RAILROAD WEEK IN REVIEW

September 28, 2018

“If I had it to do over again, we would have done a much better job with our short lines — which handle 20 percent of our business — pre-blocking by destination and making more joint sales calls.” — Clarence Gooden, retired CSX Vice Chairman, at NEARS Fall 2018 Conference

The Northeast Association of Rail Shippers (NEARS) this week held its annual fall conference in Tarrytown, NY. With the timely theme of “The Capacity Crunch Conundrum” (try to say that three times fast), the conference featured panels and presentations covering a wide range of topics. And, as a special treat, we heard Clarence Gooden, retired CSX Vice Chairman, hold forth on where the railroad is, how it got here, and where it may be going.

Rail Analyst (and NEARS President) Jason Seidl hosted his usual web-driven survey of the room and found that, in his words, “Shippers were fairly positive on the economy, though several noted a recent lull, which may be the result of a pull forward of business due to tariff concerns.” The survey also revealed that many shipper representatives have seen an improving business environment and that, even given the tight truck market, three quarters of those in the room hadn’t made any significant truck-rail shifts.

I came away with the sense that the presenters as a whole confirmed previous WIR observations that car supply, transit times, lease cost/ton, switch frequency, and reliability remain serious concerns for customers in the carload commodity sectors. As one would expect, Precision Scheduled Railroading was mentioned more than once in the context of addressing these concerns.

Asked specifically about carload trip plans, Norfolk’s Jim Schaaf, Group VP for Industrial Products, confirmed that NS is working toward providing carload trip plans from release to placement and then measuring compliance against these plans. He added this will be a true dock-to-dock process, even if the one or both ends of the move are on a non-Class I partner railroad.

Back to Clarence. A dear friend for many years, Clarence held forth on topics ranging from Lessons Learned to the resurgence of paper as a packaging medium preferable to plastic, and to the shift in global demographics that will shape the transportation business for generations to come. Specifically, Clarence feels that the “Amazonification” of the supply chain is a powerful motivator for the railroads to embrace automation (track crews from 100 men to ten, e.g.) in order to facilitate the fluid last-mile performance Amazon Prime customers rely on.

His remarks on paper vs. plastic were music to many railroad ears. Says he, “Millennials and centennials (those born after 2000) are very conscious about what’s happening with plastics” and paper packaging is the coming thing. Starting with the famous “Plastics” film clip from *The Graduate*, Clarence said that over the next 20-40 years paper will make a big comeback. More of the Prime stuff coming to his door is in a paper, not plastic, package that is easier to open and disposable. Paper and packaging in the future will change dramatically and Amazonification will be a big part of changing the way business is being done.

Railroad speed and reliability will no longer be an option, but rather a requirement as global e-commerce becomes the norm. Even though rail does not directly serve the big distribution centers, PTC will add capacity — more trains closer together — meaning better speed and reliability for the trailers and containers that *do* serve the DCs, assuring a railroad role in the reinvented logistics chain. In sum, those in the room got a lot to think about and build on. Thanks, Clarence.

A pair of September 24 notes from Stifel touch on recent developments in the Oil & Gas Exploration and Production arena. Following an E&P conference they sponsored in Midland, Stifel has “a greater conviction the anti-Permian trade is nearing the end of its course.” Starting in two or three months we ought to see “several upstream companies formalize 2019 plans.”

> Most agree with our assessment that the proliferation of in-basin sand mines is creating an oversupply of frac sand that will severely weigh on both Northern White (NWS) and in-basin sand prices…
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> We reiterate our cautious outlook for frac sand providers, but concede that any signs that large players are shunning in-basin sand for higher-quality NWS, or any evidence that NWS is leading to materially better well performance, would be net positives for NWS providers. That being said, recent conversations with industry participants support our view that sand prices are falling.

Soybean growers continue to get hammered by the US trade restrictions. Dennis Gartman reports in his eponymous Gartman Letter Sep 27 that Brazil will send record amounts of Brazilian beans — some 12 to 14 million tonnes (a tonne is 2200 lbs) — to China starting in a few weeks. Gartman adds,

> Last year Brazil shipped just a bit less than 9 million tonnes to China in the entire final quarter, well above the average of 3.7 million tonnes the country had shipped during that quarter from 2010 through 2015. Thus, it does indeed appear that China is getting the beans it needs from US off-shore competitors. This cannot play well with America’s farmers.

Indeed not. The *Wall Street Journal* reported just yesterday that the Trump administration efforts to compensate US farmers for damage the tariffs are doing isn’t doing the job. “Many farmers say the payments won’t make up for lost sales to China and other foreign markets.” The huge amounts of product planted for export are filling up the bins, and, as supply exceeds demand, prices go down and farmers hold their harvests until prices improve. Not good for railroads.

Cherilyn Radbourne, railroad analyst for T-D Securities in Toronto, sat down recently with CN and came away with the sense that the railroad is well-positioned to cope with next year's burgeoning demand for its service. Current RTM trends lag expectations a bit (it's still up five percent) due to the extensive track upgrades — 11 out of 27 projects are already complete, and a further 11 should be completed over the next week or so.

She notes that CN not only benefits from the strong North American economy in an environment conducive to demand pricing, but also "enjoys a number of opportunities for company-specific growth" at the Prince Rupert port, where CN is the only railroad in town. Cherilyn adds that the CN crude-oil business could well run to more than 75,000 cars a year starting next month. CN is her top pick among the Big Five Public Class I rail stocks.

Iowa Interstate Railroad has promoted Joe Parsons to President and CEO. Joining IAIS in 2013 as Chief Operating Officer, he was promoted to GM four years later. Before moving to IAIS, Parsons had acquired more than 10 years of railroad management experience at Class I and short line railroads, including two years as AGM for the Chicago, Fort Wayne and Eastern.

Parsons began his railroad management career with Norfolk Southern in the transportation department, working in various locations before being promoted to terminal superintendent in Cincinnati, Ohio. H earned a bachelor's degree from West Virginia Wesleyan College and a Master of Business Administration from the University of Iowa Tippie College of Business.

RailTrends 2018 is coming to the Times Square Marriott in NYC November 29-30. Yes, that's two months away, but given the way calendars have a habit of filling up quickly, it's appropriate to note now the "Short Lines' Competitive Advantage" panel. Holding forth will be chief marketing officers from four operating companies: Anacostia (Eric Jakubowski); GWR (Michael Miller); Pan Am Railways (Mike Bostwick); and Watco (Stefan Loeb).

Each of these outfits has racked up an exceptional number of successes in finding more business from long-standing customers, creating new customers, and helping Class I partners identify better ways to create value out of their respective books of business. This is the 14th consecutive running of RailTrends, and I can guarantee you'll get your money's worth — I've been to most of the 13 previous iterations and have always come away encouraged and refreshed.

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