RAILROAD WEEK IN REVIEW
June 17, 2022

"The plans simply failed to instill confidence that the carriers have a serious approach to fixing a problem caused by their own lack of preparedness to respond to external shocks and fluctuations in demand, including especially short-sighted management of labor forces and other resources… [I]t is particularly disturbing that the railroads failed to comply with the order requiring them to file adequate service recovery plans." — STB Decision, June 13

The STB is not pleased with the Class Is' first round of responses to the Board's May 6 directive concerning service recovery plans. And so on June 13 the Board scolded the four Class Is, issuing a Decision saying the plans submitted "were perfunctory and lacked the level of detail that was mandated by the Board's order."

Moreover, "UP and NS flatly refused to provide the six-month targets for achieving their performance goals explicitly required by the Board's order." As a result, "The Board finds it necessary to require the railroads to supplement their plans and provides explicit further instruction on the critical information they must include."

The Decision, EP 770 (Sub-No. 1) summarizes the findings of April's hearings and reviews the May 6 Decision requiring progress reports. The board adds -- quite properly, I think -- "The Board has given the carriers an opportunity to show how they each intend to resolve the service problems themselves. Self-correction minimizes the need for further regulatory intervention and, according to hearing testimony, is the carriers' preferred option."

Unfortunately, "The carriers failed, in varying degrees, to provide service recovery plans that met the Board's stated expectations. In some instances, the carriers refused or otherwise failed to provide the required information. In other instances, the carriers provided information responsive to a particular requirement, but without sufficient detail. These omissions are inexcusable."

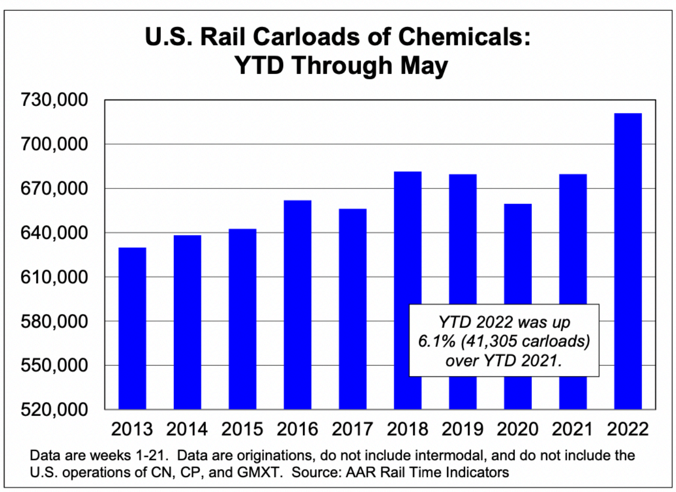
I can see where the Board is coming from. I read the May 6 responses and though they addressed the specific reporting requirements as to key operating metrics, I found few clues as to what they planned to about the shortcomings. The press release accompanying the Decision was blunt, to say the least: "The plans simply failed to instill confidence that the carriers have a serious approach to fixing a problem caused by their own lack of preparedness to respond to external shocks and fluctuations in demand…

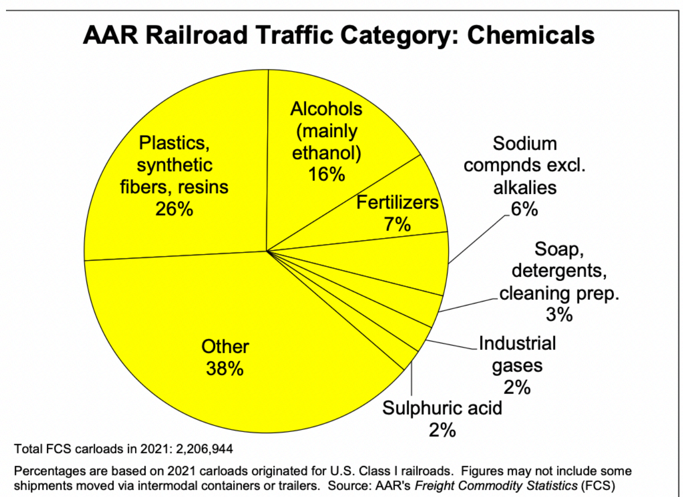
"It is particularly disturbing that the railroads failed to comply with the order requiring them to file adequate service recovery plans… I had expected a better response from the carriers to the Board's previous order, and now with more explicit instructions, which should not have been needed, there will be no excuse for continued lack of compliance."

If it bleeds it leads. That's why the bad news always gets the headlines. A recent Wall Street note begins, "North American carloads decreased 2.8 percent year-over-year and decreased 5.9 percent sequentially in Week 22. Compared to 2019 levels (pre-COVID), carloads were down 0.2 percent in week 22." Recall "carloads" means revenue units.

Looks bleak, eh? But it's really intermodal that drives the bad press. Down five percernt for the week and YTD. Yet why do these railroads put so much emphasis on intermodal where the margins are thin and you're dealing with a flaky retail base? And if your focus is merchandise carloads, you gotta dig a little deeper. Perpend:

AAR industrial chemicals as a group are up six percent YTD through May, outpaced only by aggregates, up ten percent. The chemicals group makes up 14 percent of non-intermodal revenue units, exceeded only by coal at 20 percent; chemicals have been on a steady upward trend for the last ten years, making this the strongest merchandise commodity group. Plastics, alcohols, and fertilizers comprise half the volume.





Which suggests to me that this commodity group is one of the least subject to diversion to truckload. To be sure, there are always transload opportunities but the long haul remains the province of the railroads. And even where transloads are part of the mix, very often short lines can and do provide the ideal landing spot.

Keith Creel's conversation with Scott Group at the recent Wolfe Transportation Conference was really all about just two things: identifying markets the railroad can serve given its footprint and creating the asset base to create customers within that market. "We're running an effective, healthy, ***precision scheduled railroad*** operating model" (emphasis mine) and it's opening new doors.

"If you're going to run a PSR railroad, you got to have the infrastructure to do it on." He says that the unique way CPKC can connect La Crosse, Wisconsin, with Laredo, Texas, is key. It's "our line from La Crosse, Wisconsin and the west side of the Mississippi River over to Chicago, at Savanna, Illinois, and then KCS down to Kansas City and Laredo."

You want pivot to growth? Creel sees "strong double-digit RTM growth" starting in Q3. In grain, 40 percent of Canadian loaders on CP will have the capacity to "load and launch" 8,500-foot trains of export grain to western terminals. In potash, CPKC will have "an ability to move between two and four million new growth tons [into Texas and Mexico] at a lower cost and create more market share for the next decade plus." And they'll do to with the 8,500-foot train model developed for the grain trade.

CP continues to repurpose its properties previously used for other activities, using land assets that are contiguous to existing terminals. "We'll use Vancouver as an example, with Maersk. We built a transload facility on our land. We paid to build the building. They paid to equip the inside of it. They're running it and it's connected to the rail, and it's taking trucks off the road." Ditto Toronto and perhaps even Lazaro.

Then there's food, "You can create an ecosystem (channeling Tim Cook?) with an ability to bring in density off the road, say, in Toronto, cold or frozen goods, put it on the rail, take it to the Midwest, and from there take the beef and the pork that's being trucked into Mexico. Put it on the rail in Kansas City, take it to Monterrey, offload it, get some of those avocados and fruit that's going to the Midwest and Canada that's now being trucked across the border." And so on. The ecosystem idea boggles the mind. I can hardly wait.