The Railroad Week in Review
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Canadian Pacific Chief Operating Officer Fred Green writes in an e-mail, "At CPR's Short Line conference in September, Rob Ritchie had promised to provide an update on our restructuring efforts with the D&H. It has taken longer than we originally thought to sort through this work as we are reviewing several interesting options. We are hopeful that a decision can be made within the next two months and an announcement will be made once we have finalized our restructuring." Thanks, Fred. The world is rife with rumors and it's good to know progress is being made.

CBS Market Watch, an on-line financial newsletter, reports that some rail analysts are changing their positions re who's hot and who's not. We're remarked before that reading the numbers in a vacuum vs. going out on the railroad to look can one lead one to entirely different conclusions. Simply riding the rails and watching for trash and tie butts, brush-cutting and mud pumping up between ties can be quite revealing. Or looking for trains held out of yards and plugged yards. Now comes word that the numbers are catching up to what one sees in the field.

Properties that had been rated "attractive" or "overweight" are swapping positions with those names that had garnered less enthusiastic ratings. One writer concedes that differing growth strategies and attention to economics of running a railroad will actually affect profitability. Both **BNSF** and **NS** have gotten upgrades; **CSX** and **UP** have come down a notch.

In a separate report, analysts gave the rails credit for a customer base across the very commodity makers whose stocks have been on a role of late: forest products, metals, primary foods (grains and sweeteners), and chemicals. **BNSF** and **NS** are given good marks trading as they are at the low end of their historical range, 11-15 times forward earnings. Moreover, both are down a bit from their Jan highs, perhaps creating new opportunities for the contrarians among us.

UP's troubles stem in part from crew-hiring decisions made more than a year ago. Insufficient crews mean insufficient relief when crews go on the law or have to deadhead from A to B (and in some cases back again). Consequently T&E comp costs go up while GTMs per gallon, average train speeds and revenue per train-start all head south. Long-time WIR readers may recall these UP tidbits from earlier writings: a one MPH decrease in average train speed means doing the same work requires 250 more locos, 5,000 more freight cars, and 180 more crews.

Also this week S&P cut its short-term credit rating for CSX, citing "sub-par operating performance." The outlook was downgraded to negative from stable. S&P held the long-term "BBB" debt ratings **Conrail** while revising the outlook to negative from stable. The corporate credit rating for Conrail is set at the lower of the corporate credit ratings on CSX and Norfolk Southern.

Re last week's remarks on the **Watco** approach to operations planning, a friend writes, "This is not a railroad. This is a transportation company. I was also impressed in that [in the website photos] every senior executive is wearing a tie and jacket for the formal picture. (Founders are allowed to wear what they want) I wouldn't be surprised to see them dress this way when they face their customers or regulators. The majors could learn from this."

“Watco is doing everything possible to communicate *and* make it one-step simple to contact them. On any level. I know nothing about them but I would probably buy the stock were it public.” This from a guy who is a shortline co-owner, a railroad investor, and hedge fund operator.

Progressive Rail Inc. (PGR) out of the Twin Cities (WIR 12/19/2003) is cut from very much the same cloth, self-described as a “business development” company. In just a few short years they have grown from a few miles of ex-CP branchlines to an integrated network of more than 100 miles of owned and leased track over several fallen-flag lines south of Minneapolis.

Tim Eklund, their VP-Industrial Development, is a dear friend and recently he’s shown me more of the stuff of which PGR is made. I had the opportunity the other day to look over Tim’s shoulder at some PGR operating and financial metrics. The quality and diligence of the work is worthy of a public company. I mention this because at some shortlines getting customer and operating data is like pulling teeth – they just don’t have it organized.

I’ve also found the more disorganized the shortline with their own internal processes the more difficult time they have getting the attention of their connecting Class I railroads. It must be remembered that in any new business agenda with a Class I the shortline is the seller and the guy on the other side of the table is your customer. The surest way home is to put your Unique Selling Proposition (USP) in terms of benefit to the buyer.

But before you can even identify your USP you have to know what makes you unique and the competitive advantage your service offers the customer. And there’s no better way to tell your story than with solid performance metrics. Thanks, Tim, for the lesson.

Another shortline success story concerns Pennsylvania’a **Everett Railroad** (ERR), now celebrating its 50th year of operation. EVRR started out with four miles of track acquired from the bankrupt Huntingdon & Broad Top Mountain Railroad & Coal Company. Then in 1982 Conrail closed the branch line connecting ERR to the rest of the world. Two years later ERR started anew with eight miles of ex-PRR and in the ensuing years added another 17 miles. ERR connects with **NS** at Hollidaysburg.

Today, under the leadership of entrepreneur Alan Maples, ERR averages a healthy 100 cars per mile per year. The distinguished customer list includes Appleton Papers, Cargill, Pennfield Feeds, A.P. Green Refractories, and Roaring Spring Paper Products. The railroad employs nine people and owns four locomotives. An office is located in Duncansville, PA, and a repair shop in Claysburg, PA.

Australia’s Pacific National, a joint venture of Toll Holdings and Patrick Corp., will pay **RailAmerica** AUS$ 285 mm (US$ 214 mm) cash for 100% of the latter’s Freight Australia ownership. The closing date will be in 2Q04 and represents a double-plus of the US$103 mm RRA paid in 1999. (Doubling your money in 5 years implies a CAGR of 14.4%. using the Rule of 72. Not bad.) Chairman Bill Pagonis said in a press release that $59 mm in senior debt will be retired.