

RAILROAD WEEK IN REVIEW

December 6, 2024

“The railroad on the wrong side of Trump’s tariffs. The CPKC railroad is the ultimate bet on the promise of the free flow of goods and a key cog in an intricate supply chain that underpins North American trade. It is a bet that suddenly got a lot riskier. Donald Trump’s election victory sparked a small selloff in CPKC’s shares and the president-elect’s threat last week to impose new 25% tariffs on Mexico and Canada further spooked investors.” – WSJ Dec 2

“Genesee & Wyoming Inc. (G&W) on Dec. 2 celebrated the launch of Red Deer Railway Limited (RDR), the shortline railroad holding company’s first railroad in western Canada. RDR acquired its assets and other rights from Canadian Pacific Kansas City (CPKC) as part of a previously announced transaction between G&W and CPKC.” Railway Age Newswire Dec 4

“The service crisis is still too fresh in the minds of rail customers, inhibiting share recapture from trucks. This will remain the case for some time, though the fact is that methodical progress on railroad service is being made.” — Rick Paterson, State of the Rails, Dec 1

While combing through the financial reports sent to the SEC, I frequently find items that tell me the numbers I’m looking at may not necessarily represent what I’m looking for. Take average revenue per car, for example.

The per-car number shown on their financial statements may or may not represent the freight revenue received for moving the car from A to B. From page 9 of the NSC 3Q2024 SEC Form 10-Q:

“We may provide customers’ ancillary services, such as switching, demurrage and other incidental activities, under their transportation contracts. The revenues associated with these distinct performance obligations are recognized when the services are performed or as contractual obligations are met. These revenues are included within each of the commodity groups.” [Emphasis added]

As a result, what you see in their handouts may or may not represent the actual freight rate charged. And so the reported YOY change in revenue per car for agriculture, say, in 3Q2024 may not truly reflect the revenue received for the over-the-road move for a load of corn or soy meal, to continue our example.

Let’s say that in 3Q2024 NS started moving unit trains of grain that require a lot of contractual in-plant switching at one end or the other — or both — of the move. Thus Norfolk can report an increase in average revenue per car for agriculture that inflates the apparent freight rate. I mention this because when you are doing a competitive analysis of

potential moves, you want to know the actual rates being charged between A and B. Ganging ancillary charges with the freight rate doesn't help you. But it sure helps NS show a nice change in agriculture RPU for this year versus last year.

I like to start reading the Qs and Ks at the end where all the juicy bits are hidden and gradually work my way forward. In the above case, I was reading the notes section concerning revenue recognition. In the same 10-Q it appears there are personnel-related expenses that were treated as one time and not recorded, thereby increasing operating income. This is why starting at the end with a railroad's notes regarding non-GAAP results can be quite useful.

The ASLRRRA reports that Kentucky will award \$7.5 million in grant funding for eight rail infrastructure projects in the state, all of which will be completed by ASLRRRA-member railroads. Funding for these projects comes from the new Kentucky Short Line Infrastructure Preservation (KSLIP) Program, which was established in the state's most recent budget.

R. J. Corman Railroad Group, a pioneering Kentucky shortline owner/operator, will receive \$1.5 million for two projects, one each on its Central Kentucky Line and Memphis Line, helping fund construction of a new transload yard, rehabilitation of mainline track, and more.

Transkentucky Transportation Railroad and the Paducah & Louisville Railway will also receive grants for two projects each, which will help fund crosstie replacement, rail yard improvements, new track and siding construction, and general maintenance.

Two other railroads, Tennken Railroad Company and Louisville & Indiana Railroad, will complete a project each with their respective grant awards. Tennken Railroad Company will replace over a mile of worn and undersized rail, while Louisville & Indiana Railroad will upgrade its existing 900 MHz network data radios to improve communications security and capabilities.

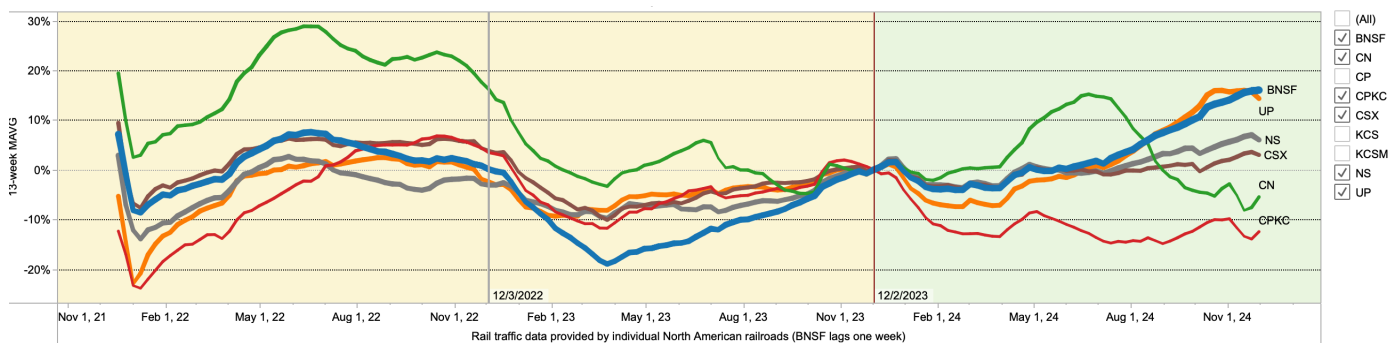
Additionally, North Carolina's Department of Transportation's Rail Division is distributing nearly \$13 million to 11 short lines through the Freight Rail & Rail Crossing Safety Improvement (FRRCSI) program. Funding from the FRRCSI initiative will help short lines upgrade more than 10 miles of railroad corridor, improve 16 rail bridges and enable increased freight rail traffic on the state rail network.

These funding activities will make significant contributions to the highly-touted new business efforts at CSX and NS. These state-supported programs will be particularly valuable in improving first-mile/last-mile service — a hot topic at the the STB for a number of years.

This is important because, as Susquehanna Financial's Bascome Majors writes, "Railroad intermodal RPU's are heavily pressured between TL rates, fuel, and negative mix. After 6 straight quarters of negative IM yield for the Big 3 U.S. rails, comps are getting easier, but lagging rail IM rates likely won't show material growth until later in 2025. Hence, *merchandise volumes are needed to drive profit growth and attractive incremental margins next year.*" *[italics added]*

Not to their credit, the Class Is have been known to stymie shortline new business and site development programs. Happily, if the new feed plant on Pennsylvania's North Shore group is any indication, the Class Is are finally discovering that local railroads can be true partners in bringing on trainloads of new revenue.

We're still not seeing much of an improvement in merch carload volumes year-over-year. Through 2024's Week 48 intermodal boxes are up 7%, grain is up 5%, but merch is up a mere 2%. Drew Robinson's ASI Transmatch shows the trends graphically:



BNSF and UP look pretty good, but that appears to be mostly intermodal as opposed to any sustainable uptick in merch carload volumes. Yet I'm seeing signs the ISM manufacturing curve may start to pick up in the first quarter. Fingers crossed.

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