THE RAILROAD WEEK IN REVIEW

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"We expect annualized real GDP growth of just 1.5-2.0 percent in the second half of 2011 and 2.0-2.5 percent through the end of 2012." -- Goldman Sachs ***Global Economics Weekly****, September 28, 2011*

Goldman continues, "Since this pace is below the US economy's potential, we expect the unemployment rate to be at 9.4% by the end of 2012, slightly above the current level. The large —and now growing—output gap will result in significant renewed disinflation, pushing core inflation from a peak of around 2.0% in late 2011 to 1-1/4% in late 2012." And...

> The US economy has not fallen off a cliff, despite the 'confidence shock' precipitated by the debt ceiling impasse, the downgrade of its sovereign rating and the recent turmoil in financial markets. We continue to see a one-in-three risk of renewed recession due to the worsening European financial crisis and the potential for greater-than-expected fiscal drag in early 2012 if the payroll tax cut is not extended for another year.

On the other hand, consumer demand still languishes, says this week's "Heard on 24th Street" from Credit Suisse. The context of the note is mainly air freight and package however...

> *Consumer Demand Unlikely to Take Off*. We analyzed a series of key consumer indicators and compared current conditions to 2H09 (when overall consumer demand was still in the recovery phase). We find that in nearly every case, conditions have deteriorated significantly. The threat of a recession is significantly greater; consumer confidence and expectations have plummeted; disposable income growth has turned negative; unemployment remains stubbornly high; and the stock market has taken a nose dive. This does not bode well for near-term consumer spending.

How bad is it? The C-S note lists changes Sep 09 vs Sep 11 in eleven "Key Consumer Demand Indicators" from Recession Probability and Consumer Confidence all the way down to Presidential Approval Rating. Six are "worse," three are 'unchanged and just two (unemp rate and private payroll growth) are "better."

The way I see it, short lines, switch carriers and regionals where revenue gains are a direct function of volume gains and where there is no pricing power are best served building franchises heavy in the non-cyclical commodities -- chemicals, coal, grains, and aggregates -- that comprise more than half all shortline YTD carloads per RMI's RailConnect Index for Week 39, Oct 1. (Yes, grain is off, but that has a lot to do with the dearth of Kansas and Oklahoma wheat due to the worst drought in years.)

Value Line corroborates. They measure stocks on timeliness, safety and technical trends and the top 15 groups for Timeliness includes companies in Integrated Petroleum (Exxon, Chevron, Hess), Packaging (MeadWestvaco, Ball Corp.), Chemicals (DuPont, Dow, Huntsman), Auto

Parts (BorgWarner, Tenneco), Steel (ArcelorMittal, Worthington) and, yes, Railroads. Two industry groups not in the top 15 but critical to short lines nonetheless are Oilfield Services and Petroleum Producing industries. They are ranked 56 and 57 for timeliness but are long-term attractive thanks to rising energy demand and capital appreciation.

Amtrak's Vermonter is running again! Christopher Parker, Executive Director of the Vermont Rail Action Network, informs us that October 1st was the first day of rail service on the whole route the length of Vermont. Amtrak had provided bus service as a substitute while track was rebuilt and flood damage from Irene cleaned up.

Parker continues, “When you take your first ride you will immediately notice how much smoother is the ride with new welded rail. The job of installing the rail is almost complete with only a bit left in Vernon to the state line. Surfacing work continues south of White River Junction at night.

“RailAmerica’s New England Central Railroad, the freight railroad which owns and dispatches the tracks used by the Vermonter north of Palmer MA, deserves a lot of credit for a heroic effort after some pretty significant devastation. Contractors R.J. Corman, Engineers Construction and others assisted and the Vermont Agency of Transportation played a huge role in facilitating the work, starting with helping to provide access in the first place.”

NECR’s mid-section, roughly White River Junction to Essex Junction, VT got it worst, with downed trees, washed out track and knocked down bridges. It took a team of close to 90 people and 15,000 tons of ballast to restore rail service on the NECR. Several railroads in the region, including Canadian National, Pan Am Southern, Amtrak, and Providence & Worcester, provided much needed equipment to transport large volumes of rock and fill.

Local Vermont vendors worked tirelessly to provide support in the form of crushing stone for ballast, trucking, and railroad contract services. “We greatly appreciate everyone’s efforts and team spirit,” said Charles Hunter, RailAmerica AVP of Government Affairs. (And for more from Charles and his Amtrak counterpart, Paul Vilter, come hear our panel at the *Railway Age* Passenger Trains on Freight Railroads conference in Washington Oct 24, 25.)

The FRA on Thursday placed a notice in the *Federal Register* about its “Safety Advisory 2005-04” advising “shippers, consignees and railroads of the dangers of allowing ‘time - sensitive’ chemicals to remain undelivered” beyond their scheduled delivery date and “to recommend enhanced procedures to avoid such occurrences.”

It appears that the event triggering this Safety Advisory took place on RailAmerica's Indiana & Ohio Railway in Cincinnati six years ago. A carload of styrene was interchanged to IORY from NS in January, 2005, sat undelivered for seven months, essentially became unstable and caused a release. The FRA, according to the current *Federal Register* item, "found no records indicating that the IORY had attempted to contact the customer to arrange for delivery."

The *Register* then cites chapter and verse of the 49CFR and OT-55H that make it the railroad's responsibility to keep TIH cars moving and consignees notified. And the proposed Safety Advisory seeks to underline these provisions.

To put the 2005 styrene release incident in context, recall that RailAmerica at that time was still under the previous owners (Fortress closed on its RA acquisition in Feb, 2007). Moreover, at that time the short line industry lacked sufficient oversight, tracking and reporting protocols for time-sensitive and hazardous materials.

More recently RailAmerica continued to assert its safety leadership in the short line industry when, in June 2009, its railroads issued Tariff 1000, TIH/PIH Procedure addressing the concerns of toxic materials shipments.

> Item 1000 – Procedure on Delivery and Placement of Cars: Customer shall be prepared to receive carloads of TIH/PIH commodities immediately upon notification of availability at destination by carrier railroad. There will no free time granted to customer once notification takes place. Charges will begin at 12:01AM the morning after customer tender/notification or the first day of deliverable service, whichever occurs first. If a receiver/customer or receiving location is unable to accept a TIH/PIH commodity carload when it is first tendered/notified and available for delivery, and RailAmerica must then hold the car(s) in its rail facilities, a charge of $1,000 per car, per day or portion thereof will be assessed until the car(s) are placed at its billed destination.

RailAmerica's railroads instituted new protocols in handling TIH movements, mandating that local RA crews are to make a special inspection of each TIH/PIH car once it is received at interchange. Such cars are then moved in special train service, with no more than three TIH cars per train. The train is also operated at a safer, lower speed.