance measures for an explanation of these non-GAAP measures.

(2) See the section of this MD&A entitled Liquidity and capital resources – Free cash flow for an explanation of this non-GAAP measure.

2017 Business outlook and assumptions

The Company continues to see growth across a range of commodities, particularly in intermodal traffic, frac sand, Canadian grain, coal exports, and finished vehicles, as well as volume weakness in U.S. thermal coal shipments to domestic markets. The Company now also expects to see growth in volumes of crude oil and petroleum coke, as well as lower volumes for U.S. grain.

Underpinning the 2017 business outlook, the Company assumes that North American industrial production will increase by approximately two percent. For the 2016/2017 crop year, the grain crops in both Canada and the U.S. were above their respective five-year averages. The Company assumes that the 2017/2018 grain crops in both Canada and the U.S. will be in line with their respective five-year averages.

The forward-looking statements discussed in this section are subject to risks and uncertainties that could cause actual results or performance to differ materially from those expressed or implied in such statements and are based on certain factors and assumptions which the Company considers reasonable, about events, developments, prospects and opportunities that may not materialize or that may be offset entirely or partially by other events and developments. In addition to the assumptions and expectations discussed in this section, reference should be made to the section of this MD&A entitled *Forward-looking statements* for assumptions and risk factors affecting such statements.

Forward-looking statements

Certain statements included in this MD&A are "forward-looking statements" within the meaning of the *United States Private Securities Litigation Reform Act of 1995* and under Canadian securities laws. By their nature, forward-looking statements involve risks, uncertainties and assumptions. The Company cautions that its assumptions may not materialize and that current economic conditions render such assumptions, although reasonable at the time they were made, subject to greater uncertainty. Forward-looking statements may be identified by the use of terminology such as "believes," "expects," "anticipates," "assumes," "outlook," "plans," "targets" or other similar words.

Forward-looking statements include, but are not limited to, those set forth in the table below, which also presents key assumptions used in determining the forward-looking statements. See also the section of this MD&A entitled *Strategy overview – 2017 Business outlook and assumptions*.

Forward-looking statements	Key assumptions
Statements relating to revenue growth opportunities, including those referring to general economic and business conditions	• North American and global economic growth • Long-term growth opportunities being less affected by current economic conditions
Statements relating to the Company's ability to meet debt repayments and future obligations in the foreseeable future, including income tax payments, and capital spending	• North American and global economic growth • Adequate credit ratios • Investment-grade credit ratings • Access to capital markets • Adequate cash generated from operations and other sources of financing
Statements relating to pension contributions	• Adequate cash generated from operations and other sources of financing • Adequate long-term return on investment on pension plan assets • Level of funding as determined by actuarial valuations, particularly influenced by discount rates for funding purposes

Forward-looking statements are not guarantees of future performance and involve known and unknown risks, uncertainties and other factors which may cause the actual results or performance of the Company to be materially different from the outlook or any future results or performance implied by such statements. Accordingly, readers are advised not to place undue reliance on forward-looking statements. Important risk factors that could affect the forward-looking statements include, but are not limited to, the effects of general economic and business conditions; industry competition; inflation, currency and interest rate fluctuations; changes in fuel prices; legislative and/or regulatory developments; compliance with environmental laws and regulations; actions by regulators; increases in maintenance and operating costs; security threats; reliance on technology; trade restrictions; transportation of hazardous materials; various events which could disrupt operations, including natural events such as severe weather, droughts, floods and earthquakes; climate change; labor negotiations and disruptions; environmental claims; uncertainties of investigations, proceedings or other types of claims and litigation; risks and liabilities arising from derailments; timing and completion of capital programs; and other risks detailed from time to time in reports filed by CN with securities regulators in Canada and the U.S., including its Annual Information Form and Form 40-F. See the section entitled *Business risks* of this MD&A and the Company's 2016 Annual MD&A for a description of major risk factors.

Forward-looking statements reflect information as of the date on which they are made. CN assumes no obligation to update or revise forward-looking statements to reflect future events, changes in circumstances, or changes in beliefs, unless required by applicable securities laws. In the event CN does update any forward-looking statement, no inference should be made that CN will make additional updates with respect to that statement, related matters, or any other forward-looking statement.

Financial highlights

	Three months ended June 30		Six months ended June 30	
In millions, except percentage and per share data	**2017**	2016	**2017**	2016
Revenues	**$ 3,329**	$ 2,842	**$ 6,535**	$ 5,806
Operating income	**$ 1,495**	$ 1,293	**$ 2,798**	$ 2,510
Net income	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Adjusted net income (1)	**$ 1,013**	$ 865	**$ 1,892**	$ 1,657
Basic earnings per share	**$ 1.36**	$ 1.10	**$ 2.52**	$ 2.11
Adjusted basic earnings per share (1)	**$ 1.34**	$ 1.11	**$ 2.49**	$ 2.12
Diluted earnings per share	**$ 1.36**	$ 1.10	**$ 2.51**	$ 2.10
Adjusted diluted earnings per share (1)	**$ 1.34**	$ 1.11	**$ 2.48**	$ 2.11
Dividends declared per share	**$ 0.4125**	$ 0.3750	**$ 0.8250**	$ 0.7500
Total assets	**$ 37,245**	$ 36,094	**$ 37,245**	$ 36,094
Total long-term liabilities	**$ 18,646**	$ 18,555	**$ 18,646**	$ 18,555
Operating ratio	**55.1%**	54.5%	**57.2%**	56.8%
Free cash flow (2)	**$ 811**	$ 585	**$ 1,659**	$ 1,169

(1) See the section of this MD&A entitled Adjusted performance measures for an explanation of these non-GAAP measures.

(2) See the section of this MD&A entitled Liquidity and capital resources – Free cash flow for an explanation of this non-GAAP measure.

Financial results

Second quarter and first half of 2017 compared to corresponding periods in 2016

Net income for the second quarter of 2017 was $1,031 million, an increase of $173 million, or 20%, when compared to the same period in 2016, with diluted earnings per share rising 24% to $1.36. Net income for the six months ended June 30, 2017 was $1,915 million, an increase of $265 million, or 16%, when compared to the same period in 2016, with diluted earnings per share rising 20% to $2.51.

Operating income for the quarter ended June 30, 2017 increased by $202 million, or 16%, to $1,495 million. Operating income for the six months ended June 30, 2017 increased by $288 million, or 11%, to $2,798 million. The increase in operating income in both periods mainly reflects higher volumes, and for the second quarter, the positive translation impact of a weaker Canadian dollar.

The operating ratio, defined as operating expenses as a percentage of revenues, was 55.1% in the second quarter of 2017, compared to 54.5% in the second quarter of 2016, a 0.6-point increase. The six-month operating ratio was 57.2% in 2017, compared to 56.8% in 2016, a 0.4-point increase.

Revenues for the quarter ended June 30, 2017 totaled $3,329 million compared to $2,842 million in the same period in 2016, an increase of $487 million, or 17%. Revenues for the first half of 2017 were $6,535 million, an increase of $729 million, or 13%, when compared to the same period in 2016. The increases were mainly attributable to higher volumes of Canadian grain and fertilizers, overseas intermodal traffic, frac sand, coal and petroleum coke exports, crude oil, and finished vehicles; higher applicable fuel surcharge rates; and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Operating expenses for the second quarter of 2017 amounted to $1,834 million compared to $1,549 million in the same quarter of 2016, an increase of $285 million, or 18%. Operating expenses for the first half of 2017 amounted to $3,737 million compared to $3,296 million in the same period of 2016, an increase of $441 million, or 13%. The increases were mainly due to higher fuel costs, increased purchased services and material costs, and higher labor and fringe benefits expense resulting from increased volumes, as well as increased casualty and other expense. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Non-GAAP measures

This MD&A makes reference to non-GAAP measures including adjusted performance measures, constant currency, free cash flow, and adjusted debt-to-adjusted EBITDA multiple, that do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies. From management's perspective, these non-GAAP measures are useful measures of performance and provide investors with supplementary information to assess the Company's results of operations and liquidity. These non-GAAP measures should not be considered in isolation or as a substitute for financial measures prepared in accordance with GAAP.

