The Railroad Week in Review
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Railroads a century ago were the mainstays of the NY stock exchange and all paid handsome dividends. With the tax law changes on dividends, how do rails compare today? Times change, and mergers, consolidations, share repurchases and sheer competitive economics now make higher claims on cash flow than paying dividends to shareholders. Still, with the S&P average dividend yield under two percent, Table 1 shows the Class 1s are holding their own

Among the non-Class Is Providence & Worcester (PWX) has a hefty payout however there is so little trading volume just one big trade either way drives the yield the opposite way (as price goes down yield goes up). Moreover, annual freight revenues going back to 1998 have remained in the $22-$23 mm range while income from property sales ranges from $1 mm to $4 mm. Annual eps have slid steadily down from $1.10 in 1998, yet the dividend has crept up to 16 cents from 12 cents in 1998. Share count rose to 4.5 mm from 3.5 mm in the same period.

FLA this week increased the dividend 60% to $0.16 from a dime payable June 25 to shareholders of record as of June 11. In contrast, Pioneer Rail (PRRR) is a "penny stock." The cash value of a day's average trades is about equal to that of PWX, so it too is subject to wide percentage swings in price and yield.

On the vendor side GATX (GMT) has both significant trading volume and a whopping 7,64% yield at today's prices. This is more of an asset play like banks or utilities that generates a ton of cash. It has more than $3.6 bn in rail assets, roughly half its total asset base. Over the year the dividend payment has been a half to a third of earnings per share, though in 2002 the dividend was twice the eps.

And speaking of GMT, a news item this week says a Warren Buffett affiliate sold off about a third of its GMT holdings, 2.5 mm shares. Last month S&P downgraded GMT to Triple-B minus from BBB based on sluggish forward earnings performance estimates. The cautious investor will note that from early 1999 through mid-2001 the 200-day average price per share rose to $35 from $25. Dividend yields ran more in the 3-4% range and increased a few cents a year. Now the stock price has been cut in half with the same dividend payout, ergo the seemingly generous 7%.

A second question has to be how much of a premium one is willing to pay for the dividend. Recall our earlier discussion on price-earnings-growth ratios (WIR 5/3/2003). The PE ratio theoretically equals the expected one-year forward growth rate so an equity is fairly priced with a PEG of one. Anything under one could be a screaming Buy and anything north of 1.5 may be a bit rich. Based on these fundamentals both RRA and GWR have legs; the Canadians and CSX may merit further investigation.

Canadian Pacific will take delivery of 500 new "lumber cars from Greenbrier's Trenton (Nova Scotia) Works at a rate of about 45 a week starting in July. The car is designed to carry packaged lumber and other products with load bearing pieces attached to the packaging (see photo at www.gbrx.com). It has 15" end-of-car cushioning, 286,000 lb. gross rail load and 110-ton capacity.

It also has an 11' 7 3/8" clear loading height and can be loaded to its weight capacity over the 60' between truck centers. As they are delivered, CPR will purge from its fleet some 300 older, less productive lumber cars that are leased on a short- term but higher cost basis. The purchase will increase CPR's fleet of cars to 2,650, its largest fleet ever of modern, high-capacity lumber cars.

Elsewhere, CP has posted “For Sale” signs three Saskatchewan branch lines that have seen little or no traffic in the past three years as former rail users either closed or stopped shipping by rail. CP first announced these lines were candidates for discontinuance with the update of its three-year network plan in August 2001. Interested parties must say so in writing to CP by July 31, 2003. If no interest, the lines will be offered to the provincial government with 30 days to make up their minds. If no sale, CP may discontinue operations on these lines.

Caveat emptor. As I recall the provincial requirements for line abandonments are pretty stringent and any shortline getting into any of these lines will have a tough time getting out. CP does not give up branch lines lightly as more than 60% of revenue comes from the merchandise carload side of the house, so there’s good reason for selling.

Continuing the Tranzrail Holdings (TRH) saga, S&P’s credit rating service removed RailAmerica (RRA) from its “CreditWatch” because the Boca team took a bye on TRH. Said S&P, “The ratings reflect the company's aggressive debt leverage and the potential for debt-financed acquisitions.” S&P went on to say RRA’s strength as a NA shortline operator is a plus. But what I don’t get is why anybody would want TRH in the first place, absent some serious trimming.

According to the TRH “Interim Report” for the six months ending 12/3/02002, the *Interisland Line* ferry service generated 83% of total operating income to railroad’s 14%. Seems to me TRH would be better off dumping the RR, hyping the boat rides, and re-naming the company. So far TRH has piece-mealed off long-distance and commuter passenger lines, outsourced engineering and maintenance, and worked hard to downsize the carload business in favor of hub-and spoke container services with highways acting as feeder routes. Why not get rid of it all?

TRH share prices since Jan 2002 had dropped to less than $NZ0.50 pre-RRA offer from $NZ4.00 where they had been level for some years. Following the $NZ0.75 RRA offer the public suddenly woke up, trading TRH back up to $NZ0.84 this week. But long-time WIR readers will recall that any company with “Rail” in its name generating minuscule profits from rail and major income from non-rail operations ought to raise eyebrows.

Eyebrows evidently were not raised at Australia's Toll Holdings Ltd. On Thursday the company, which has said it already holds a 10.1% stake in TRH, made good on last week’s hint that it might make a bid. Like RRA, Toll will offer $NZ0.75 per share and assume existing debt and lease commitments. The Toll offer will be fully funded by debt. The analyst community seems to think TRH is a viable company and once it gets past a near-term debt crunch it should do OK. Maybe.

Norfolk Southern holds its annual shortline meeting in Roanoke this coming week. The program promises a good mix of operations and commercial with a generous amount of feedback time for the shortline attendees. It has been a long-standing WIR theme that shortlines need to tell their story with facts and performance measures. John Kraemer and associates have op’d the doors wide, so bring it on.

Table 1. Railroad and Vendor Dividend Yield and Price Multiples, 5/28/2003

Tick	Close	Class	Vol	Div/Share	Div Yield	PE	PEG
BNI	$ 28.80	I	1,428,000	$ 0.48	1.67%	11.63	1.38
UNP	$ 59.00	I	1,622,700	$ 0.92	1.56%	11.59	1.22
CP	$ 23.14	I	50,200	$ 0.35	1.52%	11.37	1.09
CNI	$ 48.55	I	230,700	$ 0.69	1.42%	12.02	1.05
NSC	$ 21.04	I	1,560,900	$ 0.28	1.33%	13.38	1.42
CSX	$ 31.65	I	821,400	$ 0.40	1.26%	11.57	1.15
KSU	$ 11.76	I	286,700	$ -	0.00%	12.11	1.28
FLA	$ 27.70	II	28,700	$ 0.16	0.58%	N/A	N/A
PWX	$ 6.84	III	700	$ 0.16	2.34%	N/A	N/A
PRRR	$ 1.55	III	4,300	$ 0.03	1.94%	N/A	N/A
GWR	$ 20.10	III	36,200	$ -	0.00%	10.53	0.71
RRA	$ 7.13	III	112,900	$ -	0.00%	7.28	0.69
GMT	$ 16.75	Vendor	665,800	$ 1.28	7.64%	9.88	1.05
TRN	$ 16.79	Vendor	283,600	$ 0.24	1.43%	14	8
WAB	$ 13.03	Vendor	69,100	$ 0.04	0.31%	14.77	1.44
GBX	$ 10.23	Vendor	14,900	$ -	0.00%	19.46	8.48