# RAILROAD WEEK IN REVIEW

## October 21, 2022

*"We have to make it easier for our customers to use our service. We have to provide better service to our customers. We have to engage with all of our employees, especially those out in the field serving our customers every day to ensure that we deliver the reliability that we promised. And we have to challenge ourselves to nurture the kind of culture that fosters a nimble, creative, and market-leading company, while staying true to the operational discipline that makes this all possible." — Joe Hinrichs, CSX incoming President and CEO*

*"Markets are softening a bit, and that is resulting in a slight reduction in our overall volume expectations, now more in the range of 3 percent growth for full year 2022. With more clarity on the impact from the new labor agreements, our operating ratio outlook also has changed. We now expect our reported full year operating ratio to be around 60 percent." — Jennifer Hamann, Union Pacific CFO*

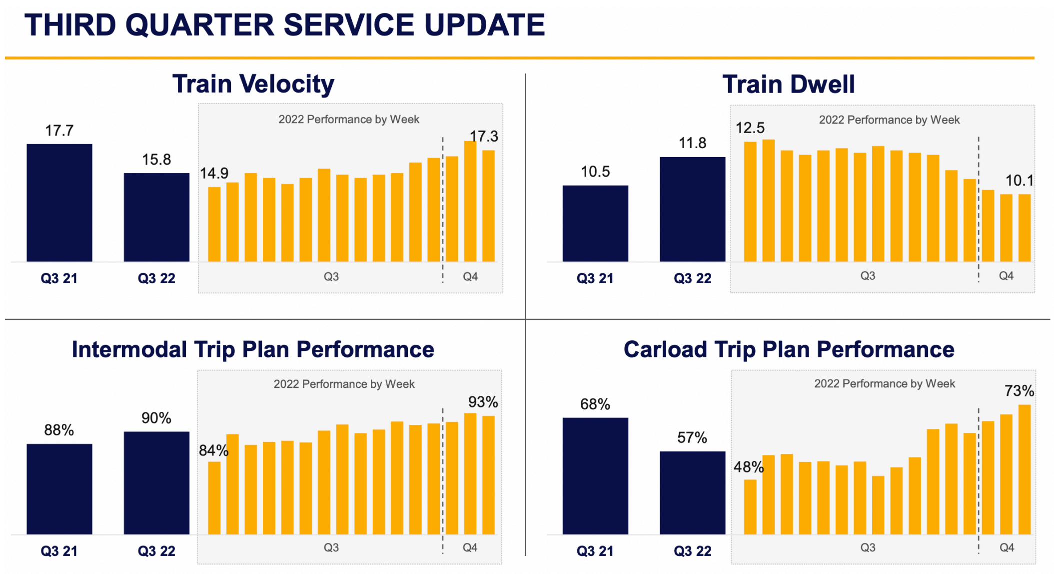
**I am very pleased** with the way Joe Hinrichs set the tone for CSX going forward on his watch. The railroad weathered some tough times with the sudden passing of Hunter Harrison, the Covid years, and now embarking on what promise to be some challenging economic times. Hinrichs' resume at Ford tells me this is a man who lives to be close to his customers, and that's a timely talent to bring to CSX.

Third quarter total revenues came to $3.9 billion, up 18 percent including trucking and others. Freight revenue hit $3.4 billion, also up 18 percent; manifest carload revenue including auto was $2.1 billion, a 14 percent gain. CSX moved a total of 1.6 million revenue units; manifest carloads made up 40 percent of the total with an average $3,307 RPU, a healthy 12 percent gain.

Operating income rose only ten percent to $1.6 billion against the 18 percent revenue gain because operating expense increased to 25 percent of revenue, mainly on fuel and labor. The operating ratio gained three points to a still respectable 59.5. Net income grew 15 percent to $1.1 billion.

Putting the fuel bite in perspective, a gallon of diesel jumped 71 percent to four bucks. Fuel burn increased ten percent on a two percent GTM increase; GTMs per gallon slipped seven percent and gallons per thousand GTM increased a like amount. But I think those numbers will improve markedly as CSX continues at the present rate of efficiency gains.