For further details of these non-GAAP measures, including a reconciliation to the most directly comparable GAAP financial measures, refer to the sections entitled *Adjusted performance measures, Constant currency* and *Liquidity and capital resources.*

Adjusted performance measures

Management believes that adjusted net income and adjusted earnings per share are useful measures of performance that can facilitate period-to-period comparisons, as they exclude items that do not necessarily arise as part of CN's normal day-to-day operations and could distort the analysis of trends in business performance. Management uses these measures, which exclude certain income and expense items in its results that management believes are not reflective of CN's underlying business operations, to set performance goals and as a means to measure CN's performance. The exclusion of items in adjusted net income and adjusted earnings per share does not, however, imply that these items are necessarily non-recurring. These measures do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

For the three and six months ended June 30, 2017, the Company reported adjusted net income of $1,013 million, or $1.34 per diluted share, and $1,892 million, or $2.48 per diluted share, respectively. The adjusted figures for the three months ended June 30, 2017 exclude a deferred income tax recovery of $18 million ($0.02 per diluted share), resulting from the enactment of a lower provincial corporate income tax rate. The adjusted figures for the six months ended June 30, 2017 exclude a deferred income tax recovery of $18 million ($0.02 per diluted share) in the second quarter and $5 million ($0.01 per diluted share) in the first quarter, resulting from the enactment of lower provincial corporate income tax rates.

For the three and six months ended June 30, 2016, the Company reported adjusted net income of $865 million, or $1.11 per diluted share, and $1,657 million, or $2.11 per diluted share, respectively, which exclude a deferred income tax expense of $7 million ($0.01 per diluted share) in the second quarter, resulting from the enactment of a higher provincial corporate income tax rate.

The following table provides a reconciliation of net income and earnings per share, as reported for the three and six months ended June 30, 2017 and 2016, to the adjusted performance measures presented herein:

	Three months ended June 30		Six months ended June 30	
In millions, except per share data	**2017**	2016	**2017**	2016
Net income as reported	**$ 1,031**	$ 858	**$ 1,915**	$ 1,650
Adjustment: Income tax expense (recovery)	**(18)**	7	**(23)**	7
Adjusted net income	**$ 1,013**	$ 865	**$ 1,892**	$ 1,657
Basic earnings per share as reported	**$ 1.36**	$ 1.10	**$ 2.52**	$ 2.11
Impact of adjustments, per share	**(0.02)**	0.01	**(0.03)**	0.01
Adjusted basic earnings per share	**$ 1.34**	$ 1.11	**$ 2.49**	$ 2.12
Diluted earnings per share as reported	**$ 1.36**	$ 1.10	**$ 2.51**	$ 2.10
Impact of adjustments, per share	**(0.02)**	0.01	**(0.03)**	0.01
Adjusted diluted earnings per share	**$ 1.34**	$ 1.11	**$ 2.48**	$ 2.11

Constant currency

Financial results at constant currency allow results to be viewed without the impact of fluctuations in foreign currency exchange rates, thereby facilitating period-to-period comparisons in the analysis of trends in business performance. Measures at constant currency are considered non-GAAP measures and do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies. Financial results at constant currency are obtained by translating the current period results denominated in US dollars at the foreign exchange rates of the comparable period in the prior year. The average foreign exchange rates were $1.35 and $1.33 per US$1.00, respectively, for the three and six months ended June 30, 2017, and $1.29 and $1.33 per US$1.00, respectively, for the three and six months ended June 30, 2016.

On a constant currency basis, the Company's net income for the three and six months ended June 30, 2017 would have been lower by $28 million ($0.04 per diluted share) and $6 million ($0.01 per diluted share), respectively.

Revenues

	Three months ended June 30				Six months ended June 30			
In millions, unless otherwise indicated	**2017**	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Rail freight revenues	**$ 3,111**	$ 2,646	18%	15%	**$ 6,186**	$ 5,491	13%	13%
Other revenues	**218**	196	11%	8%	**349**	315	11%	10%
Total revenues	**$ 3,329**	$ 2,842	17%	14%	**$ 6,535**	$ 5,806	13%	12%
Rail freight revenues								
Petroleum and chemicals	**$ 549**	$ 492	12%	8%	**$ 1,133**	$ 1,070	6%	6%
Metals and minerals	**389**	292	33%	29%	**750**	602	25%	24%
Forest products	**464**	439	6%	2%	**911**	901	1%	1%
Coal	**126**	95	33%	29%	**255**	188	36%	36%
Grain and fertilizers	**530**	432	23%	20%	**1,137**	954	19%	19%
Intermodal	**815**	697	17%	15%	**1,557**	1,390	12%	12%
Automotive	**238**	199	20%	16%	**443**	386	15%	15%
Total rail freight revenues	**$ 3,111**	$ 2,646	18%	15%	**$ 6,186**	$ 5,491	13%	13%
Revenue ton miles (RTMs) *(millions)*	**58,789**	49,717	18%	18%	**118,565**	101,973	16%	16%
Rail freight revenue/RTM *(cents)*	**5.29**	5.32	(1%)	(3%)	**5.22**	5.38	(3%)	(3%)

Revenues for the quarter ended June 30, 2017 totaled $3,329 million compared to $2,842 million in the same period in 2016, an increase of $487 million, or 17%. Revenues for the first half of 2017 were $6,535 million, an increase of $729 million, or 13%, when compared to the same period in 2016. The increases were mainly attributable to higher volumes of Canadian grain and fertilizers, overseas intermodal traffic, frac sand, coal and petroleum coke exports, crude oil, and finished vehicles; higher applicable fuel surcharge rates; and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Fuel surcharge revenues increased by $65 million in the second quarter and $105 million in the first half of 2017 when compared to the same periods in 2016, as a result of higher applicable fuel surcharge rates and higher freight volumes.

Revenue ton miles (RTMs), measuring the relative weight and distance of rail freight transported by the Company, increased by 18% in the second quarter and 16% in the first half of 2017 relative to the same periods in 2016.

Rail freight revenue per RTM decreased by 1% in the second quarter and 3% in the first half of 2017 when compared to the same periods in 2016 mainly driven by an increase in the average length of haul; partly offset by higher applicable fuel surcharge rates and freight rate increases. The positive translation impact of a weaker Canadian dollar also partly offset the decrease in the second quarter.

Petroleum and chemicals

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 549**	$ 492	12%	8%	**$ 1,133**	$ 1,070	6%	6%
RTMs *(millions)*	**11,027**	9,575	15%	15%	**22,855**	20,881	9%	9%
Revenue/RTM *(cents)*	**4.98**	5.14	(3%)	(6%)	**4.96**	5.12	(3%)	(3%)

Revenues for this commodity group increased by $57 million, or 12%, in the second quarter and $63 million, or 6%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to higher volumes of crude oil resulting from increased production in the Alberta oil sands, and higher volumes of hydrochloric acid and caustic soda; freight rate increases; and higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter. Partly offsetting the increases in both periods were lower volumes of plastic pellets and condensate.

Revenue per RTM decreased by 3% in both the second quarter and first half of 2017 when compared to the same periods in 2016, mainly due to an increase in the average length of haul; partly offset by freight rate increases and higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also partly offset the decrease in the second quarter.

