

The Railroad Week in Review
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Shortlines, like any business, must continually reinvent themselves to remain in the game. One of the best in this regard is Progressive Rail in Minneapolis. They've done a nice job with their website – www.progressiverailroad.com – and I've asked their VP Marketing Tim Eklund to give WIR a little more detail on their approach to the business and some successes to date.

Tim writes, "Progressive Rail is really a 'business development company' that utilizes the tools of railroading, transloading/warehousing/local trucking, and other value-added services to create new business opportunities for our communities, our customers and our Class 1 partners. We execute our Business Model from an aggressively retail-oriented perspective and are shameless marketers and promoters of the business. We cold-call, we do mailings and campaigns and advertising and a whole host of other "retail" activities designed to build awareness and business."

They don't stop at trackside, either. Progressive partners with development stakeholders, both public and private, to market the specific benefits of rail service. They've bought or secured options on more than 160 acres of industrial development space. Over the past six years these efforts have brought nine new industries to the property, recycling vacant buildings, building new facilities, and creating jobs.

We've mentioned before the Unique Selling Proposition (USP) that any company needs to gain competitive advantage. At Progressive Rail it's the seamless package of site selection, rail service, transloading, warehousing, inventory management and local delivery all on one invoice. Says Eklund, "Most railroads focus on one or two potential value-added services. We aggressively promote all six."

And it's paying off. Doors were opened in 1996 with three customers, 600 revenue loads and a few miles of former CP track. Today, Progressive Rail has 18 rail-direct customers on the original line segment plus another 70 transload customers through their proprietary Carload Connection Transload Facilities. Business is up ten-fold to 6000+ carloads. Two additional line segments from CP will add another 5500 carloads and UP has expressed an interest in adding Progressive Rail to its shortline roster.

Norfolk Southern will take a \$50 mm 4Q03 write-down on its T-cube telecom subsidiary, reducing eps by about 13 cents. The current consensus before the write-down calls for 37 cents a share, up from 33 cents in 4Q02. In a note to clients Bear Stearns says, "NS has not booked earnings from T-Cubed thus far, which we view as a non-core holding. As such, the impairment should not impact recurring EPS."

For its part, Norfolk says the charge "recognizes the reduced value of telecommunications assets based on prevailing market conditions in the telecommunications industry as reflected by a recent valuation study." The map at www.t3inc.com shows the network complete from Alexandria to Chicago via Harrisburg, Pittsburgh and Cleveland plus Chattanooga-Jacksonville via Atlanta and Macon, some 1600 miles in all.

Elsewhere, NS set the 2004 capital plan at \$810 mm of which \$517 mm will go for ROW improvements and \$258 mm for equipment. The biggest track allocation will be \$384 mm for T&S plus bridges. Equipment allocations include \$178 mm for 100 new 6-axle locos plus to upgrading existing power and augmenting the auto rack fleet.

The STB has instituted a proceeding to determine the 2003 railroad cost of capital. There are four elements: (1) the railroads' 2003 current cost of debt capital; (2) the railroads' 2003 current cost of preferred equity capital; (3) the railroads' 2003 cost of common equity capital; and (4) the 2003 capital structure mix of the railroad industry on a market value basis. The sample will include only AAR Class I roads with bonds are rated at least BBB by Standard & Poor's and Baa by Moody's, are listed on the NYSE or AMEX, and have paid dividends throughout 2003.

Class I railroad performance measures posted at www.aar.org are a good indicator of industry trends. Looking at November 2003 vs the entire 4Q02 experience we see trains speeds are generally down and cars-on-line generally up. Last week we saw that AAR November carloads were up 2.6% yoy, indicating the western and Canadian roads picked up the slack from the eastern roads.

Of more concern is the relationship between cars on line and average train speed. It appears that as cars go up, velocity goes down. Among the up rails, CN posted the largest increase in cars but was tied with BNSF in train speed degradation. UP and BNSF were about the same in cars on line increase yet the former was three points worse off in train speed. Perhaps NS was the best story where inventory was off less than a point and speed off half that.

One conclusion is that as volume goes up so does congestion and any significant traffic gains can only make matters worse. Moreover, the roads with the heaviest merchandise carload concentrations (UP, CSX, e.g.) seemed in this sample to suffer the most. We've said before that as presently constituted the merchandise carload network is too complicated and it takes too much handling between O-D pairs. And this may well be where it's showing up.

Canadian Pacific has become the first railroad in Canada to operate intermodal freight trains with mid-train remote-control locomotives. The technology lets CP run intermodal trains approaching three kilometers in length through the winter when they were previously shortened because of air-pressure loss in colder temperatures. Since 1995 all new main-line locomotives ordered by CP have been equipped to operate in leading or remote-control configuration.

CP is also adding 5,500 new double-stack cars capable of handling any size of container in any load configuration, and will do away with older cars that are less flexible. The net result will be an estimated 28% increase in containers per train and 16-per-cent decrease in intermodal train starts. As a result the intermodal car fleet can shrink by about 1300 units without losing any volume capacity. Can you say fewer train starts?

Rail Stocks this week enjoyed yet another round of new highs. It has been most heartening to watch the parade of successive new highs week to week. Included in this august list are the likes of BNSF, CSX, GWR, NS, RRA and UP. Not only are the prices moving up but they're supported by good volumes as well. There are more up days than down and the daily close is frequently not far off the session's high. All of which bodes well for the near term at least.

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Table 1. Cars on Line, Average Train Speed

	BNSF	CN	CP	CSX	KCS	NS	UP
Cars on Line							
4Q02	189,945	92,340	68,860	227,356	30,167	184,721	310,369
Nov-03	196,392	105,986	70,257	229,049	25,579	183,121	320,185
Change	3.4%	14.8%	2.0%	0.7%	-15.2%	-0.9%	3.2%
Avg Train Speed							
4Q02	25.9	28.1	28.1	22.5	20.7	23.4	25
Nov-03	23.7	25.7	24.4	21.4	27.8	23.3	22.2
Change	-8.5%	-8.5%	-13.2%	-4.9%	34.3%	-0.4%	-11.2%

Source: AAR Performance Measures, www.aar.org