THE RAILROAD WEEK IN REVIEW
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"What a remarkable level of enthusiasm among Senior Management presenters. CFO Munoz a delight." – Shortline attendee at last week's CSX Shortline Workshop

CSX held its annual Short Line Workshop in Jax last week and as luck would have it prior commitments prevented me from attending. However, notes from a select group of attendees who can be depended on for accurate feedback tell me it was informative and encouraging.

The response is not surprising. CSX brought out the best and the brightest to show where and how growth that is profitable to shortlines and CSX can be emphasized and nurtured. Focused presentations on Sales & Marketing, Service Design, Operations, Industrial Development, Car Management, e-Business, and Accounting all shared this common thread.

Chief Commercial Officer Clarence Gooden headed up Thursday's marketing panel with four of his Vice Presidential direct reports -- Chris Jenkins, Coal/Automotive; Kyle Hancock, Metals/Forest Products/Food & Consumer; Dean Piacente, Chemicals and Fertilizer; and Derrick Smith, Emerging Markets). Better asset turns – no surprise there – was a continuing theme.

Then the ops and service deign teams got up: Tony Tuchek, VP Northern Region, Mike Pendergrass, VP Southern Region, Jim Snyder, VP Network Operations, Chantel Campbell, Director of Merchandise Design, and Shelly Mast, VP Customer Service). It was particularly good news to learn that in 3Q06 CSX will debut an ISA Performance Measurement scorecard, now under development. And, before they're done, 35% of CSX' medium-sized yards will touch a shortline partner, taking down intermediate dwells still further.

The Trade Show – another CSX first -- was again a big hit, allowing for dialogue and an improved knowledge base across over three dozen different disciplines. Rounding out the first day, CEO Mike Ward gave his sixth consecutive annual shortline keynote address. He emphasized continuous, consistent improvement in operations backed up with CSX' focus on and commitment to profitable growth and reinvesting for growth.

On Friday, CFO Oscar Munoz (the only Class I CFO to ever to address any shortline conference) drilled down on the financials and got rave reviews. He was followed by Engineering's Hurricane Katrina recovery video and a presentation on Gulf Coast recovery efforts, now complete. Good news to the more than 225 attendees because, regardless of where your shortline lies, service interruptions on one part of the system invariably cascade down through the rest of the network.

Proof of this particular pudding is the fact that FY 2005 CSX same-store shortline volumes increased 4% and 6% in revenue. Recall that CSX itself was up 7% in revenue and down 2% in volume for the year (WIR 1/27/2006). This is after 14% growth in both shortline metrics in 2004, and is the fourth consecutive year of "same store" growth with the shortline industry.

Forest Products may not be out of the woods yet. On the STCC 26 side *Barron's On-Line* for Feb 16 opines that entering 2006 "opportunities for out-performance" would be limited. MeadWestvaco is embarked on a transformation into a consumer packaging firm and that could affect production and financial results. GP and Smurfit-Stone have upped container-board prices by $50 a ton. PCA is doing a bit better according to analysts.

The STCC 24 business is still there if you know where to look. My friends at Pennsylvania's North Shore Rail Group scored another coup with the delivery of their first inbound car to Savoy Furniture in Montoursville, PA on their Lycoming Valley Railroad (LVRR). This car of hi-grade plywood originated ion the CN in Longlac, Ontario and was unloaded at the LVRR Team track adjacent to I-80 and trucked to the plant a few miles away. The story is particularly encouraging because not all payers bought in easily at first. One of the biggest objections was the perceived rail transit time from western Ontario – four weeks.

As it was, the car arrived in seven days following loaded release at origin. Longlac is about 100 miles north of the northern-most part of Lake Superior and the route was CN Buffalo NS. The car ran on NS via Ashtabula-Conway-Enola-Northumberland to get to LVRR. It wasn't the most direct route as the crow flies but ample proof that scheduled service has more to do with performance than actual routing as viewed on a map.

Moreover, there are many signs that the consumer isn't dead yet, to quote the line from a man being carted away in Holy Grail. Home Depot reported Tuesday morning that its fiscal fourth-quarter profit zoomed up 23% on revenues up 16% system-wide and 5.5% in same-store sales. And even if there is a slow-down in new construction, HD says it expects strong sales will continue.

Customers (and not just contractors) spent more in transactions at Home Depot stores, with the average increasing 5.7% to $57.20 per ka-ching at the register. I think Jim Cramer got it right when he wrote that results like these "fly right in the face of" those who bemoan the tightening of consumer pocket-books, " the moribund credit markets, the toxic housing and resale market."