Metals and minerals

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 389**	$ 292	33%	29%	**$ 750**	$ 602	25%	24%
RTMs *(millions)*	**6,887**	4,751	45%	45%	**13,330**	9,454	41%	41%
Revenue/RTM *(cents)*	**5.65**	6.15	(8%)	(11%)	**5.63**	6.37	(12%)	(12%)

Revenues for this commodity group increased by $97 million, or 33%, in the second quarter and $148 million, or 25%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to a rise in oil and gas drilling activity along with higher frac sand usage per well, which resulted in increased shipments of frac sand and drilling pipe; higher volumes of wind turbine components and iron ore; freight rate increases; as well as higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Revenue per RTM decreased by 8% in the second quarter and 12% in the in the first half of 2017 when compared to the same periods in 2016, mainly due to an increase in the average length of haul and unfavorable changes in traffic mix, partly offset by freight rate increases and higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also partly offset the decrease in the second quarter.

Forest products

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 464**	$ 439	6%	2%	**$ 911**	$ 901	1%	1%
RTMs *(millions)*	**7,789**	7,807	-	-	**15,479**	15,736	(2%)	(2%)
Revenue/RTM *(cents)*	**5.96**	5.62	6%	2%	**5.89**	5.73	3%	2%

Revenues for this commodity group increased by $25 million, or 6%, in the second quarter and $10 million, or 1%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to freight rate increases and higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter. Partly offsetting the increases in both periods were lower volumes of a broad range of forest products.

Revenue per RTM increased by 6% in the second quarter and 3% in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to freight rate increases and higher applicable fuel surcharge rates. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Coal

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 126**	$ 95	33%	29%	**$ 255**	$ 188	36%	36%
RTMs *(millions)*	**3,355**	2,686	25%	25%	**6,957**	4,934	41%	41%
Revenue/RTM *(cents)*	**3.76**	3.54	6%	4%	**3.67**	3.81	(4%)	(4%)

Revenues for this commodity group increased by $31 million, or 33%, in the second quarter and $67 million, or 36%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to increased exports of Canadian petroleum coke due to improved market conditions, higher metallurgical coal exports via west coast ports following the reopening of two mines in British Columbia, increased exports of U.S. thermal coal via the Gulf Coast primarily in the first quarter; and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter. Partly offsetting the increases in both periods were reduced volumes of U.S. domestic thermal coal to U.S. Midwest utilities, mainly due to the loss of a utility customer.

Revenue per RTM increased by 6% in the second quarter and decreased by 4% in the first half of 2017 when compared to the same periods in 2016. The increase in the second quarter was mainly due to favorable changes in traffic mix, freight rate increases, and the positive translation impact of a weaker Canadian dollar; partly offset by a significant increase in the average length of haul. The decrease in the first half was mainly due to a significant increase in the average length of haul, partly offset by favorable changes in traffic mix and freight rate increases.

Grain and fertilizers

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 530**	$ 432	23%	20%	**$ 1,137**	$ 954	19%	19%
RTMs *(millions)*	**13,415**	10,353	30%	30%	**28,902**	22,883	26%	26%
Revenue/RTM *(cents)*	**3.95**	4.17	(5%)	(7%)	**3.93**	4.17	(6%)	(6%)

Revenues for this commodity group increased by $98 million, or 23%, in the second quarter and $183 million, or 19%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to higher volumes of Canadian wheat to North American and export markets, higher export volumes of Canadian canola, barley, and potash driven by strong offshore demand and a strong 2016/2017 Canadian grain crop, and higher volumes of U.S. soybeans and corn mainly in the first quarter; as well as freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Revenue per RTM decreased by 5% in the second quarter and 6% in the first half of 2017 when compared to the same periods in 2016. The decreases were mainly due to a significant increase in the average length of haul; partly offset by freight rate increases. The positive translation impact of a weaker Canadian dollar also partly offset the decrease in the second quarter.

Intermodal

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 815**	$ 697	17%	15%	**$ 1,557**	$ 1,390	12%	12%
RTMs *(millions)*	**15,109**	13,519	12%	12%	**28,813**	26,182	10%	10%
Revenue/RTM *(cents)*	**5.39**	5.16	4%	3%	**5.40**	5.31	2%	2%

Revenues for this commodity group increased by $118 million, or 17%, in the second quarter and $167 million, or 12%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to higher international container traffic via the ports of Vancouver, Prince Rupert, Montreal and Halifax, and increased domestic retail volumes in the consumer and industrial products segments; higher applicable fuel surcharge rates; and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter. Partly offsetting the increases in both periods were lower domestic wholesale volumes.

Revenue per RTM increased by 4% in the second quarter and 2% in the first half of 2017 when compared to the same periods in 2016, mainly due to higher applicable fuel surcharge rates and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Automotive

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 238**	$ 199	20%	16%	**$ 443**	$ 386	15%	15%
RTMs *(millions)*	**1,207**	1,026	18%	18%	**2,229**	1,903	17%	17%
Revenue/RTM *(cents)*	**19.72**	19.40	2%	(1%)	**19.87**	20.28	(2%)	(2%)

Revenues for this commodity group increased by $39 million, or 20%, in the second quarter and $57 million, or 15%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to higher volumes of domestic finished vehicle traffic and finished vehicle imports via the Port of Vancouver resulting from new business; higher applicable fuel surcharge rates; and freight rate increases. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Revenue per RTM increased by 2% in the second quarter and decreased by 2% in the first half of 2017 when compared to the same periods in 2016. The increase in the second quarter was mainly due to the positive translation impact of a weaker Canadian dollar, higher applicable fuel surcharge rates, and freight rate increases; partly offset by an increase in the average length of haul. The decrease in the first half of 2017 was mainly due to an increase in the average length of haul, partly offset by higher applicable fuel surcharge rates and freight rate increases.

Other revenues

	Three months ended June 30				Six months ended June 30			
	2017	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Revenues *(millions)*	**$ 218**	$ 196	11%	8%	**$ 349**	$ 315	11%	10%

Other revenues increased by $22 million, or 11%, in the second quarter and $34 million, or 11%, in the first half of 2017 when compared to the same periods in 2016, mainly due to higher revenues from docks and vessels, and automotive logistic services. The positive translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Operating expenses

Operating expenses for the second quarter of 2017 amounted to $1,834 million compared to $1,549 million in the same quarter of 2016, an increase of $285 million, or 18%. Operating expenses for the first half of 2017 amounted to $3,737 million compared to $3,296 million in the same period of 2016, an increase of $441 million, or 13%. The increases were mainly due to higher fuel costs, increased purchased services and material costs, and higher labor and fringe benefits expense resulting from increased volumes, as well as increased casualty and other expense. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

	Three months ended June 30				Six months ended June 30			
In millions	**2017**	2016	% Change	% Change at constant currency	**2017**	2016	% Change	% Change at constant currency
Labor and fringe benefits	**$ 527**	$ 469	(12%)	(10%)	**$ 1,107**	$ 1,059	(5%)	(5%)
Purchased services and material	**432**	377	(15%)	(12%)	**872**	785	(11%)	(11%)
Fuel	**329**	243	(35%)	(30%)	**671**	478	(40%)	(41%)
Depreciation and amortization	**326**	296	(10%)	(8%)	**649**	603	(8%)	(8%)
Equipment rents	**103**	92	(12%)	(8%)	**204**	187	(9%)	(9%)
Casualty and other	**117**	72	(63%)	(58%)	**234**	184	(27%)	(27%)
Total operating expenses	**$ 1,834**	$ 1,549	(18%)	(16%)	**$ 3,737**	$ 3,296	(13%)	(13%)

Labor and fringe benefits

Labor and fringe benefits expense increased by $58 million, or 12%, in the second quarter of 2017 and by $48 million, or 5%, in the first half of 2017 when compared to the same periods in 2016. The increases were primarily due to general wage increases, higher headcount and overtime costs due to increased volumes of traffic, and higher incentive-based compensation. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Purchased services and material

Purchased services and material expense increased by $55 million, or 15%, in the second quarter of 2017 and $87 million, or 11%, in the first half when compared to the same periods in 2016. The increases were mainly due to higher costs of services purchased from outside contractors and higher repairs and maintenance costs resulting from increased volumes of traffic. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Fuel

Fuel expense increased by $86 million, or 35%, in the second quarter of 2017 and $193 million, or 40%, in the first half of 2017 when compared to the same periods in 2016. The increase in the second quarter was primarily due to increased volumes of traffic, higher fuel prices, and the negative translation impact of a weaker Canadian dollar. The increase in the first half was primarily due to higher fuel prices and increased volumes of traffic.

