RAILROAD WEEK IN REVIEW

May 25, 2018

"Above two percent inflation might make the Fed happy but won't be helpful to an economy that is dependent on consumer spending." — Peter Boockvar, Bleakley advisory Group, quoted by Art Cashin, May 24

"A blockchain is a continuously growing list of records, called blocks, which are linked and secured using cryptography. Each block is resistant to external modification of the data, and is managed by a peer-to-peer network with members adhering to a protocol for inter-node communication and validating new blocks." — Wikipedia

Blockchain is entering the railroad conversation as a means for providing everybody with an interest in a particular freight move access to all information concerning that move (WIR 5/4). We heard a lot about the importance of technology in managing the railroad process at this week's NS Shortline Meeting (full report coming next week), but the car has to move for there to be data on it. That's one reason there is an emphasis on operating to plan and event reporting.

To see what the competition is doing, check out the truck Load Board at dat.com [1] to find trucks for your loads, run pricing samples for commodity O-D pairs, and track loads. Try that with the present railroad offering (none). CSX touts their new carload trip plan process, yet the car hits their system at interchange with you, not when the customer releases the car to you. NS doesn't yet track shortline interchanges with the Local Operating Plan Adherence (LOPA) tool, even though LOPA's been around 20 years.

The newly announced Blockchain Alliance seeks to merge movement data so everybody can can see everything (WIR 5/11). A recent investor note from Cowen adds a caveat, however. "Blockchain offers intriguing possibilities but Enterprise adoption is limited, likely 5+ years out. Although not a panacea, Blockchain has a strong fit around supply chain use cases."

By its very nature, the Blockchain data series is secure, being a distributed computing system, and making this process suitable for the recording of events, such as you'd get from an event report or AEI reader. Yet a fair number of short lines tell me they don't believe in the ISA because, even though they show up according to plan, the Class I doesn't. So why bother? Which proves once again that all the tech tools are worthless if you're not On Plan.

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[1] I went to their website for a test inquiry. Had an email response in 15 minutes.

AAR carloads for Week 19 increased 3.2 percent to 14.2 million units. Intermodal gained nearly six percent, and represents half the total volume. Merchandise carloads — everything but intermodal, auto, and coal — rose a paltry one percent. We keep hearing how scarcer truck capacity is creating new railroad opportunity (see below) and would hope some of this could rub off on the merch carload sector. It isn't, and I see two reasons why.

Commodity	2018	2017	Delta	Pct Tot
Total Units	14,274,661	13,817,872	3.20%	100.00%
Intermodal	7,133,627	6,727,010	5.70%	49.97%
Auto	533,627	551,770	(3.40%)	3.74%
Coal	1,794,412	1,780,057	0.80%	12.57%
Merch Carloads	4,812,995	4,759,035	1.13%	33.72%
Source:AAR				

First, Class I sales coverage has to be lacking because planners seem to be surprised at volume growth spurts. You can't know what customers are planning unless you ask, and you can't know whom to ask if you're not covering the account. Thus any change in past patterns throws a monkey wrench into asset planning, from crews to locos to capex.

Second, short lines *are* calling on customers and are intimately involved with those customers' forward supply chain and transportation needs. But short lines managers continue to relate instances where they've taken rate requests to Class Is only to be turned down. One gets a back haul priced the same as a front-haul. Another sees interchange understandings changed by the Class I with no regard for the effect on customers. Still another says he needs a new track lease agreement to build the franchise and his inquiries go unanswered.

This is unfortunate. Railinc reports April shortline carloads up three percent, with gains in every merchandise commodity but non-metallic minerals (all STCC 14), pushing the merchandise carload commodities up nine percent YTD. So, even though I'm comparing April Short lines with industry YTD, the fact remains that short lines are growing merch volumes faster than the Class Is. And that make one ask why Class I middle managers are so resistant to shortline initiatives.

Commodity	2018	2017	Delta	Pct Tot
Total Units	352,781	343,665	2.7%	100.00%
Intermodal	38,150	50,360	(24.2%)	10.81%
Auto	9,021	9,531	(5.4%)	2.56%
Coal	23,217	24,159	(3.9%)	6.58%
Merch Carloads	282,393	259,615	8.8%	80.05%
Source: Railinc				

Even more puzzling, Norfolk's Jim Squires calls the present transportation environment "most conducive" for top-line growth (WIR 5/11). Could be. The *Cass Truckload Linehaul Index* in April showed pricing up eight percent year-on-year – the largest gain since the base year of 2005, and the strongest normalized percentage level since deregulation.

Says *Railway Age*, "Long-haul trucking capacity has been in a vise thanks to a shortage of drivers, higher diesel fuel prices and a surging economy boosting retail sales." We're seeing the law of supply and demand working well, with intermodal rates nicely up this year. So why are Class I managers pushing back on the very commodities senior management (not just NS) says it needs to grow?

OmniTRAX continues to expand its logistical service business. Their Energy Solutions (OES) division — active in the proppant supply chain support of oil and gas exploration — has reopened three silos at its Cotulla, Texas, terminal. This facility is one of the largest of its kind in the Eagle Ford basin, with enough storage space to take 240 cars at 100 tons each, with more than 18,000 feet of rail car capacity. The reopened silos will have a positive impact on the local economy and will reduce truck traffic in the region.

OES President Pierre Luc Mathieu says reinvestment of this sort provides enhanced customer service in the Eagle Ford other OEP basins. He cites a reputation of performance and stability that customers and local communities rely on. This is good news because I think short lines are uniquely suited to adding local logistical services to extend connecting Class Is' reach.

GWR's Huron Central says the Canadian government "has turned a 'deaf ear' to northern Ontario transportation needs." According to CBC News, the road will quit running by the end of 2018, thanks to high operating costs and low commodity prices. HCRY runs between Sault Ste. Marie and Sudbury, serving such customer names as Algoma Steel, Domtar Paper, Eacom Timber in Nairn Centre, and Vale in Sudbury.

Says HCRY in its press release, "We have done everything in our power to keep HCRY in operation, but both the provincial and federal governments have turned a deaf ear on the situation." Reading between the lines of the various popular press reports, I gather that funds promised by one party have been blocked by the opposition. Shows the folly of depending on government support to keep the doors open. Just ask OmniTRAX about their Churchill problem.

Coming events: I'll give you my take on this week's Norfolk Southern short line meeting next week. Too much there to summarize in two days of computer time.