RAILROAD WEEK IN REVIEW
June 24, 2022

"Central banks may have difficulty getting inflation expectations down again. After decades of low and stable inflation, few people pay much attention to what Jerome Powell, Christine Lagarde or Andrew Bailey say, or even know who they are." — The Economist, June 19

"The S&P 500 over the past fifty years has never, not once, been down this much for this long without there being a recession, with the recession occurring an average of six months after the peak (which was early January) and never longer than a 12-month lead time, which places the recession as a second-half 2022 story." — Breakfast with Dave, June 20

"The Board may issue an Emergency Service Order when it determines that …a failure of traffic movement creates 'an emergency situation of such magnitude as to have substantial adverse effects on shippers… when a rail carrier providing transportation subject to the jurisdiction of the Board . . . cannot transport the traffic offered to it in a manner that properly serves the public.'" — STB Decision FD 36609, June 17

Foster Poultry Farms, a UP-served California chicken grower and processor, petitioned the STB for an Emergency Service Order concerning UP service failures dating back to February. According to the petition, UP delivers corn in 100-car unit trains from origins in Iowa and other midwest points to be processed into animal feed for both poultry and cattle. Foster says the Emergency Service Order "is necessary to alleviate harm to the poultry, dairy, and feed yard livestock that depend on the corn meal supplied by Foster Farms." That was June 15.

On June 17 the Board issued its Emergency Service Order, showing the STB can be quite fleet of foot when it needs to be. The UP had acknowledged on June 16 that service to Foster Farms had not been "adequate" and that it is "committed to improving." Such remedial steps include putting on another train set, prioritizing crews and power for the Foster service, and weekly conference calls between UP and Foster at least until service is back to where it should be.

One has to ask why senior management allowed this to happen, or even if they knew about it. We all know how reluctant middle managers are to let bad news filter its way up to the corner office and we have no way of telling how far up the the management food chain news of this situation actually went.

Part of the reason stuff isn't getting fixed as fast as it ought to be gets back to the financialization drum I've been beating for the last couple of years. As Julian Brigden of MI2 Partners so pithily points out, "CEOs are literally paid to drive that equity price higher, not to make a bloody product. And the minute those equity prices start to wobble, they start laying people off." Which may be one reason the Street started counting headcount reductions even before Covid hit.

Perhaps it's time to start paying attention to the bloody railroad once again. As for fixing what's wrong, we need to empower all those experienced middle managers to coach their charges as to the finer points of the game. Here's a baseball analogy:

Your third base guy is great on defense but only gets to first base in ten percent of his at-bats. How often does he get to first on a walk or hit by pitched ball? How often does he hit that solid single? How often does he get safely to first on a defensive error?

The coach looks at all these stats and then works with the player to improve his chances of getting to first by any means. Maybe he could increase the odds of drawing a walk by reading pitches better. Maybe defense is weak between second and first — can our guy hit to that point? In every case the coach diagnoses what's wrong and comes up with remedies.

So where's the coach for the crew that consistently outlaws? Or can't finish the switch work in the time allotted? Or is having a higher percent of locomotive road failures than their peers? In every case there's got to be someone on the payroll who can increase the on-base averages and be responsible for crew performance.

Maybe that's one thing that can be done NOW to to answer the STB's looking for quick acting medicines for service failures. Given the UP's monumental grain train failure rate, it looks like there's no coach to help them get on first, as it were. Unfortunately, that won't necessarily goose short-term share prices, but it will get them closer to the World Series — a railroad of long-term investor value derived from a solid, sustainable service.

The going-out-of-business sale continues. Year-to-date Class I revenue units through Week 24 (June 18) shows carloads including coal and automotive unchanged at 5.5 million units. Intermodal was the big loser, down 6.3 percent, dragging total traffic down 3.5 percent to 11.9 million units. Chemicals, coal, grain mill products, and aggregates were all in the green.

We continue to see employee counts in the headlines, especially as they relate to the T&E employees actually out there running trains. Recall there was a big push to increase the

T&E numbers but that push may be running out of steam. And I think it may be related to the declines in railroad share prices as much as anything.

IMHO headcount gains are slowing because more heads mean a bigger comp & benefits line on the income statement. Can't have that when share prices are falling and the CEO's Job Number One is to keep share prices going up.

The chart is the IYT Transports ETF year-to-date and includes airlines and trucks as well as railroads. All three publicly traded Class Is are included and comprise 30 percent of the index weighting. They are all trading well below their 200-day moving averages (dashed green) and are tracking the 20-day (red) as resistance. Tells me investors aren't buying all the happy talk from the recent transport conferences.

The Railroad Week in Review, a compendium of railroad industry news, analysis, and comment, is sent as a PDF via e-mail 50 weeks a year. Individual subscriptions and subs for short lines with less than $12 million annual revenue are $175. Subscriptions for Class I railroads and short line/regional operators with more than $12 million annual revenue are $599 per year. To subscribe, click on the Week in Review tab at www.rblanchard.com.