RAILROAD WEEK IN REVIEW

November 3, 2023

"Over the last several weeks, each department has examined opportunities to reduce layers, increase spans of control, restructuring teams and processes to empower employees to make decisions. The approach to identify opportunities was not 'one-size-fits-all' idea. Each department reviewed how they are working today and how they can re-prioritize work and better focus their teams and resources to deliver the greatest value." — Jim Vena, CEO, Union Pacific

We continue to expand our reach through transloading. We recently completed significant infrastructure enhancements at Loup Logistics' Colton transload facility, managed by Mountain Reload. Loup has also expanded their partnerships with these best-in-class transload operators: MHX LLC in Portland, Oregon and Tacoma, Washington; Jaguar Transport in Dallas, Texas; and Savage in Odessa, Texas. — Kenny Rocker, EVP Marketing & Sales, Union Pacific

"Last week we highlighted a big drop in terminal dwell in Mexico as evidence that CPKC's broader Mexican operation is finally turning around, after a year in the doldrums. Our Oct. 23 report came with some caveats, including the fact that it was just one week's worth of data." — Rick Paterson, Loop Capital, in Railway Age

BNSF wraps up the third quarter 2023 railroad results Saturday. Preliminary reports show 3Q revenue units — intermodal and carload including coal and auto — decreased 4.5 percent. Intermodal by itself was off 7.5 percent; carloads including coal and auto slipped a mere point. Year-to-date intermodal cascaded down a whopping 14.4 percent whereas carload freight fell just 2.6 percent.

Of the 18 AAR commodity groups reported, nine were up. Ag (less grain but including grain mill products and packaged food) reported gains as did commodities in the metals category. Industrial chemicals were a disappointment, falling 6.5 percent and representing five percent of total volume. We'll get the financial results when BNSF reports with Berkshire tomorrow.

BNSF is unique among Class Is in that the railroad publishes weekly service updates by commodity group. Check out the link to the October 24 report on its *website*. This excerpt is particularly timely: "Winter storm warnings are in effect across the Rockies and Central Plains as a strong system brings snow and freezing rain into the weekend.

"This system will spread south and eastward as far as Oklahoma and the Texas Panhandle through Sunday, bringing more rain and cooler temperatures to the area by the end of the weekend. Due to the wintry system, the southwest can expect to see high winds over the weekend." Customers who can modify pull/place requirements accordingly will benefit.

Over at Union Pacific, Chief Commercial Officer Kenny Rocker's October 27 *Status of the Railroad* report highlights significant gains in car velocity in miles per day, first mile/ last mile performance, and trip plan compliance across the board in bulk, intermodal, and manifest trains. The letter itself is posted *here* on the UP website.

Rocker's message is quite straightforward: "The key is to focus on the things that we can control, chiefly the service that we provide you. With our improved service product, we're striving to deliver the service that we committed to provide as well as pursuing new growth opportunities to help you win with your customers."

That is certainly consistent with what Jim Vena is saying about his vision for UP going forward. "We have to provide service. And service is what we sold the customer. Sometimes looking at trip plan compliance numbers, that's really not what we sold them. That's an amalgamation of a lot of things because we sell different customers different services. A parcel company expects a different level of service than some of the other intermodal business. Some of them just want consistency. And the bulk customers are different." (As told to Bill Stephens of *Trains* magazine, October 19.)

As if to put an exclamation point on Rocker's comments, four days later CEO Jim Vena wrote his *letter to UP employees* announcing serious cuts in middle management levels. We got our first clue that he was intending to streamline the management function on the recent third quarter earnings call.

"It's being mindful of our cost and developing our people. A key early initiative of mine is to drive decision-making lower in the organization. This means reducing layers and simplifying how we work. We need to deliver value with speed. This is a cultural change to empower our people." Moreover, "you can't have nine levels from the CEO to the people who actually do the work and expect that the message is clear, the decisions are made clear, and there isn't some hiccup where the decision stops. And I want to drive it so that we have way fewer layers. And that means with fewer layers, the people out in the field are empowered to make the right decision."

Later in the call, on the subject of locomotives, Vena observed, "I see potential productivity gains in how well we use our assets. We can't afford to park 1,000 units [as was done before] and we need to be sure the in-service locos we have are used efficiently. Stay tuned with us and you'll see incremental changes to our numbers that will tell you that we're headed the right way." And here's a number to remember: Being short just one unit for one day means you'll move 250 fewer revenue carloads on that day.

