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The Railroad Week in Review 4/20/2002

A recent article in *Barron's On-Line* features Hersh Cohen, manager of the $5 billion Smith Barney Appreciation Fund and others for more than 30 years. Says he, "Our best stock last year was probably Canadian Pacific Ltd. which we had owned as a value story. I love companies that have assets that people don't recognize." Recall when the breakup was first announced many of us felt CP as the sum-of-the-parts was worth something north of $45 a share. Cohen kept the hotels "because their properties are great." As for CP Rail, "We kept the rail piece because we liked industrial stocks, and it is a well-run railroad." Sounds familiar, eh?

Henry Posner held forth on the international shortline scene at February's Railroad Financial Forum in NYC . The remarks have been posted on his Railroad Development Company (RDC) website, www.rrdc.com/spch_nyc_2002.htm. Henry's presentations are always thought-provoking, and this one is no exception, comparing ownership trends in domestic shortlines and offshore privatizations. It's an excellent read.

Developing the offshore thread further, a companion piece on Estonia co-authored with Ed Burkhardt ran in the March 2002 *Railway Gazette International*. The argument is that the vertically-integrated North American operating model is well-suited to this environment where the main focus is a bridge route between Estonian ports and the Russian heartland. Download the well-illustrated PDF version at www.rrdc.com/press_releases.html.

RailAmerica (RRA) has won two marketing awards from the American Short Line and Regional Railroad Association (ASLRRA). The first award goes to the Indiana Southern for its new agreement with Peabody Coal to put 110 truckloads daily into rail cars increasing the traffic base by some 20%. The Dallas Garland & Northern was tapped for its commitment to deliver 900,000 tons of stone to two cement plants in central Texas, replacing 36,000 potential truck trips with 9,000 carloads.

Genesee & Wyoming (GNWR) revenue carloads for March 2002 were up for the month and quarter yoy in both North American and overseas sectors. In the former (USA, Canada, Mexico) loads were up 9.6% for the month and 11.7% in 1Q02. This compares favorably with the class 1s, off 2.2% for Mar and 3.8% for the Q. Best quarterly commodity performers were metals, forest products and automotive, reflective of the national trend. It should be noted that absent results from the South Buffalo and Emons acquisitions loads in Q1 dipped 4.3% due to low coal comps.

Class 1s report Q1 results next week. All will be conference calls but CN (Tues) and NS (Wed). If you're interested, dates and times may be found on the investors pages of the individual websites. For a foretaste of the feast to come, see the charts on page 3. Here we see how much of the carload base is intermodal, coal and chemicals. More telling, perhaps, are the per-unit revenue numbers. It will be fun to follow the money when all the results are in next week.

Big Six rail stocks were mixed, with the stocks north of the border heading north and the other four in negative territory by a couple of percentage points. Rail performance YTD generally beat the DJIA, though that's not saying much as it's up a mere percent or so. The big winner has been NS, up 25% followed by CP with a 13% gain with the other four clustered in the under-5% range. As for the smaller class 1s and the shortlines we see FEC the clear winner, up 20%. GNWR and KCS are tied with a 10% gain while RRA has sold off a third YTD.

FEC is interesting because its 2001 performance was nothing to write home about – a swing from a plus 71 cents a share to a minus buck sixty-nine on an 8% revenue increase vs a 65% jump in expenses. The stock price was in the doldrums languishing in the low 20s till mid-Feb when it suddenly jumped seven points and is now in a range at that level. The Feb 12 announcement that the EPIK telecomunications unit was "curtailing other initiatives" may have helped.

Hersh Cohen (see above) among others see this as an asset play where there are both real estate and transportation parts that separately may be worth more than the present aggregation. It's one of the best run railroads around, and has always been a leader in technology and operations – concrete ties, two-man crews, scheduled railroad, bi-directional operation, etc. That's the real jewel in this crown.

A friend who is closely wired to the railway supply industry writes that not only are the car builders having a bad time but also the class 1s may not have been keeping up with their maintenance programs. He feels that fleets may shrink now while business if off and scheduled operations improve cycle time, but the piper will have to be paid when the service initiatives start to pay off.

Trinity (TRN), Greenbrier (GBX) and Wabtec (WAB) are plays in this sandbox, and of the three only WAB showed double-digit gains in stock price over the past six months, up 35%, and that driven largely by its presence in the public transit sector. Interestingly, GATX (GMT) also gained handsomely. Even as better car cycles mean private car fleet operators can move more goods in fewer cars, a deteriorating railroad car fleet means more shippers are forced into privates if they want to stay on the rails.

It will be instructive to see what happens to maintenance expenses yoy next week. One class 1 has seen its bad order ratio increase by about two percentage points a year since 1999, though I'm told efforts are afoot to stem that tide. But anecdotal evidence collected trackside tells me there are a lot of ratty cars out there carrying the marks of every railroad. We may not be down to straw stuffed in the sidesheets of OT hoppers yet, but…

Homework for Earning Week might well include a review of 2001 results, and CSX has published an excellent tool for seeing three years' results all at once. It's their 22-page Financial Supplement, available as a PDF file at www.csx.com in the Investors area. Revenue-watchers will find page 7 particularly helpful for its commodity trends. Note particularly the 7% revenue increase for the carload trade even carload volumes are stagnant. Tells me yields are up, and that's always a good sign.

Roy Blanchard

Disclosure: Blanchard may from time to time hold long, short, or debt positions in the companies mentioned here. A list of such holdings is available on request.

Class 1 Commodity Mix

1Q2002

Percent carloads

Tick	Intermodal	Carload	Coal	Chems
BNI	27.6	72.4	33.9	5.5
CNI	16.4	83.6	14.1	19.5
CP	22.1	77.9	17.9	14.4
CSX	27.2	72.8	23.2	9.1
KSU	15	85	28.8	11.4
NSC	20.6	79.4	28.1	6.7
UNP	20.3	79.7	29.5	10.5

Source: AAR

Revenues per Unit

Tick	Intermodal	Coal	Chems
BNI	$ 778	$ 995	na
CNI	$ 866	$ 660	$ 1,814
CP	$ 876	$ 1,250	na
CSX	$ 555	$ 970	$ 1,655
KSU	na	na	na
NSC	$ 507	$ 897	$ 1,742
UNP	$ 686	$ 1,107	$ 1,756

Source: Indiv RR reports, FY 2001