

THE RAILROAD WEEK IN REVIEW

September 25, 2015

“Quantitative Easing enabled many companies to get a lot of cheap credit they shouldn’t have gotten; all we’re seeing now is price validating and showing you the way things really are.” — John Burbank, Passport Capital

When the FOMC punted on rates last Friday it didn’t do the railroads any favors. Frankly, I wasn’t surprised they blinked. Liz Ann Sonders, Chief Investment Strategist at Charles Schwab & Co., wasn’t either. She writes,

The FOMC did acknowledge the improvement in economic and job growth: “On balance, labor market indicators show that underutilization of labor resources has diminished since early this year.” But it also noted the still very low levels of inflation and global turmoil, which remain a concern: “Recent global economic and financial developments may restrain economic activity somewhat and are likely to put further downward pressure on inflation in the near term.”

To me, it seems truly a mixed message. The Fed says, “underutilization of labor resources has diminished since early this year,” and yet “economic and financial developments may restrain economic activity somewhat.” Restrained economic activity does not lead to greater utilization of labor resources, so such diminishment as we have seen will likely be fleeting, in my opinion. So with the Fed’s accommodative doves outnumbering the more aggressive hawks, the Fed punts on monetary policy, giving us, groundhog-like, six more weeks of economic winter.

Over at *Seeking Alpha*, we get “Thirteen Economic Charts That Wall Street Doesn’t Want You To See,” with each example running counter to the Official Narrative. A sampling: since 2009 average wage gains have been stagnant; worker participation has dropped 300 basis points to 63 percent in eight years; year-over-year consumer spending was down five of the eight months Jan-Aug 2015; the 1.36 Inventory-to-Sales Ratio is the worst since 2009. And so on.

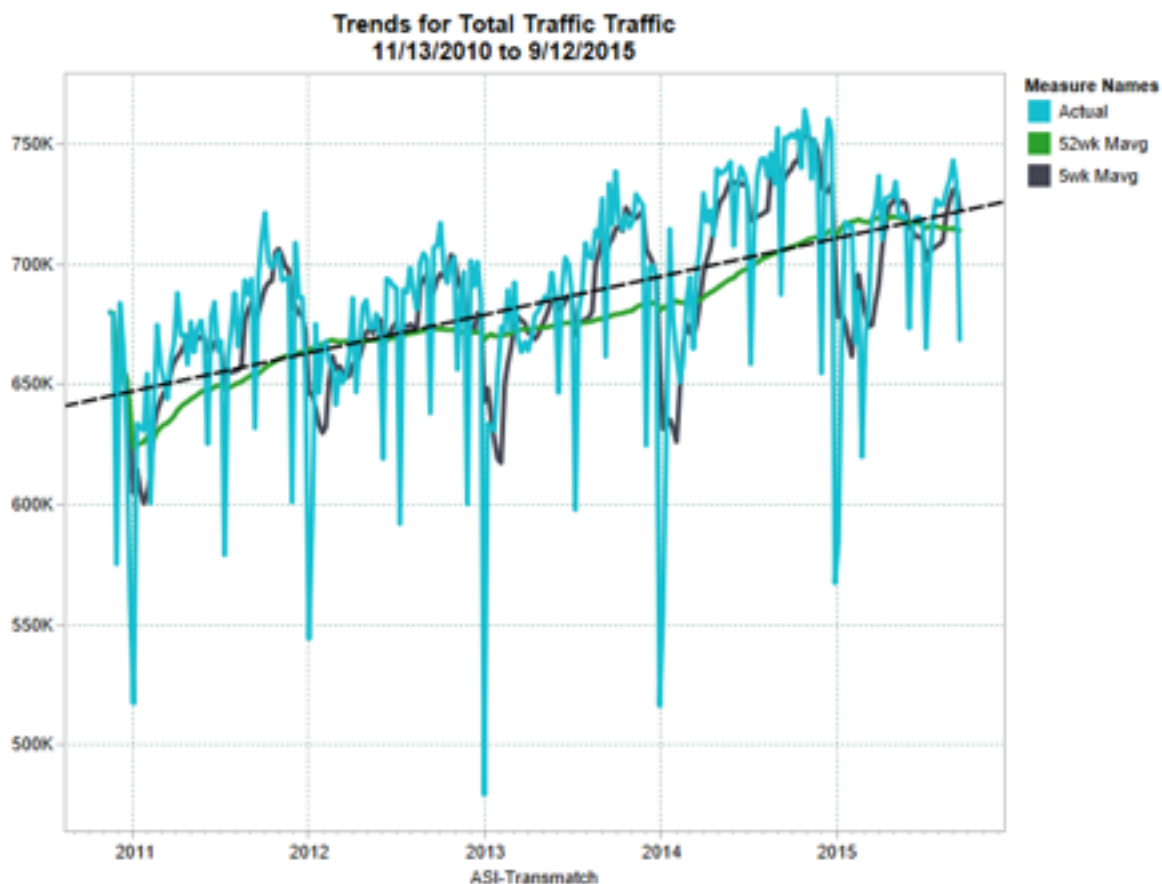
With the consumer hunkering down and inventory eating up working capital, it follows that there is less need to move goods from one place to another. AAR total revenue units through September 12 are down a point from last year (which was up four percent over 2013). Year-to-date take-aways: Coal is down everywhere but BNSF, where it’s the largest percentage of total vols. (BNSF has always been bigger than UP in western coal. UP has simply had a steadier decline than has BNSF, possibly on vols coming down for Colorado/Utah coal.)