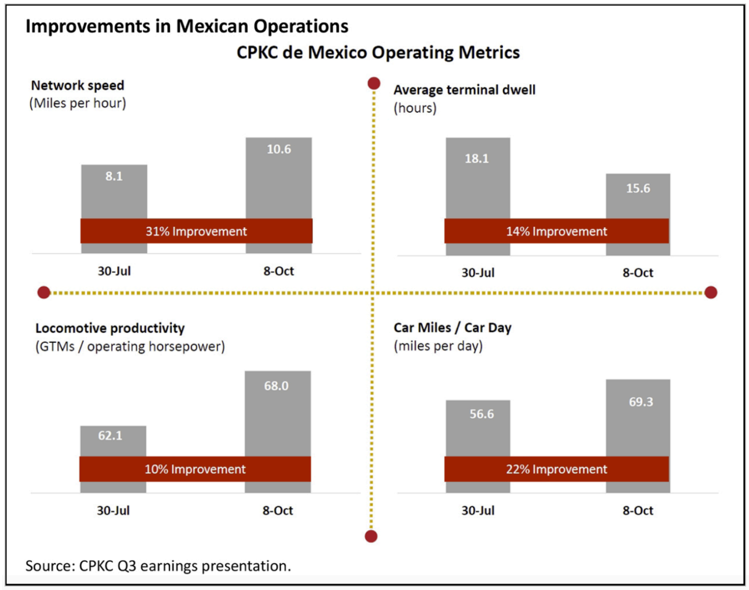
Vena may well be particularly stung by the fact that it took a scold from the STB's Marty Oberman to get UP to move a major soda ash plant expansion off the dime. Speaking at NARS in May, the Chair had asked rhetorically, "What kind of business needs a government official to lean on it in order to relate to its own customers in order to increase its own sales and make more money? Apparently, only a railroad."

My take from the earnings call and Vena's subsequent comments in person and in writing is that UP is returning to its basic roots of "It takes money to make money." So if the soda ash guy can add 65,000 loads a year with some added switching capacity, you do it. Now. Without spending months going through nine layers of managers.

Terminal dwell in Mexico has been challenging CPKC operations there for some time and Loop Capital rail analyst Rick Paterson has been continuously on their case. Finally, there appears to be a turn-around at hand. Rick writes in *Railway Age*, "The big drop in terminal dwell in Mexico is evidence that CPKC's broader Mexican operation is finally improving —after a year in the doldrums."

Rick continues, "Terminal dwell at Sanchez Yard, near the border, has fallen from 27.0 to 23.5 hours and is now below its three-year trailing average of 24.7 hours. Monterrey deteriorated a little, from 30.4 to 33.0 hours (vs. a trailing average of 30.4, so not terrible) and San Luis Potosi deteriorated from 6.0 to 8.8 hours."

One must keep in mind that CPKC includes run-through trains in its yard dwell calculations, which tends to skew the results. Never mind the fact that the STB standard is to exclude run-throughs — delays in those trains only make the yards' bad numbers worse.



Average terminal dwell for these three high-volume Mexican yards since 2019 peaked at 30 hours last July and is now down to nearly 20 hours. Let's hope the trend continues.

Assuming it does, there are two targets of opportunity for additional inbound containers through Lazaro. First is low water in the Panama Canal. One of my sources writes that the canal is "reducing appointments again and that could benefit Lazaro if it is ready to handle things in boxes swiftly enough to compete with Gulf ports given sailing times." I'm also thinking the Meridian Speedway access to both NS and CSX offers a longer rail haul and shorter transit times to east-of-Mississippi markets.

The second possible longer-term opportunity comes from the greater physical security of goods in railroad containers as opposed to over-the-highway trucks. Another of my sources offers this tidbit: "Rumor has it that you have to pay the mafioso narcos $500-$1,000 per container to get to the port via truck." But they can't stop the train.

Then there's the matter of trackage rights limits across the UP between Corpus Christi and the western suburbs of Houston. A subset of that could be potential UP physical use restrictions between Houston and Beaumont. So even though Lazaro offers some mostly near-term competitive advantages, the fact is that Prince Rupert is now and ever shall be the shortest route into eastern markets from Pacific Rim origins.