Depreciation and amortization

Depreciation and amortization expense increased by $30 million, or 10%, in the second quarter of 2017 and by $46 million, or 8%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to net capital additions. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Equipment rents

Equipment rents expense increased by $11 million, or 12%, in the second quarter of 2017 and by $17 million, or 9%, in the first half of 2017 when compared to the same periods of 2016. The increases were primarily due to higher car hire expense resulting from increased volumes of traffic, partly offset by lower car and equipment lease expenses. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Casualty and other

Casualty and other expense increased by $45 million, or 63%, in the second quarter of 2017 and by $50 million, or 27%, in the first half of 2017 when compared to the same periods in 2016. The increases were mainly due to higher incident costs, and increased environmental expenses. The negative translation impact of a weaker Canadian dollar also contributed to the increase in the second quarter.

Other items

Interest expense

Interest expense was $123 million and $245 million for the three and six months ended June 30, 2017, respectively, compared to $116 million and $239 million, respectively, for the same periods in 2016. The increases were mainly due to the negative translation impact of the weaker Canadian dollar and a higher level of debt.

Other income (loss)

In the second quarter and first half of 2017, the Company recorded other income of $1 million and $3 million, respectively, compared to other loss of $1 million and other income of $4 million, respectively, for the same periods in 2016.

Income tax expense

The Company recorded income tax expense of $342 million and $641 million for the three and six months ended June 30, 2017, respectively, compared to $318 million and $625 million, respectively, for the same period in 2016.

The six months ended June 30, 2017 figure included deferred income tax recoveries of $18 million recorded in the second quarter and $5 million recorded in the first quarter, both resulting from the enactment of lower provincial corporate income tax rates.

The six months ended June 30, 2016 figure included a deferred income tax expense of $7 million recorded in the second quarter, resulting from the enactment of a higher provincial corporate income tax rate.

The effective tax rates for the three and six months ended June 30, 2017 were 24.9% and 25.1%, respectively, compared to 27.0% and 27.5%, respectively, for the same periods in 2016. Excluding the aforementioned deferred income tax recoveries and expense, the effective tax rates for the three and six months ended June 30, 2017 were 26.2% and 26.0%, respectively, compared to 26.4% and 27.2%, respectively, for the same periods in 2016. The decrease in the effective tax rate for the six months ended June 30, 2017 was mainly due to a lower proportion of the Company's pre-tax income being earned in higher tax rate jurisdictions and the impact of a higher excess tax benefit resulting from the settlement of equity settled awards in the first quarter of 2017.

Summary of quarterly financial data

	2017 Quarters		2016 Quarters				2015 Quarters	
In millions, except per share data	**Second** (1)	First (2)	Fourth (3)	Third	Second (4)	First	Fourth	Third
Revenues	**$ 3,329**	$ 3,206	$ 3,217	$ 3,014	$ 2,842	$ 2,964	$ 3,166	$ 3,222
Operating income	**$ 1,495**	$ 1,303	$ 1,395	$ 1,407	$ 1,293	$ 1,217	$ 1,354	$ 1,487
Net income	**$ 1,031**	$ 884	$ 1,018	$ 972	$ 858	$ 792	$ 941	$ 1,007
Basic earnings per share	**$ 1.36**	$ 1.16	$ 1.33	$ 1.26	$ 1.10	$ 1.01	$ 1.19	$ 1.26
Diluted earnings per share	**$ 1.36**	$ 1.16	$ 1.32	$ 1.25	$ 1.10	$ 1.00	$ 1.18	$ 1.26
Dividends per share	**$ 0.4125**	$ 0.4125	$ 0.3750	$ 0.3750	$ 0.3750	$ 0.3750	$ 0.3125	$ 0.3125

(1) Included in Net income was a deferred income tax recovery of $18 million that resulted from the enactment of a lower corporate income tax rate.

(2) Included in Net income was a deferred income tax recovery of $5 million that resulted from the enactment of a lower corporate income tax rate.

(3) Included in Net income was a gain on disposal of the Viaduc du Sud of $76 million, or $66 million after-tax, which was recorded in Other income.

(4) Included in Net income was a deferred income tax expense of $7 million that resulted from the enactment of a higher corporate income tax rate.

Revenues generated by the Company during the year are influenced by seasonal weather conditions, general economic conditions, cyclical demand for rail transportation, and competitive forces in the transportation marketplace (see the section entitled *Business risks* of the Company's 2016 Annual MD&A). Operating expenses reflect the impact of freight volumes, seasonal weather conditions, labor costs, fuel prices, and the Company's productivity initiatives. Fluctuations in the Canadian dollar relative to the US dollar have also affected the conversion of the Company's US dollar-denominated revenues and expenses and resulted in fluctuations in net income in the rolling eight quarters presented above.

Liquidity and capital resources

An analysis of the Company's liquidity and capital resources is provided in the section entitled *Liquidity and capital resources* of the Company's 2016 Annual MD&A. There were no significant changes during the first half of 2017, except as noted below.

As at June 30, 2017 and December 31, 2016, the Company had Cash and cash equivalents of $131 million and $176 million, respectively; Restricted cash and cash equivalents of $461 million and $496 million, respectively; and a working capital deficit of $1,391 million and $901 million, respectively. The working capital deficit increased by $490 million in the first half of 2017 primarily as a result of an increase in the Current portion of long-term debt and Accounts payable and other. There are currently no specific requirements relating to working capital other than in the normal course of business as discussed herein.

The Company expects cash from operations and its various sources of financing to be sufficient to meet its ongoing obligations. The Company is not aware of any trends or expected fluctuations in its liquidity that would impact its ongoing operations or financial condition as at the date of this MD&A.

Available financing sources

Shelf prospectus and registration statement

The Company's shelf prospectus and registration statement, for which CN can issue debt securities in the Canadian and U.S. capital markets until February 4, 2018, has remaining capacity available of $4,466 million. Access to the Canadian and U.S. capital markets under the shelf prospectus and registration statement is dependent on market conditions.

Revolving credit facility

On March 15, 2017, the Company's revolving credit facility agreement was amended to extend the term of the credit facility by one year. The credit facility of $1.3 billion consists of a tranche for $420 million maturing on May 5, 2020 and a tranche for $880 million maturing on May 5, 2022. As at June 30, 2017 and December 31, 2016, the Company had no outstanding borrowings under its revolving credit facility and there were no draws during the six months ended June 30, 2017.

Commercial paper

There were no changes to the Company's commercial paper programs in the first half of 2017. As at June 30, 2017 and December 31, 2016, the Company had total commercial paper borrowings of US$435 million ($564 million) and US$451 million ($605 million), respectively, presented in Current portion of long-term debt on the Consolidated Balance Sheets.

Accounts receivable securitization program

As at June 30, 2017 and December 31, 2016, the Company had no proceeds received under the accounts receivable securitization program, which provides the Company with access to up to $450 million of proceeds.

