

RAILROAD WEEK IN REVIEW

May 20, 2016

“Watco subsidiary Kanawha River Railroad has reached a definitive agreement with Norfolk Southern to lease and increase operations on 309 miles of rail line in Ohio and West Virginia.”
— Watco press release, May 20.

Norfolk Southern held its Annual Short Line Meeting in Norfolk this week. This was the 15th in the series and the first one in Norfolk. Judging from comments during and after the session, the 200 or so feeder line attendees deemed it highly worthwhile. I also deem it so.

NS has interchanges with some 246 different short line names with roughly 20,000 route-miles among them, effectively doubling NS' reach. Last year these roads brought in \$2.7 billion revenue dollars, roughly 26 percent of NS 2015 total revenue of \$10.7 billion, touching 1.1 million revenue units, more than 15 percent of the NS total 7.5 million units. Moreover, short lines touched more than half the single-car movements in what NS calls its General Merchandise commodity group (everything but intermodal and coal/coke).

NS feeder-line carloads finished 2015 up 1.4 percent, vs. NS total revenue units off 2.6 percent year-over-year, yielding a 4-point spread between volume deltas. The NS “250-squared” challenge (250 new carloads from each of 250 railroads) has brought in more than 120,000 new carloads since the program’s 2008 start, more than covering any slippage as old customers move away. These carload gains prove there’s a pipeline of new business that can more than offset organic losses. We got a taste of that pipeline from ASLRRA President Linda Darr: 16,000 2016 carloads in five lanes involving nine shortline names and commodities from flour to wind turbine blades.

Key take-aways for me:

— The meeting theme was “Break on Through — Exceeding the Economy,” certainly apt for the challenging carload environment. CEO Jim Squires and Chief Commercial Officer Alan Shaw set the tone, calling on shortline partners to help NS increase the rate of carload growth, improve customer service, and enhance extant relationships. To this end, NS is unique in providing each connecting feeder line with a single point of contact for every aspect of the NS interface, from ops to customer relationships to accounting. That the NS single point of contact scheme works is evident from the number of awards garnered by the names that use this key NS resource to best advantage.

— The NS agenda with short lines for 2016 is very simple. Rob Robinson, AVP for Short Line Marketing, says the name of the game in this economy is to develop and maintain a “robust

pipeline of projects and initiatives” and continue to execute. The three drivers are: the focus on service, relationship building, and growth beyond organic.

- Blocking for the distant node and block-swapping to bypass intermediate hump yards are doable when the data supports it. Conversations with EVP Ops Mike Wheeler and VP Transportation Terry Evans confirm that there is a “real value-add to NS and our mutual customers to pre-blocking where it makes sense. Anything you can do to improve transit time helps us to compete for more carload business.”
- VP Strategic Planning John Friedmann talked about how NS is aggressively adjusting the cost structure of its Strategic Line Network. Since most of the few shortline opportunities are spoken for, there will be no windfall of lines in that category. Still, if you think you can make a contribution to this process, by all means present your case to John. As Watco’s Stefen Loeb said in his remarks on how to “break through” with NS, think of NS as a customer and what you must present to get a YES when asking for the order.
- ISAs are essential. This is a common theme echoed by COO Wheeler, Senior Short Line Development Manager Don Jones, who heads up the Short Line Development Team, and others. Jones says meetings with short lines always start with an ISA review because it’s the foundation for improved customer service. In his “Short Lines Metrics” break-out session, Don introduced the “shortline dashboard,” a spreadsheet tool that gives NS complete visibility of the short line partner’s business from interchange-on to interchange-off and every event in between.
- Shortline miles are not included in calculating car-miles per day, but shortline hours *are* included when calculating car cycle times. As noted above, the dashboard tracks shortline dwells, so the short line that turns cars promptly will offer its customers a competitive advantage over customers on slower-moving branches.
- VP Industrial Products Mike McClellan’s wrap is that NS is open to a fact-based, data-driven discussion complete with suggested solutions for specific cases. A metrics-based conversation is essential; mere anecdotes won’t do. Successful shortline relationships are a huge driving force in growing the NS merchandise carload franchise, whether in single cars, blocks, or unit trains.

Bottom line: NS wants to grow the shortline franchise, period. The outlook for organic growth is minimal, and the logical place to look is existing truck moves. Cover your own first-mile/last-mile performance and work with NS to get the move right in the middle. I’d suggest doing so on a project basis, identifying goals, the resources you need to accomplish same, and tapping your NS sales team’s skills to create the winning combination.

Genesee & Wyoming April 2016 NorthAmerican carloads were off 13 percent with six of the seven commodity groups comprising 80 percent of the carloads down. According to the press release, the coal hit was biggest in the Midwest, Central, Ohio Valley, and Northeast Regions. Minerals/stone dropped on frac sand and salt, partially offset by a gain in cement. The 15 percent

agricultural products drop comes on low grain prices and the strong dollar, mainly on the Ohio Valley, Mountain West (this would be the ex-DM&E) and Canadian lines. Paper-related carloads dropped in Canada, the southeast, and the PNW.

So here you have major downers in commodities that are weather-dependent, depend on the general manufacturing environment, and on consumer behavior — none of which one can control. As a result, YTD vols are off 10.2 percent and down 6.3 percent from March, after having had slight monthly sequential gains in Feb and Mar. The only good news in all of this is coal dropping to 4th place as percent of total carload vols. As a reminder, I use the GWR carload trends as a proxy for the North American short line regional railroad scene as a whole.

Norfolk Southern and Watco have an agreement regarding the former Virginian and NYC lines between Mullens, West Virginia and a point just outside Columbus, Ohio. The transaction, a lease of more than 300 route-miles, includes the ex-NYC Conrail branch between Alloy and Cornelia, WV, crossing the CSX (ex-C&O) line (used by Amtrak's Cardinal) at Deepwater. Watco will operate the lines as the Kanawah River Railroad (KNWA), restoring daily service to a portion of the line in Ohio where NS had suspended operations earlier this year for want of sufficient business on the line.

The May 20 press release says the line supports customers in the agriculture, energy and chemical industries. KNWA will soon begin the hiring process and will hold a series of meetings for Watco and KNWA leaders to brief current NS employees on the transaction and explain the process for how they apply to become members of the KNWA Team. The KNWA General Manager and marketing officer will be named in the weeks ahead.

Meanwhile, KNWA will begin the process of seeking approval of the transaction from the STB. Operations are expected to begin in about two months. This lease transaction is the first piece of the Norfolk Strategic Line cost structure adjustment process (see Friedmann, above), and it's easy to see why Watco got the nod.

A number of Watco lines won awards Tuesday evening for their successful collaboration with NS on new business development, particularly on the Grand Elk in southern Michigan, which is not exactly a hotbed of economic activity, but they created new customers regardless. Watco began a conversation with NS early on and has demonstrated its skills in creating customers, treating NS as a customer, and getting a YES when they asked for the order.

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