AAR chems (strictly STCC 28; 29s are in petrol with crude oil) are up a point. Aggregates - crushed stone, sand and gravel - include frac sand, a measure of the carrier’s OGE (oil and gas

exploration) involvement, and are up a point but metals are down 11 percent. Ag products (grain, sweeteners, oils, and canned goods etc.) are down a point. Waste and scrap are down, too.

By railroad, BNSF is up a point in total carloads to UP's down 13 percent. CSX and NS look a lot alike in the carload sector; NS is the stronger intermodal performer by far — containers are 51 percent of revenue units, more than any other Class I. CP is better off than CN in year-to-date volume gains with its strong bulk franchise; however, CN is the stronger intermodal player.

You can't make this stuff up. You can see how every prior year started out slow in terms of year-over-year revenue-unit growth and gradually increased as the year progressed. Not so 2015, which looks like the 2013 first half, except that was a serious winter of discontent; we've had no such excuse this year. So if the Dow Theory is right, and rail traffic is a leading economic indicator, we can expect 2016 will be another year of less-than robust growth.



Mark Manion is decamping from NS after forty years of service, taking his retirement February 1, 2016. As Chief Operating Officer, he brought an open, non-confrontational style, seeking always to provide operations personnel the tools to do the job better and more safely. I've been particularly impressed with the way Mark made safety a personal matter for every employee and instituted a behavior-based management approach to leadership development.

Manion joined NS in 1975 as a management trainee. He served in a range of operations positions, including trainmaster, superintendent, general manager, vice president mechanical, and senior vice president transportation operations, being tapped EVP Ops in 2004. I've enjoyed working with him on strategic operational matters that affected short lines and will miss his candor and his objective, fact-based management style.

Mike Wheeler, presently vice president engineering, will succeed Manion in February, but first will be SVP Ops starting October 1. Though he's been the main NS track guy since 2012, he did a stint as VP Transportation starting in 2009, so is already qualified there. Wheeler joined NS in 1985 as a research engineer and has served in positions of increasing responsibility in mechanical and transportation management slots. Philip Merilli steps up to VP Engineering, reporting to Wheeler and based out of Atlanta.

Elsewhere, Cindy Earhart becomes EVP Admin and Chief Information Officer, adding the new responsibility for Information Technology following the October 1 retirement of Deb Butler. Also on October 1, Wick Moorman passes the CEO baton to Jim Squires, but will stick around as a director until he officially retires Dec 31.

RailTrends 2015 has announced the starting lineup. The show runs Nov. 19-20 at its usual venue, the W New York Hotel on Lexington at roughly 50th. All the usual suspects will present: AAR's Ed Hamberger, STB's Dan Elliott, ASLRRRA's Linda Darr, RAC's Michael Bourque, and RSI's Tom Simpson. Interim Federal Railroad Administrator Sarah Feinberg has agreed to present as well. You can expect this august group to touch on a broad range of vital issues, from safety and infrastructure to PTC, rail-car design, and the truck size and weight question.

CSX Chairman Michael Ward leads off as the Progressive Railroading/RailTrends 2015 Railroad Innovator Award winner. The international lineup of speakers includes senior railroad executives from the US, Canada, Mexico, and Australia. For the shortline and regional railroads, we'll hear from T.J. Gallagher (GWR), Rick Webb (Watco), John Fenton (Patriot Rail), and Kevin Shuba (OmniTrax).

Covering the intermodal beat will be UP's VP and General Manager-Intermodal John Kaiser and XPO (née Pacer) Logistics President-Intermodal Paul Smith. FEC (a significant intermodal player itself) President Jim Hertwig will bring us up to date on his road's experience with gas-powered locomotives. All Aboard Florida President Michael Reininger will provide insights on providing a passenger rail product in a car-oriented state. And that's just for openers. Watch this space for more line-up details.

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