Bilateral letter of credit facilities

The Company has a series of committed and uncommitted bilateral letter of credit facility agreements. On March 15, 2017, the Company extended the maturity date of the committed bilateral letter of credit facility agreements to April 28, 2020. As at June 30, 2017, the Company had outstanding letters of credit of $380 million ($451 million as at December 31, 2016) under the committed facilities from a total available amount of $441 million ($508 million as at December 31, 2016) and $124 million ($68 million as at December 31, 2016) under the uncommitted facilities. As at June 30, 2017, included in Restricted cash and cash equivalents was $391 million ($426 million as at December 31, 2016) and $68 million ($68 million as at December 31, 2016) which were pledged as collateral under the committed and uncommitted bilateral letter of credit facilities, respectively.

Additional information relating to the Company's financing sources is provided in the section entitled *Liquidity and capital resources – Available financing sources* of the Company's 2016 Annual MD&A as well as *Note 5 – Financing activities* to the Company's unaudited Interim Consolidated Financial Statements.

Credit ratings

The Company's long-term debt and commercial paper credit ratings remain unchanged from those described in the section entitled *Liquidity and capital resources – Credit ratings* of the Company's 2016 Annual MD&A.

Cash flows

	Three months ended June 30			Six months ended June 30		
In millions	**2017**	2016	Variance	**2017**	2016	Variance
Net cash provided by operating activities	**$ 1,505**	$ 1,271	$ 234	**$ 2,761**	$ 2,336	$ 425
Net cash used in investing activities	**(694)**	(686)	(8)	**(1,102)**	(1,167)	65
Net cash used in financing activities	**(937)**	(628)	(309)	**(1,731)**	(1,182)	(549)
Effect of foreign exchange fluctuations on US dollar-denominated cash, cash equivalents, restricted cash, and restricted cash equivalents	**(6)**	3	(9)	**(8)**	7	(15)
Net decrease in cash, cash equivalents, restricted cash, and restricted cash equivalents	**(132)**	(40)	(92)	**(80)**	(6)	(74)
Cash, cash equivalents, restricted cash, and restricted cash equivalents, beginning of period	**724**	710	14	**672**	676	(4)
Cash, cash equivalents, restricted cash, and restricted cash equivalents, end of period	**$ 592**	$ 670	$ (78)	**$ 592**	$ 670	$ (78)

Operating activities

Net cash provided by operating activities increased by $234 million in the second quarter and $425 million in the first half of 2017 when compared to the same periods in 2016, due to improvements in cash earnings and favorable changes in working capital.

Pension contributions

The Company's contributions to its various defined benefit pension plans are made in accordance with the applicable legislation in Canada and the U.S. and such contributions follow minimum and maximum thresholds as determined by actuarial valuations.

Actuarial valuations are generally required on an annual basis for all Canadian plans, or when deemed appropriate by the Office of the Superintendent of Financial Institutions (OSFI). Actuarial valuations are also required annually for the Company's U.S. qualified pension plans. For accounting purposes, the funded status is calculated under GAAP. For funding purposes, the funded status of the Company's Canadian registered defined benefit pension plans is calculated under going concern and solvency scenarios as prescribed under federal pension legislation and is subject to guidance issued by the Canadian Institute of Actuaries and OSFI. The federal pension legislation requires funding deficits to be paid over a number of years. Alternatively, a letter of credit can be subscribed to fulfill solvency deficit payments.

The Company's most recently filed actuarial valuations for funding purposes for its Canadian registered defined benefit pension plans conducted as at December 31, 2016 indicated a funding excess on a going concern basis of approximately $2.6 billion and a funding excess on a solvency basis of approximately $0.2 billion calculated using the three-year average of the plans' hypothetical wind-up ratio.

Pension contributions for the six months ended June 30, 2017 and 2016 of $76 million and $88 million, respectively, primarily represent contributions to the CN Pension Plan, for the current service cost as determined under the Company's current actuarial valuations for funding purposes. In 2017, the Company expects to make total cash contributions of approximately $115 million for all of the Company's pension plans.

Adverse changes to the assumptions used to calculate the Company's funding status, particularly the discount rate, as well as changes to existing federal pension legislation could significantly impact the Company's future pension contributions.

Additional information relating to the pension plans is provided in *Note 12 – Pensions and other postretirement benefits* to the Company's 2016 Annual Consolidated Financial Statements.

Income tax payments

Net income tax payments decreased by $65 million in the first six months of 2017 when compared to the same period in 2016, mainly due to a lower required final payment in Canada for the 2016 fiscal year, made in February 2017. For 2017, the Company's net income tax payments are expected to be approximately $675 million.

On July 6, 2017, the state of Illinois enacted into law an increase to its current corporate income tax rate from 7.75% to 9.5%, effective as of July 1, 2017, and canceled the scheduled corporate income tax rate decrease to 7.3% in 2025. As a result of this change in law, the Company's net deferred income tax liability is expected to increase by approximately $31 million in the third quarter.

Investing activities

Net cash used in investing activities increased by $8 million in the second quarter of 2017 when compared to the same period in 2016. Net cash used in investing activities decreased by $65 million in the first half of 2017 when compared to the same period in 2016, mainly as a result of lower property additions.

Property additions

	Three months ended June 30		Six months ended June 30	
In millions	2017	2016	2017	2016
Track and roadway	**$ 554**	$ 560	**$ 853**	$ 838
Rolling stock	**25**	43	**50**	164
Buildings	**13**	13	**22**	21
Information technology	**51**	22	**90**	42
Other	**32**	32	**56**	74
Property additions (1)	**$ 675**	$ 670	**$ 1,071**	$ 1,139

(1) Includes $110 million and $192 million associated with the U.S. federal government legislative Positive Train Control implementation in the three and six months ended June 30, 2017, respectively ($64 million and $110 million in the three and six months ended June 30, 2016, respectively).

2017 Capital expenditure program

In the first quarter of 2017, the Company increased its budget for capital spending from approximately $2.5 billion to approximately $2.6 billion, allocating an additional $0.1 billion for the acquisition of 22 new high-horsepower locomotives and various other projects to support growth opportunities. Additional details of the Company's 2017 capital program are provided in the section entitled *Liquidity and capital resources – Cash flows* of the Company's 2016 Annual MD&A.

Financing activities

Net cash used in financing activities increased by $309 million in the second quarter and $549 million in the first half of 2017 when compared to the same periods in 2016, primarily driven by less cash provided by debt financing activities in the current year.

Debt financing activities

Debt financing activities in the first half of 2017 included the following:

- Net repayment of commercial paper of $112 million in the second quarter and $23 million in the first half; and
- Repayment of debt related to capital leases of $29 million in the second quarter and $39 million in the first half.

Debt financing activities in the first half of 2016 included the following:

- On February 23, 2016, issuance of US$500 million ($686 million) 2.75% Notes due 2026 in the U.S. capital markets, which resulted in net proceeds of $677 million;
- On June 1, 2016, repayment of US$250 million ($328 million) 5.80% Notes due 2016 upon maturity;
- Repayment of debt related to capital leases of $59 million in the second quarter and $170 million in the first half; and
- Net issuance of commercial paper of $622 million in the second quarter and $322 million in the first half.

Additional information relating to the Company's outstanding debt securities is provided in *Note 10 – Long-term debt* to the Company's 2016 Annual Consolidated Financial Statements.

Share repurchase program

The Company may repurchase shares pursuant to a Normal Course Issuer Bid (NCIB) at prevailing market prices plus brokerage fees, or such other prices as may be permitted by the Toronto Stock Exchange. Under its current NCIB, the Company may repurchase up to 33.0 million common shares between October 30, 2016 and October 29, 2017. As at June 30, 2017, the Company had repurchased 14.1 million common shares for $1,305 million under its current program.

