

# THE RAILROAD WEEK IN REVIEW

## May 10, 2013X

*“You really have to understand the company and its competitive position -- that’s not disclosed by the math. We know that Burlington Northern will have a competitive advantage for years.” -- Charlie Munger, Berkshire Hathaway Annual Meeting, May 4.*

**BNSF files a 10-Q when Berkshire reports** and a doozie it is. Revenue up 5.6 percent to \$5.3 billion on 2.4 million revenue units, up 3.2 percent, beating out second-place gainer NS by a tenth of a point. Combined merch and ag carload revs increased 7.8 percent, second only to CP’s 24 percent gain, though the BNSF number excludes automotive as that group is buried in “consumer products.” Merch carloads -- industrial and ag products only -- takes the brass ring, up 5.6 percent to 692,000 units. Operating income increased 16.0 percent to \$1.5 billion; the OR improved 249 basis points to 72.2 percent.

Within the industrial products sector, crude-by-rail is the big winner, with petroleum products up 80.8 percent to more than 120,000 units while generic chems actually dipped 3.6 percent to 103,000 units. Sand/gravel gained 16.2 percent on frack sand; lumber increased 12.0 on housing starts in the PNW and Texas. The IP group as a whole was up 14.3 percent to 448,000 units but ag including grain-mill products slipped 7.2 percent, not unexpected given Steve Bobb’s predictions (WIR 4/5/2013, second bullet point). Intermodal/auto was flat; coal was off 3.4 percent on easing year-over-year comps.

In that same commentary, I noted the BNSF emphasis on velocity. Here’s BNSF running three percent more revenue units yet holding fuel gains to 2.5 percent, comp to two percent, and dropping two points in equipment rents. I still see that Katie Farmer chart from a shortline meeting some years ago with shortline dwells ranging from four to fourteen days. And I know from some conversations at the ASLRRA Gala in Atlanta last week the usual suspects are not improving.

To drive the point home, let me offer a Buffett quip from Saturday’s Q&A: “We are looking at businesses exactly as if somebody came in and asked us to buy the whole business.” And that questioning attitude extends to companies Berkshire does business with. If that vendor isn’t sufficiently solid that Berkshire would want to buy it, then maybe Berkshire -- and by extension BNSF -- will want to look elsewhere for a vendor of the goods and services in question.

With IP and ag up 14 percent, even with a big push from petroleum, it’s clear to me that BNSF is a merch carload powerhouse, generating 43 cents of every revenue dollar, close to double what coal brings in, and nowhere near as volatile as coal given the EPA and other external follies.

**BNSF may well be the Oakland A's** of the railroad community. I say Oakland because I see a parallel between the use of stats in the Money Ball story of the A's and what BNSF is doing. Billy Beane's thing was about finding players who get get on base -- by any means. (Miami recently clobbered the Phillies 14-2 doing exactly that. In the first inning Roy Halladay waked three and two batters got on being hit by pitched balls -- can you say crowding the plate? One Miami player was up four times and got hit twice, walked once, and flied out the fourth time. Scored twice, too. That's the guy I want on *my* team.)

So what's the railroad parallel? Revenue-ton-miles. You can drag all the cars you want, but if they're not producing the revenue -- getting to first -- you're not going to win any operating income contests. The way I see it, every railroad has assets, shareholders equity (skin in the game), route-miles and employees (locos, freight cars, switch-stands -- whatever, pick one). Green shading is first place; red is last place.

|  | BNSF     | UNP      | CNI      | CP       | CSX      | NSC      |
|--|----------|----------|----------|----------|----------|----------|
| Route miles  | 32,500   | 32,615   | 20,400   | 14,700   | 21,500   | 21,500   |
| FTEs**   | 39,300   | 48,200   | 23,000   | 16,100   | 28,200   | 30,000   |
| Equity   | \$34,329 | \$19,877 | \$11,018 | \$5,097  | \$9,002  | \$9,760  |
| Assets \$mm  | \$72,016 | \$47,153 | \$26,659 | \$14,427 | \$30,571 | \$30,342 |
| Rev Units (000)                                      | 9,622    | 9,048    | 5,059    | 2,669    | 9,048    | 7,107    |
| RTMs*  | 648,000  | 521,100  | 201,500  | 135,000  | 219,600  | 185,600  |
| RTM/mile   | 19.94    | 15.98    | 9.88     | 9.18     | 10.21    | 8.63     |
| RTM/FTE  | 16.49    | 10.81    | 8.76     | 8.39     | 7.79     | 6.19     |
| RTM/Equity\$   | 18.88    | 26.22    | 18.29    | 26.49    | 24.39    | 19.02    |
| RTM/Asset\$  | 9.00     | 11.05    | 7.56     | 9.36     | 7.18     | 6.12     |
| RTM/Rev Unit   | 67.35    | 57.59    | 39.83    | 50.58    | 24.27    | 26.12    |
| *RTMs in millions; BNSF 2011 per 2012 AAR Fact Book  |          |          |          |          |          |          |
| ** 2011 FTEs from AAR 2012 Fact Book, to nearest 100 |          |          |          |          |          |          |

BNSF "went private" and disappeared from Wall Street's view. By going private, Carl Ice and company now can shift and shape rail operations to get the most men on first (RTMs) for the money available. To be sure, the decimals can get tricky. We're looking at millions of RTMs per thousands of carloads but millions of RTMs per individual employee or route-mile. What really jumps out for BNSF in this example is length of haul -- nearly triple the RTMs/unit that CSX gets. And five times the RTMs per full-time employee of NS. Amazing.

**WIR is taking the short-form** this week and next due to away games. Hope to be back to the usual three-page-plus format by May 24.

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