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To nobody's great surprise the economy has now been officially decreed to be in a Recession. But it's nothing like we've ever seen before. The National Bureau of Economic Research maintains the downturns in employment and industrial production "is sufficient to merit the determination that a recession is under way." NBER goes on to say that absent the Sep 11 attacks "it is possible that the decline in the economy would have been too mild to qualify as a recession."

Here's where it gets weird. Goldman Sachs allows as how it may be worse than the Commerce Dept's initial annualized 0.4% shrinkage predicted for 3Q01, yet the declines in jobless claims suggests a decline slower than the initial forecast. Goldman Sachs also says there will be clear signs of recovery by 2H02 "with a reacceleration of aggregate profit growth" albeit with some variation between and among sectors and industries.

Profits under pressure continue to drive close scrutiny of production costs, and supply chain management is a major portion thereof. That's why it's so important to have carriers perform consistently dock-to-dock. Trucks are easy – you make an appointment and there he is. Until now, rail customers have been limited in the ways they can measure performance. But that has changed.

Union Pacific grades performance on five measures: safety, trip plan compliance, right cars on the right train, running the train on time, and efficient use of resources. Rail users would do well to use the same yardsticks and periodically tell their service providers how they scored. Then each railroad can compare the shipper view of service provided with its own view. The results will be instructive and everybody will benefit.

Railroad Retirement has finally gotten the Congressional green light for taking up the question of overhauling the Act by allowing some private investment rather than restricting funds to government bonds. Appearing on CNBC's Squawk Box AAR President Ed Hamberger said the fund, which pre-dates Social Security, now has reserves of about $15 bn, on which it makes about 4-5% a year. He said that it should be run more like a private pension fund, which it really is because it runs totally outside Social Security system, and could conceivably double the payout.

According to the AAR, Railroad retirement "is funded by payroll taxes levied on both employees and employers and provides employees with a basic set of benefits." That's Tier 1, or 16%, just like SSI. The AAR goes on to say, "But unlike Social Security, it also provides a second set of benefits" funded by an additional 21% tax on earnings (for full text, see www.aar.org).

Still it may be a fight because some in Congress think the feds will have to pick up the slack if the private portion fails. No way, says Hamberger. If reserves fall below a certain point, the industry itself will pick up the tab. Moreover, labor says passage would increase benefits, shorten vesting time, and lower minimum retirement age to 60 from 62. Railroads say passage would lower payroll taxes by some $400 mm a year, or 25% of the typical class 1 capex budget.

Every time I venture into the field I see more and more freight cars carrying ownership marks of little-known shortlines. What's wrong with this picture? It's been duly noted here and in other industry publications that running a smarter, faster railroad means fewer cars are needed for a given baseload of traffic. That's one reason an equities market basket of builders (TRN, GBX) and lessors (GMT) would have lagged the DJIA 12-month record. On the other hand, the rails themselves and parts-supplier WAB have outpaced the index in the same period. Older cars are falling out of the fleet and leased fleets shrink as cars turn faster.

As a result many of the cars coming off lease are looking for any home at any price, often buying shortline railroad marks for this equipment. At the moment, some 40,000 cars are on the loose bearing the marks of just three shortlines. To the extent that these cars displace system or private fleet leased cars owners and lessors are disincented to make further investments. Then what guarantee is there the shipper will get the requisite car type where and when it's wanted?

Rail economics dictate smaller fleets of fewer car types managed to maximize loaded miles and minimize empty miles. Railroads and leased fleet managers know best what their markets demand. Thousands of cars marked with "flag of convenience" roads, as one wag calls 'em, can only clutter up the system and delay the evolution to the smart fleet of clean, modern cars.

Talk about metrics. Union Pacific treated a bunch of my analyst friends to a pretty powerful presentation in Omaha this week. We've known for some time that at UP a 1 mph increase in average train speed saves 250 locomotive units (at $1.5 mm up a copy, I might add). Now CFO Jim Young adds that the same 1 mph improvement frees up 5,000 freight cars and 150 train crews. Moreover, cutting just one hour of terminal dwell time gives back 2,500 freight cars and an hour of loco dwell time is worth 150 more units. Stands to reason the best way to get capex under control is to use what you got better.

Taking it a step further, Young details (and you can download the PDF slides at www.up.com) how measuring velocity and dwell time impacts costs for car hire, crews and yards. Now skip over to the slides of Dennis Duffy, EVP – Ops, and see how these metric apply in the field. Specifically, note the I-5 corridor specs (Slide 6) and the Marysville story (Slide 10). These are operating savings and customer values generated by using a *network* service design in which every player plays to the system. Local option is not an option. Shortline operators take note.

Short Takes: GATX (NYSE: GMT) garnered a consensus BUY rating on Tuesday citing an estimated $2.41 per share in 2002 over this year's expected $1.24 assuming sharper fleet management… Rail analyst Jill Evans of J P Morgan rates Union Pacific a "Cautious Buy" against the current economic backdrop noting "attractive" valuation and fundamentals… Jason Seidl of ABN AMRO calls Genesee & Wyoming (Nasdaq: GNWR) "our top pick this year," adding that he thinks this the best shortline acquisition market in ten years. [Note: These will be transactions between shortlines; none of the class 1s are talking about any new line sales of any significance -- RHB].

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