The following table provides the information related to the share repurchase program for the three and six months ended June 30, 2017 and 2016:

	Three months ended June 30				Six months ended June 30			
In millions, except per share data		**2017**		2016		**2017**		2016
Number of common shares repurchased (1)		**5.2**		7.2		**10.6**		14.6
Weighted-average price per share (2)	**$**	**99.38**	$	73.80	**$**	**94.98**	$	72.20
Amount of repurchase (3)	**$**	**521**	$	533	**$**	**1,012**	$	1,053

(1) Includes repurchases of common shares pursuant to private agreements between the Company and arm's length third-party sellers.

(2) Includes brokerage fees where applicable.

(3) Includes settlements in subsequent periods.

Share Trusts

The Company's Employee Benefit Plan Trusts ("Share Trusts") purchase common shares on the open market, which are used to deliver common shares under the Share Units Plan. For the six months ended June 30, 2017 and 2016, there were no purchases of common shares by the Share Trusts. For the six months ended June 30, 2017, the Share Trusts disbursed 0.3 million common shares, which had a historical cost of $24 million, representing a weighted-average price per share of $77.99, for settlement under the Share Units Plan. For the six months ended June 30, 2016, the Share Trusts disbursed 0.3 million common shares, which had a historical cost of $23 million, representing a weighted-average price per share of $73.31, for settlement under the Share Units Plan. Additional information relating to the share purchases by Share Trusts is provided in *Note 13 – Share capital* to the Company's 2016 Annual Consolidated Financial Statements.

Dividends paid

The Company paid quarterly dividends of $0.4125 per share amounting to $310 million and $623 million in the second quarter and first half of 2017 respectively, compared to $291 million and $584 million, at the rate of $0.3750 per share, for the same periods in 2016.

Contractual obligations

In the normal course of business, the Company incurs contractual obligations. The following table sets forth the Company's contractual obligations for the following items as at June 30, 2017:

In millions		**Total**		2017		2018		2019		2020		2021		2022 & thereafter
Debt obligations (1)	**$**	**10,257**	$	1,212	$	675	$	707	$	-	$	762	$	6,901
Interest on debt obligations (2)		**6,916**		230		424		375		355		352		5,180
Capital lease obligations (3)		**388**		174		24		16		22		12		140
Operating lease obligations		**574**		70		127		98		69		51		159
Purchase obligations (4)		**1,478**		814		137		92		84		81		270
Other long-term liabilities (5)		**740**		36		65		46		65		47		481
Total contractual obligations	**$**	**20,353**	**$**	**2,536**	**$**	**1,452**	**$**	**1,334**	**$**	**595**	**$**	**1,305**	**$**	**13,131**

(1) Presented net of unamortized discounts and debt issuance costs and excludes capital lease obligations.

(2) Interest payments on the floating rate notes are calculated based on the applicable three-month London Interbank Offered Rate (LIBOR).

(3) Includes $300 million of minimum lease payments and $88 million of imputed interest at rates ranging from 0.7% to 6.8%.

(4) Includes commitments for wheels, railroad ties, rail, fuel, and other equipment and services, as well as outstanding information technology service contracts and licenses.

(5) Includes expected payments for workers' compensation, postretirement benefits other than pensions, net unrecognized tax benefits, environmental liabilities and pension obligations that have been classified as contractual settlement agreements.

Free cash flow

Management believes that free cash flow is a useful measure of liquidity as it demonstrates the Company's ability to generate cash for debt obligations and for discretionary uses such as payment of dividends, share repurchases, and strategic opportunities. The Company defines its free cash flow measure as the difference between net cash provided by operating activities and net cash used in investing activities; adjusted for the impact of major acquisitions, if any. Free cash flow does not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

The following table provides a reconciliation of net cash provided by operating activities as reported for the three and six months ended June 30, 2017 and 2016, to free cash flow:

	Three months ended June 30		Six months ended June 30	
In millions	**2017**	2016	**2017**	2016
Net cash provided by operating activities	**$ 1,505**	$ 1,271	**$ 2,761**	$ 2,336
Net cash used in investing activities [(1)]	**(694)**	(686)	**(1,102)**	(1,167)
Free cash flow	**$ 811**	$ 585	**$ 1,659**	$ 1,169

(1) As a result of the retrospective adoption of Accounting Standards Update 2016-18 in the first quarter of 2017, changes in restricted cash and cash equivalents are no longer classified as investing activities within the Consolidated Statements of Cash Flows and are no longer included as an adjustment in the Company's definition of free cash flow. There is no impact to free cash flow resulting from this reclassification.

Adjusted debt-to-adjusted EBITDA multiple

Management believes that the adjusted debt-to-adjusted earnings before interest, income taxes, depreciation and amortization (EBITDA) multiple is a useful credit measure because it reflects the Company's ability to service its debt and other long term obligations. The Company calculates the adjusted debt-to-adjusted EBITDA multiple as adjusted debt divided by adjusted EBITDA. These measures do not have any standardized meaning prescribed by GAAP and therefore, may not be comparable to similar measures presented by other companies.

The following table provides a reconciliation of debt and net income to the adjusted measures presented below, which have been used to calculate the adjusted debt-to-adjusted EBITDA multiple:

In millions, unless otherwise indicated	*As at and for the twelve months ended June 30,*	**2017**	2016
Debt		**$ 10,557**	$ 10,322
Adjustment: Present value of operating lease commitments [(1)]		**488**	561
Adjusted debt		**$ 11,045**	$ 10,883
Net income		**$ 3,905**	$ 3,598
Interest expense		**486**	469
Income tax expense		**1,303**	1,315
Depreciation and amortization		**1,271**	1,180
EBITDA		**6,965**	6,562
Adjustments:			
Other income		**(94)**	(31)
Deemed interest on operating leases		**22**	27
Adjusted EBITDA		**$ 6,893**	$ 6,558
Adjusted debt-to-adjusted EBITDA multiple (times)		**1.60**	1.66

(1) The operating lease commitments have been discounted using the Company's implicit interest rate for each of the periods presented.

All forward-looking statements discussed in this section are subject to risks and uncertainties and are based on assumptions about events and developments that may not materialize or that may be offset entirely or partially by other events and developments. See the section of this MD&A entitled *Forward-looking statements* for a discussion of assumptions and risk factors affecting such forward-looking statements.

Off balance sheet arrangements

Guarantees and indemnifications

In the normal course of business, the Company, including certain of its subsidiaries, enters into agreements that may involve providing guarantees or indemnifications to third parties and others, which may extend beyond the term of the agreements. These include, but are not limited to, residual value guarantees on operating leases, standby letters of credit, surety and other bonds, and indemnifications that are customary for the type of transaction or for the railway business. As at June 30, 2017, the Company has not recorded a liability with respect to guarantees and indemnifications. Additional information relating to guarantees and indemnifications is provided in *Note 9 – Major commitments and contingencies* to the Company's unaudited Interim Consolidated Financial Statements.

Outstanding share data

As at July 25, 2017, the Company had 751.0 million common shares and 5.7 million stock options outstanding.

Financial instruments

Risk management

In the normal course of business, the Company is exposed to various financial risks from its use of financial instruments, such as credit risk, liquidity risk, and market risks which include foreign currency risk, interest rate risk and commodity price risk. A description of these risks and how the Company manages them, is provided in the section entitled *Financial instruments* of the Company's 2016 Annual MD&A.

Foreign currency risk

The estimated annual impact on net income of a year-over-year one-cent change in the Canadian dollar relative to the US dollar is approximately $30 million.

Derivative financial instruments

As at June 30, 2017, the Company had outstanding foreign exchange forward contracts with a notional value of US$1,126 million (US$1,035 million as at December 31, 2016). For the three and six months ended June 30, 2017, the Company recorded a loss of $26 million and $41 million, respectively, related to foreign exchange forward contracts, compared to a loss of $2 million and $47 million, respectively, for the same periods in 2016. These losses were largely offset by the re-measurement of US dollar-denominated monetary assets and liabilities recorded in Other income.

