The Railroad Week in Review
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www.rblanchard.com
(215) 985-1110

BNSF held its Annual Financial Analysts' Meeting in Chicago week before last and yours truly was privileged to attend. Matt Rose opened the proceedings with his observations that there are four clear trends. The US manufacturing base continues to shrink (2.6 mm mfg jobs lost since 2001 – WSJ 11/19) while China and the WalMart retail model grow in impact. There will be more truckload reliance on rail for the long haul, and public-private partnerships will help finance the rail infrastructure expansions needed to handle the growing demands on it.

Rose also spoke to the previously announced 3000+ branch line miles slated for transfer to shortline operators that can deliver cars at 15-25% less expense and absorb the capital requirements for the lines. Not unexpectedly, Rose said they most likely will go to shortline operators with whom BNSF already enjoys strong working relationships. And depending how the current crop of transfers goes there may well be more.

If there was any one theme to the meeting it was building on past experience to produce measurable results. Grain-related shuttle trains, for example, are down to 15 hours load and unload – part of the reason half the shuttle fleet is already booked a year out. Average rail operating cost per ton in shuttle service is 20% less than non-shuttle grain, thanks mainly to spreads in crew and car expense. That is not to say shortlines are shut out. Several (TCW, e.g.) already participate and the door is open to more – as long as the economics work.

The Industrial Products (IP) group represents the shortlines and carload shippers best. But the hard fact is that not all carload lanes are created equal. Success is driven by profitable train-starts and even back-haul capacity. Says IP's Dave Garin, "All costs are variable," meaning he's looking at contribution everything from car hire to infrastructure in evaluating commodity O-D pairs. Restating the shortline message of Denis Smith, it's "simplify, standardize and automate."

Consumer products is a $3.5 bn a year business that's 87% intermodal, leaving a hefty $500 mm in auto and perishables carload products. Drivers are again density and length of haul; apples for Amherst works; oranges for Oakland does not. This is part of the reason BNSF's average consumer products RPU is 14% ahead of the Number Two carrier among North American Class Is. Moreover the consumer products group will likely grow revenues by 7%-8% through 2008, with IP second at 4-5%. Shortlines, talk to me about STCCs 20, 24, 26 and 28 especially.

That leads us to the attached chart of growth performance and prediction. One of my continuing themes is for greater transparency in reporting how the railroad actually works. Here, in one afternoon, BNSF laid out 23 separate compound annual growth rates (CAGR) covering activities from revenue growth to rail replacement. BNSF is, to my mind, the very first road to provide this close a look and what makes the revenue growth rates possible. One would hope others follow.

My wrap is that BNSF is well-positioned to deliver double-digit operating income growth starting in 2004 based in its focus on the Best Practices of railroading, and that the focus on what it does best will add value to the freight service products and to shortline relationships. As to the latter, it will require of shortline partners measurable CAGRs of improvement. The attached list might be a good place to start.

Hours of service for truck drivers appears to have heavy users of truck transportation all in an uproar. Both the *WSJ* and *Logistics Today* cite potential productivity losses ranging from 4% to 8% or more, triggering higher freight rates and more trucks on the highways. The good news is at last shippers will have to be responsible for driver productivity. Time spent pre-tripping, fueling, and waiting at loading docks. One guess where this has been the rule for generations.

The new HOS regs require ten hours rest in 24, up from eight, and reduce duty hours to 14 from 15 per 24 hours. WSJ reports that the government estimates the new rules will add about $1.8 bn in trucking company operating costs. But before you get out the Kleenex, know that last year the highway-haulers had about an 80-share of the $571 billion spent on freight transport.

Some estimate that rates could go up 4% or more. That's on top of making detention charges for driver and equipment delay actually stick. Moreover, HOS will now include hours in the cab not driving, something that has always been lost with mileage-based compensation. It's about time. And as the rails begin to link demurrage and trip time commitments (no penalty for CP-ing an early or late car) we could see further shipper cost advantages to rail as truck penalty charges are factored into the total tab per unit of weight moved.

CSX redux. A long-time reader suggests that I may not have got it right re the 1,000 jobs lost at CSX. I had written, "CSXT says it will offer retirement to about 1,000 non-agreement personnel." The press release says CSX is "streamlining the management structure, eliminating organizational layers…and will reduce the non-union workforce by 800 to 1,000 people." In other words, asked to seek other opportunities. One would wish that the same sense of urgency and passion for that shown by the leadership can now be transmuted throughout the organization.

Elsewhere a review of the STB filings page reveals that CSX has started shedding lines and granting trackage rights to adjacent shortlines. In Alabama 93 miles in two segments went to the M&B. Buffalo & Pittsburgh gets 17 miles in western PA that have been out of service since 1993 but which now can be pressed into service for coal. R J Corman and CSX are swapping trackage rights over 35 mile segments on each to enable certain through service in Kentucky. Golden Isles Terminal in Georgia gets 11 miles of overhead rights to connect a serving yard with its core operations. Take a look around, see what value you can add, and drop Len Kellermann a note.

Export coal may be making a comeback due in part to the cheaper greenback. The AAR reports (via a story in the Norfolk *Virginian-Pilot*) that the combination of a strong US dollar and low third-world ocean shipping rates made US met coal too dear for European consumers. Now the reverse is true, making coal from Australia and South Africa the more dear. That ought to be good news both in Norfolk and in Jacksonville.

Operating Department Changes: At RailAmerica Joe Conklin becomes EVP and COO-North America, replacing Gary Spiegel who is leaving the firm. CP's Ed Dodge retires in March as EVP and COO after 35 years with CP. Fred Green becomes EVP ops *and* marketing Jan 1.

Week in Review will not be published next week. Each year we take a breather at Thanksgiving and Christmas week so you can too. Keep those e-mails coming, though.

Table 1. BNSF Compound Annual Growth Rate (CAGR)

Item	From	To	CAGR%
Intermodal Loads by Segment			
BNSF Total	1996	2002	5.9%
BNSF International	1996	2002	10.1%
BNSF Domestic	1996	2002	2.9%
BNSFDry Motor Carrier	2001	2004E	41.0%
Freight Revenue Growth Model			
Agricultural Products	2003E	2008E	1%-2%
Consumer Products	2003E	2008E	7%-8%
Coal	2003E	2008E	2%-3%
Industrial Products	2003E	2008E	4%-5%
Transportation Productivity			
MGTM*/Transp Employee	1999	2003E	4.0%
Thous. Unit Miles/Transp Emp.	1999	2003E	2.6%
Unit Miles (billions)	1999	2003YTD	2.5%
Average Cars on Line	1999	2003YTD	-1.7%
Engineering & Mechanical Productivity			
MGTM/Mech Employee	1999	2003E	9.5%
GTM/Engineering Employee	1999	2003E	6.0%
Rail Gang Lineal Ft/Employee Hour	1999	2003E	6.0%
Wood Tie Gang/Emp Hour	1999	2003E	4.0%
Rail Replacement in Track Miles			
Curve Rail Relay	1999	2004E	-14.0%
Tangent Rail Relay	1999	2004E	-4.0%
Revenue and Expense Outlook			
Total Revenue	2003	2008E	3%-5%
Operating Expense	2003	2008E	2%-4%
Operating Income	2003	2008E	8%-12%
Operating Ratio	2003	2008E	dn 1%-2%
EPS	2003	2008E	10%-15%

*MGTM = thousands of gross ton miles