# RAILROAD WEEK IN REVIEW

## June 15, 2018

*“Mexico is the largest export market for U.S. corn, having taken nearly 525 million bushels last year, as well as 24 million bushels of sorghum, five million bushels of barley, and two million tons of distillers dried grains with solubles (DDGS). — Dennis Gartman, June 11*

*“Lumber and wood products have the best correlation with GDP growth compared to any other single carload commodity group. If you want to use rail traffic as a gauge of overall economic activity, it’s best to use rail traffic aggregates. ” — AAR Rail Time Indicators, June 7*

**This week’s WSJ feature** about there being “a leak in the CSX car pool” is old news. The process actually started a year ago as CSX began to link more tightly the asset base to the demand base. Yes, the boxcar base is shrinking, but part of that comes from turning cars faster so you can carry the same or more freight with fewer cars. (An interesting exercise is to compare deltas in carloads with deltas in RTMs by commodity. It’s not unheard of to see carloads go down as RTMs go up.)

Another part of the story is shrinking the number of boxcar types. I remember Michael Ward saying on a quarterly call a couple of years ago they had some 20 different car configurations, each designed to meet a specific customer’s unique loading methods and requirements. I mean, one 53-foot truck is like any other, and so the rails logically see fit to go to the 50- or 60-foot Plate F car for just about everything. You should hear NS’ Paddy O’Neill hold forth on the two dozen STCCs they can put in one of these, for example.

As for CSX exiting certain car pools, the fact of the matter is that TTX and similar pools carry some baggage. You can only have so many pool cars on your RR. When you have too many you must give some back and you can’t get any more until you do. CSX looked at the pools they were swimming in, found the some of waters not to their liking, and so got out of those pools.

The nature of the north-south CSX (and NS) franchise in an east-west world is such that you terminate more loads than you originate. Being limited in what you can do with pool cars becomes a competitive disadvantage, so the only logical fix is to end pool participation where balancing ins and outs becomes a drag on meeting customer demand.

In their Q1 Financial Review, CSX said system train speed, velocity, train length, terminal dwell and GTMs per available HP are all moving on the right direction. On-time originations remained steady at 81 percent and on-time arrivals increased ten percent to 57 percent. All of which fulfills CSX stated goals of “executing the operational plan to deliver further service gains, improve transit times and drive asset utilization while controlling costs.” And for this reason I think their climbing out of the pool and drying off is the right move.

**AAR May carloads ex-coal and intermodal** increased 3.9 percent year-over year. That is the fourth straight month of increasing YOY gains: February +0.4, March +1.6, April + 3.8, May +3.9 percent. Fifteen of the 18 carload commodities the AAR tracks were up year-over-year; year-to-date May commodity carloads gained one point, with winners in all groups but ag products (flat, so no real loss — grain mill products saved the day), automotive, and non-ferrous waste.

Within US commodity carloads by volume, crushed stone was the big year-to-date winner, up 8.7 percent. Straight STCC 28 chems gained 3.9 percent and crude plus the STCC 29s were up 4.5 percent (the AAR does not break out crude from petroleum products such as propane and asphalt). Metals increased 3.0 percent and lumber lumbered up 5.5 percent; paper eked out a gain of four-tenths of a point.

In his *Rail Time Indicators* for May, AAR's Dan Keen, AVP for Policy Analysis, writes,

> The AAR's raw traffic numbers cover one week of activity, with the week beginning on Sunday and ending on Saturday. We create monthly figures by assigning each week to a particular month. Weeks completely within a particular month are assigned to that month. Weeks that bridge two months are assigned to the month in which more of their days fall. This means some months have four weeks while others have five. The best way to compare them is to use weekly averages, which we do in Rail Time Indicators.

Which is partly why I rely so heavily on the RTI report to detect trends. The other reason is the background detail. For example, I wrote recently that I'm seeing signs of RTMs growing faster than carloads. Keen corroborates: "Weekly average grain carloads were the highest weekly average for grain for May since 1988, when a typical carload contained much less grain by weight than a typical carload does today." Bigger cars mean more product per car. That's why one sees commodity revenues up more than carloads, in some cases.

For another example, May 2018 weekly carloads of industrial sand, STCC 14 413, was easily the best month ever for that STCC. Year-to-date carloads through May were up 8.7 percent over last year and far more than in any other year through May. As for STCC 28 chems, May volumes increased six percent year-over-year — the ninth straight year-over-year increase for chemicals. And U.S. carloads of steel and other primary metal products were up seven percent in May 2018 over May 2017, their fifth straight monthly increase and 17th in the past 18 months. May's percentage gain was the biggest in seven months.

So there you have four commodity groups showing good health: grain, industrial sand, straight chems from ferts to plastics, and metals. It behooves short lines and regional carriers to sort their commodities by volume and match them to a similar sort for their connecting Class Is (you can get that from the quarterly financials or the weekly AAR carload reports). The idea is to match your strength to theirs, and go where they're going.

**Last week CSX said** they would put a six-pack of line segments up for bid:

*Massena Line: Line extending north from Syracuse, NY to Canada*
*Baldwinsville Subdivision: Branch line west of Syracuse, NY*
*West Albany and Rensselaer, NY: Collection of properties near Albany, NY*
*Cumberland Valley: Feeder lines extending east of Corbin, KY*
*Eastern North Carolina: Branch lines terminating in Graingers and Plymouth, NC*
*Marietta Subdivision: Branch line extending north out of Parkersburg, WV*

There seems to be some confusion in shortline circles about how CSX wants to proceed. According to the press release, "CSX is committed to ensuring that local operators create continuity of service for customers as it seeks buyers with an interest in cultivating and growing traffic on these lines." From this, logically, one would assume they want local operators who can expand their footprints in their own back yards, as it were.

Yet there appear to be some who have the impression CSX is pursuing an All-or-None approach. I don't think such is the case, actually. I would not be surprised if CSX would prefer to have bidders interested in all six properties; however, my sense is that if a road wants to bid on a specific line segment, that bid will be considered if the offer is compelling. After all, CSX says clearly that it wants "buyers with an interest in cultivating and growing traffic on these lines." If it happens there is one buyer who thinks he can do it all, let him say as much.

Bottom line: If a short line contiguous to any of these lines can make a strong case, CSX would be well off considering such offers. My recommendation is that strong, highly-regarded shortline operators ought to press their cases with CSX. The net result will be a win-win in every transaction.

**GWR May 2018 revenue units** increased 14.2% year-over-year. Coal & coke gained 59.0% across most of G&W's North American regions, led by the Central Region in part due to a maintenance outage at a customer facility in May 2017. Metals were up 18.5%, primarily due to scrap steel and pig iron in G&W's Southern Region, plus scrap steel in G&W's Midwest Region. Minerals & stone traffic gained 10.6%, primarily due to increased shipments of cement, frac sand and construction aggregates almost everywhere. Same-store sales, absent the HOG, gained 13.6%. Year-to-date, total revenue units are up 4.3%. Nice job.

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