As at June 30, 2017, Other current assets included an unrealized gain of $nil ($19 million as at December 31, 2016) and Accounts payable and other included an unrealized loss of $32 million ($1 million as at December 31, 2016), related to the fair value of outstanding foreign exchange forward contracts.

Fair value of financial instruments

As at June 30, 2017, the Company's investments had a carrying amount of $71 million ($68 million as at December 31, 2016) and a fair value of $222 million ($220 million as at December 31, 2016). As at June 30, 2017, the Company's debt had a carrying amount of $10,557 million ($10,937 million as at December 31, 2016) and a fair value of $11,793 million ($12,084 million as at December 31, 2016).

Additional information relating to financial instruments is provided in *Note 10 – Financial instruments* to the Company's unaudited Interim Consolidated Financial Statements.

Recent accounting pronouncements

The following recent Accounting Standards Update (ASU) issued by the Financial Accounting Standards Board (FASB) was adopted by the Company during the current period:

Standard	Description	Impact
ASU 2016-18, Statement of Cash Flows (Topic 230): Restricted Cash	Requires that a Statement of Cash Flows explain the change during the period in the total of cash, cash equivalents, and amounts generally described as restricted cash or restricted cash equivalents.	The Company elected to early adopt the amendments of this ASU in the first quarter of 2017 on a retrospective basis. As a result of the adoption of this ASU, changes in restricted cash and cash equivalents are no longer classified as investing activities, and the Consolidated Statement of Cash Flows now explains the change during the period in the total of cash, cash equivalents, restricted cash, and restricted cash equivalents.

The following recent ASUs issued by FASB have an effective date after June 30, 2017 and have not been adopted by the Company:

Standard (1)	Description	Impact	Effective date (2)
ASU 2017-07 Compensation – Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost	Requires employers that sponsor defined benefit pension plans and/or other postretirement benefit plans to report the service cost component in the same line item or items as other compensation costs. The other components of net periodic benefit cost are required to be presented in the Statement of Income separately from the service cost component and outside a subtotal of income from operations. The new guidance allows only the service cost component to be eligible for capitalization. The guidance must be applied retrospectively for the presentation of the service cost component and other components of net periodic benefit cost in the Statement of Income and prospectively for the capitalization of the service cost component of net periodic benefit cost.	The amendments will affect the classification of the components of pension and postretirement benefit costs other than service cost which will be shown outside of income from operations in a separate caption in the Company's Consolidated Statements of Income. Had the ASU been applicable for the three and six months ended June 30, 2017, Operating income would have been reduced by approximately \$80 million and \$159 million, respectively (\$78 million and \$145 million for the three and six months ended June 30, 2016, respectively) with a corresponding increase presented in the new caption below Operating income with no impact on Net income as a result of the reclassification. The guidance allowing only the service cost component to be eligible for capitalization is not expected to have a significant impact on the Company's Consolidated Financial Statements. CN will adopt the requirements of the ASU effective January 1, 2018.	December 15, 2017. Early adoption is permitted.
ASU 2016-02, Leases (Topic 842)	Requires the recognition of lease assets and lease liabilities on the Balance Sheet by lessees for most leases. The new standard also requires additional qualitative and quantitative disclosures about leases, significant judgments made in applying requirements, and the amounts recognized in the financial statements relating to leases. Lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using the modified retrospective approach.	The Company is evaluating the effects that the adoption of the ASU will have on its Consolidated Financial Statements and related disclosures, processes and internal controls. The Company is reviewing its lease contracts and expects that the majority of its operating leases with a term over twelve months will be recognized on the Company's Consolidated Balance Sheets. The Company expects that the ASU will have a significant impact on its Consolidated Balance Sheets with the most significant changes relating to the recognition of new right of use assets and lease liabilities for leases currently classified as operating leases. CN expects to adopt the requirements of the ASU effective January 1, 2019.	December 15, 2018. Early adoption is permitted.

Standard [1]	Description	Impact	Effective date [2]
ASU 2014-09, Revenue from Contracts with Customers (Topic 606) and related amendments	The basis of the new standard is that an entity recognizes revenue to represent the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. Additional financial statement presentations and disclosures will be required to assist users of financial statements understand the nature, amount, timing and uncertainty of revenues and cash flows arising from an entity's contracts. The guidance can be applied using either the retrospective or modified retrospective transition method.	The Company continues to make progress towards implementation of the ASU. With respect to freight contracts, in-depth reviews have been completed and the Company has confirmed that freight revenues will continue to be recognized over time based on the transit time of freight as it moves from origin to destination. The Company has also evaluated principal versus agent considerations, including assessing the nature of its promises to customers, and does not expect any significant changes to revenue recognition from this guidance. The Company continues to review freight contracts for terms that could represent additional performance obligations, and evaluate transaction price considerations. The Company is also finalizing its review of non-freight contracts to determine the impact of the ASU on its Consolidated Financial Statements. Additionally, the Company is evaluating the disclosure requirements, and changes to processes and internal controls necessary to meet the reporting and disclosure requirements. Based on the work already performed, the Company does not expect that the ASU will have a material impact on its Consolidated Financial Statements. The Company plans to adopt this ASU using the modified retrospective transition method, effective January 1, 2018.	December 15, 2017. Early adoption is permitted.

(1) Other recently issued ASUs required to be applied for periods beginning on or after June 30, 2017 have been evaluated by the Company and will not have a significant impact on the Company's Consolidated Financial Statements.

(2) Effective for annual and interim reporting periods beginning after the stated date.

Critical accounting estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates, judgments and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management reviews its estimates based upon available information. Actual results could differ from these estimates. The Company's policies for income taxes, depreciation, pensions and other postretirement benefits, personal injury and other claims and environmental matters, require management's more significant judgments and estimates in the preparation of the Company's Consolidated Financial Statements and, as such, are considered to be critical. Reference is made to the section entitled *Critical accounting estimates* of the Company's 2016 Annual MD&A for a detailed description of the Company's critical accounting estimates. There have not been any material changes to these estimates in the first half of 2017.

Management discusses the development and selection of the Company's critical accounting policies, including the underlying estimates and assumptions, with the Audit Committee of the Company's Board of Directors. The Audit Committee has reviewed the Company's related disclosures.

Business risks

In the normal course of business, the Company is exposed to various business risks and uncertainties that can have an effect on the Company's results of operations, financial position, or liquidity. While some exposures may be reduced by the Company's risk management strategies, many risks are driven by external factors beyond the Company's control or are of a nature which cannot be eliminated.

Reference is made to the section entitled *Business risks* of the Company's 2016 Annual MD&A for a detailed description of such key areas of business risks and uncertainties with respect to: Competition, Environmental matters, Personal injury and other legal claims, Labor negotiations, Regulation, Economic conditions, Pension funding volatility, Reliance on technology, Trade restrictions, Terrorism and international conflicts, Customer credit risk, Liquidity, Supplier concentration, Availability of qualified personnel, Fuel costs, Foreign exchange, Interest rates, Transportation network disruptions, Severe weather and Climate change, which is incorporated herein by reference. Additional risks and uncertainties not currently known to management or that may currently not be considered material by management, could nevertheless also have an adverse effect on the Company's business.

There have been no material changes to the risks described in the Company's 2016 Annual MD&A. The following is an update on labor negotiations, regulatory matters, and trade restrictions.

Labor negotiations

As at June 30, 2017, CN employed a total of 16,116 employees in Canada, of which 11,693, or 73%, were unionized employees; and 6,973 employees in the U.S., of which 5,589, or 80%, were unionized employees. The Company's relationships with its unionized workforce are governed by, amongst other items, collective agreements which are negotiated from time to time. Disputes relating to the renewal of collective agreements could potentially result in strikes, slowdowns and loss of business. Future labor agreements or renegotiated agreements could increase labor and fringe benefits expenses. There can be no assurance that the Company will be able to renew and have its collective agreements ratified without any strikes or lockouts or that the resolution of these collective bargaining negotiations will not have a material adverse effect on the Company's results of operations or financial position.