Third quarter results reek of positive momentum. Though revenue units were up only three percent, that they could hold a 16 percent RPU gain shows there is a robust demand for the product. Sequential improvement will win the day and it's there. See how the first three months of Q4 are building on Q3's progress:



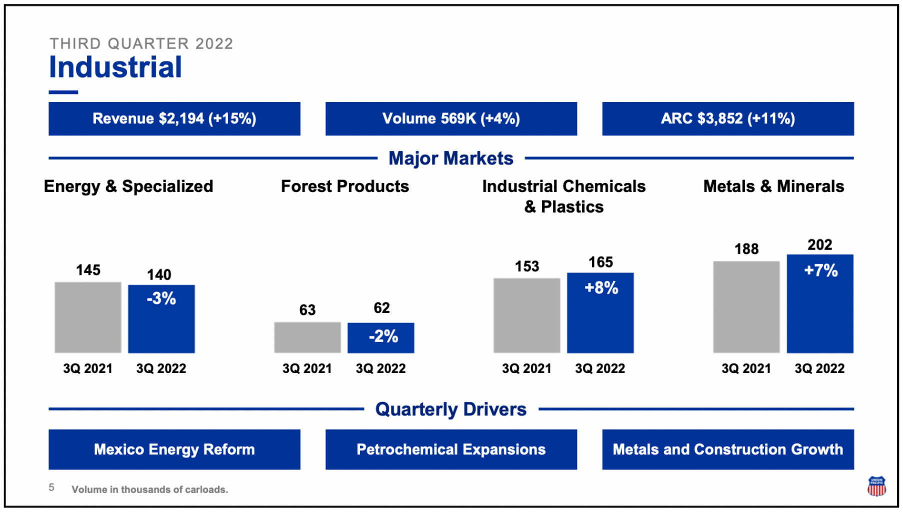

In sum, I think Jim Foote leaves a legacy of turning around a tough railroad in tough times. And I think Joe Hinrichs will prove to be the right guy in the right place at the right time.

**Union Pacific reported Q3 revenues** of $6.1 billion, up 18 percent over the 2021 Q3 on 2.1 million revenue units, up three percent. Merch carload commodities — everything except automotive, intermodal and coal/coke — gained three percent with industrial chemicals/plastics — eight percent of total units — in the lead, up eight percent. The robust revenue growth yielded quarterly records for operating revenue, operating income, and net income.

UP remains firmly in the merch carload lead with 41 percent of units in that group vs 38 percent intermodal and 11 percent coal/renewables (coal, coke, primary forest products). I am particularly encouraged that, even with the service problems reported here and there, the UP transportation product was able to earn a 14 percent increase in average revenue per unit with double-digit gains across the commodity board.

Marketing & Sales EVP Kenny Rocker noted on the call that increased coal demand plus strong biofuels production, offset by decreased potash and ferts, contributed to the 16 percent revenue gain for the bulk commodities group. Metals/minerals was the big revenue winner in the industrial products group, up 23 percent on a seven percent carload gain.

Here's how the industrials look:




Operating expense rose 25 percent, holding operating income to $2.6 billion, an eight percent gain. The OR increased 359 basis points to a still-respectable 59.9, though absent a one-time $114 million charge relating to the proposed labor agreements, the OR would be 58.2, 170 bips less and still up year-over-year. Net income gained 13 percent to $1.9 billion for the quarter.

Freight car velocity in miles per day slipped slightly to 191 from 195 a year ago; trip plan compliance for intermodal, automotive, and manifest (merchandise) carload were stuck in the sub-70 percent range. Metrics for locomotive and workforce productivity and train length were essentially unchanged.

Yet at the end of the day if UP can produce a value-added transportation product in spite of some rather mediocre operating numbers, imagine what can be done once the wrinkles are ironed out. I see a hot iron at the ready.