

RAILROAD WEEK IN REVIEW

January 17, 2025

“If you’re a professional investor, you are measured against a benchmark. You are always thinking, well, I was in Bitcoin. It had a great run since November, but I’ve now got to think about how I’m going to beat my benchmark in 2025 and if that beat doesn’t come, I’m going on to something else.”— Jim Bianco, President, Bianco Research, Real Vision, Dec 25

“Large corporations listed on major stock exchanges are beneficiaries of Fed largesse [in lowering interest rates] when they can borrow money cheaply to buy back their own shares in equity markets. By increasing earnings per share, they raise the price of their stock.” — Judy Shelton, Good as Gold, page 44

“Reflexivity is the term I use to express the dichotomy between subjective and objective realities, where opinions are stated as facts... I contend that financial markets are always wrong in the sense that they operate with a prevailing bias that can validate itself by influencing market prices.” — George Soros, The Alchemy of Finance, New Introduction 2003

Three quarters of all shares traded on all the markets are traded by institutional investors — mutual funds, family offices, hedge funds, investment bankers, etc. The portfolio managers get paid for having their stocks perform and, if they don’t perform, they are out on the street looking for work.

Which makes one ask, why would anyone buy Norfolk Southern when they can buy Nvidia or the QQQ for double — or triple — digit returns when the rails are returning less than 2% on your money. So what does this have to do with owning or operating a railroad?

As Peter Tucker said eons ago, the purpose of any business is to create customers. Apple is creating customers as much for the services portfolio as for the hardware. Truckers like Schneider and JB Hunt create customers by offering transportation services that have a competitive advantage for their customers.

The railroads today do very little of that. To be sure, they offer a competitive advantage in bulk commodities from coal to corn, but cannot compete when they move time-sensitive goods for customers who depend on a reliable supply chain for both raw materials and finished goods to stay in business.

And since growing a profitable revenue stream drives earnings, and earnings growth drives institutional managers’ share purchases, it follows that those of us in the railroad

business had best follow stock prices if we want to really know how well the carriers are doing at creating and keeping customers.

WIR this year is going to zero in on railroad share price as an indicator of how well the rails are doing in creating customers and building their revenue base. And although the interviews with the railroad CEOs published this month in both *Railway Age* and *Progressive Railroading* are all very upbeat, you can tell much of it could have regurgitated from past remarks written by a PR hack or an even AI program. Let me give you an example from another discipline.

Wall Street veteran Jim Rickards recounts an incident in the introduction of his latest book, *MoneyGPT*, in which he compares essays written on Russia's actions in the Crimea by a graduate student with one on the same subject written by Chat GPT.

Rickard writes. "I was able to identify the GPT version after one sentence without even reading the human version. The reason was the use of an overworked cliché, 'In the political chess game...', as an introduction to Russia's action. The sentence also referred to Russia's move as 'a significant shift in power dynamics.' Clichés have their place and I sometimes use them myself — yet in the first sentence it was a dead giveaway that a robot trained on millions of pages of text had driven into a literary cul-de-sac.

"In contrast, the human essay began, 'The Russian annexation of Crimea, a former Ukrainian peninsula, comprised the largest seizure of foreign land since the end of World War II.' Not exactly electrifying, but still, it was declarative, factual and informative. No cliché."

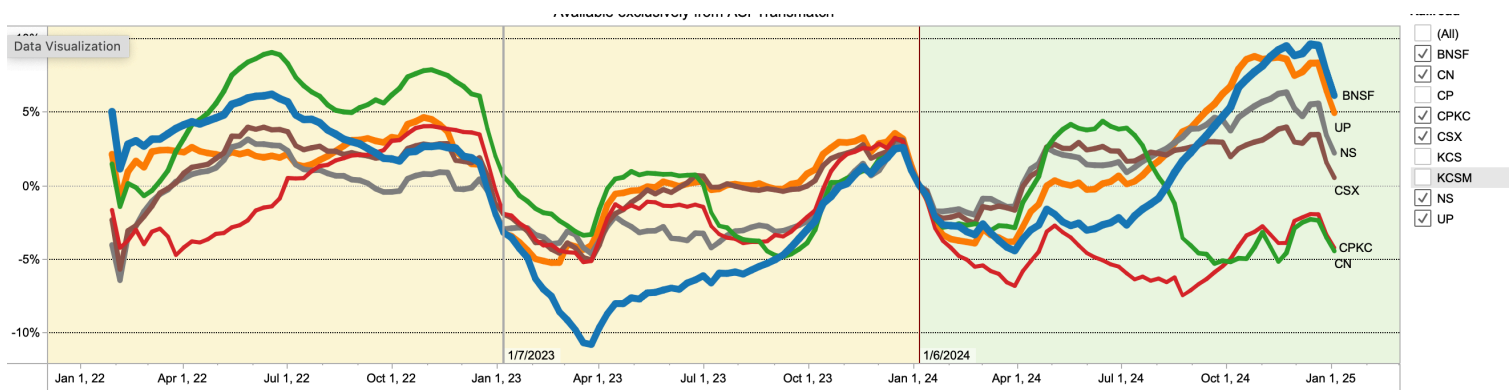
What I am suggesting here is that Chat GPT could've taken all the positive comments ever uttered by, say, Mark George of NS, and strung them together to create an upbeat picture for investors and other interested parties. And from that one can easily conclude that the best way to see how a railroad is performing is to look at the numbers. And the numbers ought to be reflected in the share prices. Never mind the official utterances.

There's also the matter of what George Soros calls "reflexivity." If investors are convinced that Invidia is really the hot setup, they will drive up prices doing market orders on the ask rather than trying to save a few pennies on lower limit orders. Thus the perception of the buyer makes higher prices a reality, pushing multiples into the stratosphere. Why buy UNP for 20x earnings when I can buy NVDA for 80x?

Then there's inflation. *Barron's* this week: "Wednesday's consumer price index data showed headline inflation measured 2.9% year over year in December. Core inflation, which excludes food and energy prices, remains above 3%, measuring 3.2% last month."

The AAR says railroad revenue units increased a mere 2% in calendar year 2024. If I'm an institutional investor, how can I sell a product with negative *real* growth (actual growth rate less the rate of inflation) when my competitors are selling products with growth rates greater than the rate of inflation? See Bianco quote above.

Graphically, Drew Robertson's Railfax Weekly Carload report shows both the growth rates and rates of change in railroad revenue units. So I guess one encouraging conclusion could well be that volumes, at least for the US roads, are seeing upwards rates of change that are significant improvements over 2023. The Canadians unfortunately are sort of mired at the zero level but I think some of that is due to their political upheavals.



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In a general sense, it appears that intermodal boxes are still leading in volumes as a percent of the whole, with grain and chemicals leading up the carload sector. Aggregates, lumber, and metals are lagging but I think that's a function of decreased manufacturing demand and a slowing of housing starts.

Nat gas prices are well north of \$4/mm BTU which, combined with the AI-driven increased power demand and a Trump administration relaxing of environmental regs, could help the PRB and related actors. Put UNP and BNSF at the top of that list.

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