Canadian workforce

On April 26, 2017, the tentative agreement reached on March 20, 2017 with the International Brotherhood of Electrical Workers (IBEW), governing approximately 700 signals and communications workers, was ratified by its members. The new collective agreement will expire on December 31, 2021.

On May 29, 2017, the Company reached a tentative agreement with the Teamsters Canada Rail Conference (TCRC) to renew the collective agreement governing approximately 3,000 train conductors and yard coordinators. Ratification is expected by August 7, 2017.

Regulation

On May 16, 2017, the Federal Minister of Transport (Minister) introduced Bill C-49, the *Transportation Modernization Act*, which proposes a series of amendments to various federal acts respecting transportation. The bill also proposes to amend the *CN Commercialization Act* to increase the maximum proportion of voting shares of CN that can be held or controlled by any one person to 25%, up from the 15% limit imposed since CN became a public company in 1995.

Economic regulation – Canada

Bill C-49 proposes to amend the *Canada Transportation Act* to, among other things:

- expand the Governor in Council's powers to make regulations requiring major railway companies to provide to the Minister and the Canadian Transportation Agency information relating to rates, service and performance;
- clarify the factors that must be applied in determining whether railway companies are fulfilling their service obligations;
- enable shippers to obtain terms in their contracts dealing with amounts to be paid in relation to a failure to comply with conditions related to railway companies' service obligations;
- create a new remedy for shippers who have access to the lines of only one railway company at the point of origin or destination of the movement of traffic in circumstances where interswitching is not available, also called "long-haul interswitching";
- change the process for the transfer and discontinuance of railway lines to, among other things, require railway companies to make certain information available to the Minister and the public and establish a remedy for non-compliance with the process; and
- change provisions respecting the maximum revenue entitlement for the movement of Western grain and require certain railway companies to provide to the Minister and the public information respecting the movement of grain.

Under Bill C-49, the provisions of the *Fair Rail for Grain Farmers Act* (Bill C-30) will be allowed to sunset on August 1, 2017, with the exception of the provisions dealing with compensation for expenses incurred by shippers and the definition by the Canadian Transportation Agency of ‘operational terms’ for the purpose of rail level of service arbitrations. Therefore, the provisions respecting authority of the Government to establish minimum volumes of grain to be moved by the Company and Canadian Pacific Railway Company and extended interswitching distances for Prairie Provinces will no longer be in force after August 1, 2017.

On June 19, 2017, Bill C-49 passed second reading in the House of Commons and is expected to be reviewed by the House of Commons Standing Committee on Transport, Infrastructure and Communities in September 2017.

Economic regulation – U.S.

On March 23, 2017, the U.S. District Court for the District of Columbia concluded that Section 207 of the *Passenger Rail Investment and Improvement Act of 2008* (PRIIA), which gave Amtrak and the Federal Railroad Association joint authority to promulgate PRIIA performance standards, was void and unconstitutional and vacated the performance standards. On May 19, 2017, the Government defendants filed a notice of appeal with the U.S. Court of Appeals challenging the March 23, 2017 decision. Amtrak’s complaint filed under Section 213 of PRIIA against CN in 2012 for allegedly sub-standard performance of Amtrak trains on CN’s Illinois Central Corporation line is still pending. On July 12, 2017, the U.S. Court of Appeals for the Eighth Circuit concluded that the Surface Transportation Board (STB) exceeded its authority in adopting its final rule defining intercity passenger on-time performance under Section 213 of PRIIA and vacated the STB’s final rule.

On April 26, 2017, the STB denied a reopening petition filed by the Village of Barrington, Illinois and the Illinois Department of Transportation seeking to have the STB extend its monitoring and oversight condition on CN’s 2009 acquisition of the Elgin, Joliet and Eastern Railway (EJ&E) for two years beyond the January 23, 2017 expiration and for a grade separation condition at the intersection of U.S. Route 14 and the EJ&E line in Barrington at CN’s expense. On May 16, 2017, the Village of Barrington filed a petition seeking reconsideration of the STB’s April 26, 2017 decision concerning the request for the grade separation condition. The Village of Barrington is not seeking reconsideration of the STB’s decision denying the request to extend the monitoring and oversight condition on CN’s 2009 acquisition.

Safety regulation – Canada

On April 26, 2017, the Minister initiated the review of the *Railway Safety Act* which was initially scheduled for 2018. A panel of three persons was appointed to proceed with the review and provide a report with recommendations by May 2018.

On May 16, 2017, the Minister introduced Bill C-49 which if enacted, in addition to the proposed amendments to federal acts already discussed, will amend the *Railway Safety Act* to prohibit a railway company from operating railway equipment unless the equipment is fitted with prescribed recording instruments and prescribed information is recorded using those instruments, collected and preserved. The enactment also specifies the circumstances in which the prescribed information that is recorded can be used and communicated by companies, the Minister and railway safety inspectors.

On June 9, 2017, Transport Canada’s *Locomotive Emissions Regulations* (under the *Railway Safety Act*) came into force. The regulations seek to limit air pollution by establishing emission standards and test procedures for new locomotives, and align Canadian standards with U.S. regulations. The new regulations require railway companies to meet emission standards, undertake emission testing, and adhere to anti-idling provisions, in addition to requirements for labelling, testing, record keeping and reporting. CN's locomotives in service at this time are not required to meet the emission standards or the testing and labelling requirements, however when they are removed from service to be remanufactured, refurbished or upgraded, they must meet the new requirements before they are placed back into service.

On June 24, 2017, Transport Canada proposed new regulations aimed at lowering the risk of terrorism on the Canadian rail system, entitled *Transportation of Dangerous Goods by Rail Security Regulations*. The proposed regulations would require all rail carriers to proactively engage in security planning processes and manage security risks, by introducing security awareness training for employees, security plans that include measures to address assessed risks, and security plan training for employees with duties related to the security plan or security sensitive dangerous goods. Rail carriers would also have to conduct security inspections of certain railway vehicles containing dangerous goods, report potential security threats and concerns to the Canadian Transport Emergency Centre, and employ a rail security coordinator.

No assurance can be given that these and any other current or future regulatory or legislative initiatives by the Canadian and U.S. federal governments and agencies will not materially adversely affect the Company’s results of operations or its competitive and financial position.

Trade restrictions

On December 15, 2016, the U.S. Department of Commerce ("Commerce") agreed to conduct countervailing duty and antidumping duty investigations of Canadian softwood lumber exports to the U.S. During the second quarter of 2017, Commerce made preliminary affirmative determinations in both investigations, announcing preliminary countervailing duties on April 24, 2017 and preliminary antidumping duties on June 26, 2017. As a result of these determinations, U.S. Customs and Border Protection was instructed to collect cash deposits from importers of softwood lumber from Canada based on a company-specific rate for mandatory respondents and a weighted-average rate for all others of 19.88% for countervailing duties and 6.87% for antidumping duties, for a maximum period of four months from the date each duty went into effect. Commerce is scheduled to announce its final determinations in both investigations in September 2017, unless postponed. If final affirmative determinations are made in both investigations, final orders for countervailing and antidumping duties could be issued before the end of 2017.

There can be no assurance that this or any other potential trade actions taken by the Canadian and U.S. federal governments and agencies will not materially adversely affect the volume of rail shipments and/or revenues from commodities carried by the Company, and thus materially and negatively impact earnings and/or cash flow.

Controls and procedures

The Company's Chief Executive Officer and its Chief Financial Officer, after evaluating the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of June 30, 2017, have concluded that the Company's disclosure controls and procedures were effective.

During the second quarter ended June 30, 2017, there was no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.