

The Railroad Week in Review
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Feedback from the UP shortline meeting has been illuminating, to say the least. Recall a thread from last week's notes had to do with product positioning and brands. Looks are important, and brand manufacturers take a great deal of pains to present an attractive image. We in the railroad industry ought to pay attention. Here's what one of the conference attendees has to say:

“During Ed Hamberger's speech at the UP Short Line Meeting, he lamented how difficult it was to get the rail freight message across ‘inside the beltway’ in Washington. The first time I heard this comment was before shippers at the National Association of Railroad shippers. When I attended the NARS meetings in Washington, my wife and I went a day early and took one of the sightseeing cruises on the Potomac River. We passed under many bridges with streets, interstates and the Metro passing overhead - all with shiny well maintained vehicles. Then we came to the rail bridge - unpainted and rusty with vines growing all over it. It looked abandoned.

“Then a long slow freight train rumbled into view, its cars covered with graffiti, wobbling and creaking its way across the bridge. I was embarrassed for my profession - it looked like a train from the worst urban war zone headed for the closest junkyard. It is time to stop complaining that people don't understand how important the freight railroads are and clean up the mess. No one ‘inside the beltway’ will take the AAR message seriously when the words do not match the visual.” He has a point.

Last week's letter also went out in a special mailing to all the UP shortline meeting attendees for whom I have e-mail addresses, about 60 in all. The response here has been gratifying as well. In a follow-up note to one responder, I remarked that there seems to be “a great unevenness among Class Is and even across commodity lines within Class Is in the way shortline new business opportunities are handled.”

My correspondent writes, “Yes, we have experienced the unevenness you describe -- both among the Class Is and within them. UP seems to be leading the pack in its efforts to assist short lines in attracting new business. Once we win a new account, UP has been very supportive, working with us on such things as infrastructure solutions, pricing options, and routings.”

“The same cannot yet be said of all Class Is where we have experienced a wide range of responses, ranging from extreme indifference to tremendous help. The reaction seems to depend on a few things. One is how the marketing people are compensated. If there is a penalty to them for traffic originating or terminating off line, they are less than helpful. Another is whether the commodity group can steer the traffic to a transload or high through-put elevator and thus garner most if not all of the revenue.”

From this it follows that shortlines would do well to understand the corporate culture of their Class I customers (and they are that when it comes to new business). The successful shortline proposal anticipates the Class I goals in terms of satisfying the commodity-routing-equipment requirements. High volume, high-rated commodities with low or no equipment cost and few car-handlings will enjoy a better chance for success than their opposite numbers.

Kansas City Southern's NAFTA Rail project took another hit as the TMM decision not to go forward with the TFM sale cascades into Tex-Mex ownership. Recall The Tex-Mex became part of the Kansas City Southern rail system in 1995 when KCS acquired 49 percent of the Tex-Mex from TMM.

Now comes TMM to say it will pay \$32.9 mm to buy back the 51% of Mexrail Inc. sold to Kansas City Southern for \$32.7 mm just three months ago. (See press release dated May 9, 2003 on the KCS website, www.kcsi.com.) Tex-Mex is critical because it owns and operates the 157-mile link between the Laredo border crossing and the end of KCS' rights on UP to Corpus Christi. So not only does the TMM tiff threaten to derail KCS access to the Mexican interior but also reaches into the US to deny KCS even getting to Laredo.

The rails were well represented in this week's list of new 52-week stock price highs. Canadian National (NYSE: CNI) and Canadian Pacific (NYSE: CP) took the honors for the Class Is. Shortline and regional railroad operators Genesee & Wyoming (NYSE: GWR) and RailAmerica (NYSE: RRA) also hit new highs. Carbuilders Greenbrier Industries (NYSE: GBX) and Trinity (NYSE: TRN) took the brass rings for the vendor side of the house.

My suspicion is the Canadians continue to benefit from the foreign exchange spread as well as lowered operating ratios and the grain belt recovery. The two shortlines I think are benefiting from the favorable small cap market in general and the rail sector's role as a leading indicator in an improving economy. Ditto for the car builders, though an article at purchasing.com notes that "the backlog of orders has doubled" in the TTM period.

Rail opportunities in scrap paper and scrap steel turned up in the papers this week. The Business section of Thursday's *Inquirer* ran a feature on the scrap steel market's revival. Scrap iron and steel now fetches about \$123 per metric ton, up 31% in the last year 66% over two years. For two reasons mainly. First, there are fewer metal fabricators in the US, and the ones that are left leave less scrap in their production processes. Second, there are more offshore fabricators clamoring for the same scrap, making it a seller's market. In this market rail's inherent rate advantage over truck, even in relatively short-haul lanes, can be advantageous as raw material costs increase.

Scrap paper was featured in a full-page Weyerhaeuser ad that ran last Wednesday in the Journal. Copy line: "We collect millions of tons of recyclable paper products every year. Picture 120,000 train [sic] cars full of office memos, empty boxes and last Sunday's sports sections. We use the fiber to make new products again. And again. And again. And again."

There are at this moment three shortline short-haul moves of aggregates, paper and scrap steel within 200 miles of where I sit. They never touch a class 1 and get more than a turn a day from the equipment. These same shortlines will be able to ship to each other once we work out a few details with the Class 1s in the middle. Call me for details and how to structure a similar package on your railroad.

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