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The Railroad Week in Review 9/29//001
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Rail stocks this week took a decided turn for the better. CSX led the pack, up 8%, followed by KSU, CNI, and UNP, up 7%, 5%, and 3% respectively. Nobody ended the week worse off, and that's somewhat comforting. There is a cautionary note, however. The WSJ on Thursday pointed out that companies with lots of debt might be slower than those with minuscule debt/equity ratios to revisit double-digit returns.

It'll be less an issue if the economy starts rebounding late this year, as many had predicted before the attacks. But if a recovery is six or more months away, many companies may face tougher times. When companies do run into problems with leverage, the business starts to matter less and the balance sheet comes to the forefront.

Railroads are not immune. Class 1 railroad debt-to-equity ratios range from a low of 0.60 (CNI) to a high of 1.34 (NSC). The two largest shortline holding companies are also at the extremes, 0.84 (GNWR) and 2.91 (RAIL). Thus forward earnings will play a key role. Remember that debt service requirements remain regardless of operating cash flow.

Earnings estimates have literally been kicked into the next year. Pre-Sep 11 numbers for 2001 now show up in the '02 column and the previous '02 estimates have been pushed into '03. Still, BNI, CNI and UNP sport '02 PEs of ten and crumbs based on Friday's closing prices. GNWR wins the low-ball prize at 8.7; RAIL is only 90 BP higher. Let's watch, shall we?

A note from the BNSF marketing department says they will no longer accept "retroactive pricing to protect shipments where the customer tendered a shipment prior to agreeing on a private price." That a carrier would ever accept a carload for movement without a prior understanding as to price was – to me at least – news. Moreover, several of my shortline clients expressed concern insofar as it could affect billing and collection.

A major selling point for shortlines paid on allowances is that their customers get a single invoice from the originating or terminating class 1, depending on the waybill terms. A shortline always has the option of refusing a car tendered for movement from a shortline origin without an agreed pricing arrangement. However a destination shortline that settles on an interline basis has collection responsibilities. They naturally expect the originating carrier to secure proper rates before accepting shipment.

BNSF writes that there should be no impact on shortlines settling with allowances as payment is made whether BNSF has collected the freight charges or not. With respect to the larger picture, BNSF says the practice of accepting shipments without prices has been going on since deregulation but now it's got to stop. Some customers have said this will cause confusion, however the opposite is the more likely outcome. Still, as in everything else, attention must be paid and the vigilant are the soonest winners.

London's *Financial Times* for Wednesday said, "The time is ripe for the US to review carriage of people and goods." Unlike other countries in the civilized world the US has no integrated transportation policy and where airlines and autos received mega-subsidies and bailouts, Amtrak

increasingly must make do from the fare box or go without. So when airlines suddenly cut capacity and lines at counter lengthened, there was no alternative but the car. Trains were jammed, and forget about booking space (the Amtrak website and 800-number frequently say all trains are full even when they are not). FT correctly notes "It's time for the federal government to start treating its passenger railroads with the same importance given air travel and the highways."

Monday brings a new guaranteed intermodal offering via Memphis over UP and NS between Los Angeles and Atlanta, with a guaranteed on-time delivery option, beginning Oct. 1. The new service, named Blue Streak, will offer customers a choice of three service levels: Standard, Premium and guaranteed SuperFlyer. The service levels are designed to meet a broader range of customer pricing and transit requirements.

The SuperFlyer service will offer "on-time or free" service for each load that does not meet the scheduled availability time for customer pick-up. Premium service offers priority train space, freight monitoring and improved cut-off and availability times. Standard service allows price-sensitive customers access to Blue Streak trains, subject to space availability.

Also on Monday NS and CP start a new tri-weekly (Mon-Wed-Sat) intermodal service between the Express Rail facility in Northern NJ and Toronto or Montreal. It lops a third off the previous transit time and promises second morning availability. Moreover, CP will forward boxes to and from Western Canada via Montreal. This is certainly timely, given the horrendous delays truckers now encounter at the border crossings.

Intermodal cooperation is not solely the province of the big roads. Just this week Emons Transportation Group (Nasdaq: EMON) had a ribbon cutting at its new Auburn (ME) intermodal terminal expansion. EMON subsidiary St. Lawrence & Atlantic Railroad (SLR) is the serving road. Traffic at the facility has tripled in the last six years to nearly 15,000 boxes and trailers using the SLR route into Montreal via a connection with CN in Quebec.

SLR was one of the early (and few) applications for ISTEAs money for construction of a rail-served intermodal terminal. The present expansion effectively doubles terminal size to 35 acres, giving SLR the physical capacity to triple these volumes. The original terminal opened in September 1994 and was built with 80% federal ISTEAs funds administered by the state of Maine and 20% funds from the city of Auburn. The \$1 mm expansion was completed in July 2001, was built with 50% TEA-21 funds from the federal government through the state of Maine and 50% from the city of Auburn.

A long-time observer of the passing railroad scene writes, "Your comments on dispersal of things as being protection against terrorists (WIR 9/22 cover note) is not necessarily good news for an industry whose economics depend on volume. That said, railroads now have a lot of multimodal (intermodal, transload, etc.) services in place that are well suited to a perhaps even more dispersed urban landscape than we have today. It is interesting that the very sprawl created by the Interstate Highway System (and something decried by many urban planners but embraced by most of the rest of us) is a good thing in the new world order." How right he is.

Roy Blanchard

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