RAILROAD WEEK IN REVIEW

November 10, 2023

"We're in what I call the hangover of the stimulus packages. GDP is not reflecting a recession fundamentally because it's bloated by debt. We have an enormous level of accumulation of debt in government spending, which obviously supports GDP. We also have an unprecedented level of credit card debt that is making the headline figure of consumer spending relatively stable. All of those indicate that things may get significantly worse as the reality of rate hikes hits and the tailwind of the stimulus plans stops working." — Daniel LaCalle, Chief Economist, Tressis Wealth Management

"Genesee & Wyoming on Nov. 1 entered into a partnership with CN involving G&W's Cape Breton & Central Nova Scotia Railway (CBNS). CN will acquire a stake in CBNS and manage interline customer movements on 145 route-miles, while a G&W subsidiary will continue to operate the CBNS line from Truro to Point Tupper, Nova Scotia. CBNS interchanges with CN's Springhill Subdivision at Truro. Terms of the transaction were not disclosed." — Railway Age, November 3

"Would You Like Small Fries With That? Many unhappy returns: Friday marked the 500th trading session since the Russell 2000 Index last established a new closing high, Bloomberg relays this morning. That's the fourth largest such drought seen during the past 30 years, eclipsed only in periods surrounding the Covid crucible, great financial crisis, and the aftermath of the dot.com bubble. This broad-based gauge of smaller publicly traded firms remains 29% below its fall 2021 high-water mark, after logging 15 monthly declines over the past two years." — Almost Daily Grant's, November 6

"BNSF total revenues for the third quarter and first nine months of 2023 decreased 13% and 8%, respectively, compared with the same periods in 2022. The decreases reflect lower volumes of 5% in the third quarter and 9% in the first nine months of 2023. Average revenue per car/unit decreased 7% in the third quarter due to decreased rates per car/unit and lower fuel surcharge revenue, partially offset by positive business mix, while average revenue per car/unit increased 2% in the first nine months of 2023 resulting from higher yield." — BNSF Financial Performance 3Q2023

I'm leading off with economic news and trends because there exists a strong parallel between the state of the economy and railroad traffic trends. I use the Russell 2000 index as my primary gauge because it covers the very kinds of businesses that are the lifeblood of the railroads in general and the non-Class Is in particular.

IWM is the ETF that "seeks to track the investment results of the Russell 2000 Index, which measures the performance of the small-capitalization sector of the U.S. equity market" per Schwab. Here's the IWM three-year weekly chart:

As you can see it's been stuck in a $160-200 range since the first quarter of 2022, suggesting lackluster results of the larger business community beyond just the Dow or S&P 500. And with respect to the latter, that index is being pulled up by the so-called "magnificent seven" tech stocks — Microsoft, Google, Apple et al — showing us the other 493 companies in the index may not be doing so well.

Want further proof there's a cause and effect relationship between the IWM and the railroads? Check out this chart of the $DWCRAI index of railroad stocks:

In both cases the blue line is the 50 day moving average and the dotted yellow line is the 200. Both charts are stuck in more or less the same range. And I have shown in previous WIRs how shares of Union Pacific, Norfolk Southern, CSX, and this railroad index have all tracked each other. As you'll see below, UP and BNSF traffic patterns look very much the same, with intermodal leading the down side. Happily, non-Class Is are using their carload focus to create competitive advantage for their customers.

BNSF freight revenue before BNSF Logistics and other items came to $5.6 billion, down 12 percent, on 1.2 million revenue units, down five percent. Merch carloads dipped 70 basis points — industrial was only off a point but ag dropped nine percent.

Ag is really a study in contrasts, with grain down 16 percent but processed ag products — meals, sweeteners, produce, beer & wine, e.g. — gaining more than 20 percent. Says BNSF in its handout, the ag decrease was "primarily due to lower grain exports, partially offset by higher volumes of domestic grains, renewable diesel, feedstocks, oilseeds, and meals."

Operating expense decreased almost everywhere — all in, down 12 percent vs 3Q2022. There are lessons in here for everybody. Fuel was off a third thanks not only due to lower per-gallon prices but also due to smarter operating practices.

Quarterly labor expense came down six percent in spite of the new labor agreements and some new hires. The changes for both the quarter and YTD reflect increased headcount, wage inflation, and lower productivity in 2023. Equipment rents — car hire and loco leasing — were unchanged.

In the Berkshire 10-Q, "BNSF operates one of the largest railroad systems in North America, with over 32,500 route miles of track in 28 states and three Canadian provinces." Berkshire also owns the Marmon industrial products group, primarily known for its railcar leasing activities under Union Tank Car — UTLX on the car bodies. Third quarter revenue increased ten percent to three $billion.