Anacostia Rail Holdings, operator five shortlines and a major presence in the shortline industry, has joined the AAR. In a joint press release Anacostia President and CEO Peter Gilbertson said, "We are pleased to become a full member of the AAR and look forward to working with the larger railroads of the U.S., Canada and Mexico addressing industry issues and opportunities." But there's more to it that that.

Three of Anacostia's railroads – the New York & Atlantic, the Chicago, South Shore & South Bend, and Pacific Harbor Lines – already operate like Class Is and face the same economic and commercial challenges the Class Is. The South Shore, for example, operates 182 miles of railroad, 80 of which it shares with "other freight railroads" and another 75 miles is shared with the Northern Indiana Commuter Transportation District.

In New York, the NYA came into existence to serve freight customers along the commuter-intensive Long Island Railroad. Pacific Harbor Lines is in reality the CSAO of the West, "providing rail transportation, maintenance and dispatching services to the Ports of Long Beach and Los Angeles" as well as dispatching some 65 trains a day. Ed Hamburg said in the AAR press release "We are delighted." Congratulations, all.

A tempest brews in Texas in a dispute between and among a shortline, a Class I and a major customer for both. An item in the 2/20/2006 *Argus Rail Business* reports that the STB has ordered the South Plains Switching railroad (SAW) in Lubbock to allow the West Texas & Lubbock (WTL), an adjacent shortline, to serve PYCO Industries. In FD 34802 dated 1/26/2006 the STB found that PYCO "has made the required showing that SAW is unlikely to restore adequate rail service to PYCO within a reasonable time and that formal intervention by the Board is appropriate."

The STB also determined that, since the order affects PYCO and not other SAW customers, there had to be assurances that "WTL can provide PYCO with service without unreasonably interfering with

SAW's service to the other shippers on this line." To this end, the STB "order[ed] the two carriers promptly to enter into operating protocols that will allow for safe joint operations on this line. We recognize that it will require good faith on the part of both SAW and WTL for this arrangement to work, and we expect both parties to act in that manner. Accordingly, both SAW and WTL will be required to report to the Board that the required protocols are in place."

The conflict comes in WTL's 2/16 filing that SAW is interfering with its operations and in SAW's rebuttal two days later. Clearly what's going on here does not create a positive picture of shortline relations with a major customer and the BNSF. And so it was that I made some calls to the BNSF, to the WTL, to the SAW and sent a copy of this note to the customer for comment. What I come away with is a huge opportunity for the shortlines and the BNSF to pull together for the *commercial* benefit of all.

Car supply, asset management, and customer management were the principal themes of the BNSF shortline meeting in October. A clear-headed approach to all the issues going all the way back to the terms of the 1999 line sale to the SAW is in the best interests of all. And perhaps the rationale is best laid down in the Amendment to the 1998 *Railway Industry Agreement* between the AAR and the ASLRRA as regards establishment of a "Railway Industry Working Group."

The RIWG was "created to address all policy aspects and issues relating to the application and effects of this Agreement." Furthermore, and this is why I think the RIWG may be the more appropriate avenue, the RIWG is meant to "provide a forum for the discussion of opportunities and concerns relating to issues between the Large Railroads and Small Railroads and to assure that the expectations of this Agreement are attained by having the terms of this Agreement consistently interpreted and applied throughout the railroad industry."

Perhaps it was Linda Morgan who, during her stint as STB head, insisted that business-to-business relationships ought to be worked out among the parties and that the STB would not be party to internecine squabbles. The result was, of course, the formation of the RIWG. Surely this team of senior representatives of seven Class Is and seven shortlines ought to be able to resolve the matter short of hundreds of pages of STB flings and untold legal fees.

GWR and RRA "same-store" carload are relevant in 1H06 for the same reason same-store counts are helpful for HD and RUTH – it's a measure of the strength of the existing franchise. And where one acquisition can increase the monthly car-count by 50% it's even more helpful to step back. GWR was up 31% in NA Jan revenue units overall with same-store vols up 10% yoy. RRA was up 7% overall in Jan with a same-store vols up 6% yoy.

Once again, I think GWR's contiguous model adds more commercial value than the more spread out model that RRA inherited from RailTex and other predecessors. However, as RRA slims down and closes in on the contiguous shortline model it too will add more value to shippers and shareholders.