RAILROAD WEEK IN REVIEW

May 11, 2018

"First quarter railcar orders of 10.3k improved sequentially (+22% Q/Q) to their highest level since 2015. The increase was driven by boxcars (+2.1k), small cube covered hoppers (+1.1k, mostly frac sand), tank cars (+1.1k), and gondolas (+0.7k, steel-related). — Bascome Majors, Susquehanna Financial Group

"What makes acquisitions so attractive? Debt is still cheap and the global economy is growing. Companies have cut costs and increased margins, but investors are looking for revenue growth, and acquisitions can provide that." — Barron's, May 10

BNSF brought up the markers on — shall we say — an interesting quarter. With all the Class I results in, one can see that BNSF blew away the competition in a number of key metric percentage gains: revenue, revenue units, merchandise carloads, and merchandise carload revenues. BNSF held the line on RPUs, up less than two points to UP's five.

The financial reports are slim, with only four commodity groups — coal, industrial, ag, and consumer (intermodal and auto) reporting. Total freight revenue increased seven percent to $5.3 billion on 2.6 million revenue units, up five percent as RPU gained two points. Total revenue including "other" rose eight percent to $5.6 billion. Operating expense gained nearly as much so ops income grew 11 points to $1.7 billion with an OR of 68.9, slipping 59 basis points.

The consumer group represents 35 percent of total revenues and about 90 percent of that is intermodal. Revenues increased 11 percent to $1.9 billion on 1.4 million units, up six percent. Industrial products revenue gained 11 percent on nine percent more volume; ag scraped by with a four percent revenue gain on six percent more loads (ag and industrial are about 45 percent of revs). Coal revenue slipped a point on a two percent volume drop.

Net income before taxes increased 13 percent to 1.5 billion; after tax the net was up 37 precent to $1.1 billion. Cash from operations remained at $1.6 billion, though capex came down 16 percent to $565 million; free cash flow jumped 13 percent to a $billion-one with capex 10 percent of revs, down from 13 percent a year ago. Fuel surcharge collections ran half again what they were last year, so if you back out FSC to arrive at pure carload revenue, it's $6.3 billion, up seven points, and the OR would be 65 bips worse — 72.9 vs 72.2.

You have to go to the AAR carload reports to parse the commodity trends. Ag products includes the grains, grain mill products, and farm products ex-grains (STCC 20 processed foods are in the industrial group). The IP group is where it gets interesting, with everything from industrial chemicals to crude oil and STCC 29s, from forest products to metals — some 17 commodity lines. Of these, all but two — boxcar foods and farm ex-grain — showed increases. But I'm not really concerned — the two misses together account for less than two percent of total loads.

For the quarter, the seven Class Is in the US and Canada rang up $22 billion on freight revenues on nearly 11 million loads, of which merch carloads — all but intermodal and coal, but including auto — accounted for some 44 percent. So even though intermodal is the big grower, I'm not quite ready to give up on the unit train and single-carload models just yet.

OmniTRAX is the first short line to join the Blockchain Alliance (BiTA, WIR May 4). This is good news indeed. As I noted last week,

> To be competitive in supply chain management and inventory control, transportation suppliers must allow customers to eliminate time-consuming tracking calls, know where their loads are 24/7, and have those loads tracked through the vendors' event-recording systems. Seems to me the BiTA bloc chain technology can collect the data, massage it, and give freight customers the management tools that add value to their customer offerings.

OmniTRAX CFO Hubert Gassner gets it. "We want to have a positive impact on efficiency, security and transparency for our customers and partners, and that's what blockchain offers. It is critical for the short line and regional railroad sector of the transportation industry to have a seat at the table when supply chain technology standards that can enhance performance are discussed."

Exactly. Moreover, since Blockchain is really a data warehouse of events, it is critical that short lines and Class Is report events accurately. My feedback says they are not. I'm hearing about Class I crews logging shortline interchanges as complete, when in fact either they took place at a later hour than reported, or sometimes skipped entirely. I'm also hearing about short lines that have resisted the whole ISA concept, saying, " The class I ignores them, so why bother?"

Here's why. My take is BiTY will help short lines stay ahead of customer requirements and Class I performance in meeting those requirements. I see active and workable ISAs as critical. Yet feedback from Class Is tells me there are short lines where ISAs are either ignored or missed badly. And until short lines and class Is start interchanging according to the ISA, scheduled railroading and car-based trip plans will all be for naught.

Your assignment: make sure you have a current, workable ISA. Then start tracking Class I (and your) performance against it. Here's a simple spreadsheet you can use to keep score. The NS Annual Shortline Meeting is in two weeks and I'm sure it will be a Hot Topic. Be prepared.

The Delaware-Lackawanna Railroad, one of four railroads in the Genesee Valley Transportation portfolio, celebrated its 25th anniversary May 5 with an office car inspection trip for friends and family. The special train was led by a pair of spotless Alco Centuries followed by five heritage cars, with GVT's heavyweight Pullman business car Erie 2, an Erie original, bringing up the rear.

The 120-mile trip from Scranton east to the Delaware Water Gap operated across 88 miles of the former DL&W main line, once a three and four-track railroad and still one of the best-engineered properties you'll see, complete with signal bridges spanning the entire roadway. (Railroad President Willam Hayes Truesdale in 1900 said he wanted a "straight, flat, and fast railroad," according to a Steamtown video on the subject.)

Though the railroad is now single-track and with the wayside signals dark, and local freights are the only trains, the D-L is a busy place. Three relatively new — in the last 10 years or so — customers are a flour mill bringing in Midwest and Canadian wheat for milling, an LPG distribution facility, and a lumber treater receiving southern yellow pine (pictured).

The principal Class I connection is Norfolk Southern at Scranton, and the commodity list runs the gamut from the grain, lumber and PPG mentioned above to paper, plastic, clay, and even some coal. Carload volumes are such that my Rule of 100 for a successful short line is handily met.

The D-L uses tracks that have been owned by the Pennsylvania Northeast Regional Railroad Authority (PNRRA) for a quarter century. GVT, established as Genesee Valley Transportation by David Monte Verde, Michael Thomas, and John Herbrand, has been in the railroad business since 1985. The other properties are in New York. The Depew, Lancaster and Western operates two divisions with terminals in Batavia and Lancaster; the Falls Road runs in westernmost NY along Lake Erie; and the Mohawk, Adirondack & Northern, headquartered in Utica and serving the Mohawk Valley and the Adirondack Region.

I think that D-L's big selling point is proximity to Northeast Corridor markets without that area's congestion, and the continuity afforded by the long-term partnership between the railroad operator, the D-L, and the property owner, the PNRRA, ably led by Larry Malski. The success of the line goes to show what one can do with a carload railroad and an intense focus on the customer.

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