THE RAILROAD WEEK IN REVIEW
MARCH 17, 2006

"*UP is blowing away expectations, but just scratching the surface." – Jason Seidl, Credit Suisse*

Union Pacific on Tuesday -- after markets closed -- raised its 1Q06 eps estimate to a range of $1.00 to $1.10 from an earlier estimate of 80-90 cents per diluted share based on new projected 17% revenue growth on a 4% volume increase. UP says in a press release that the revenue upside is driven by strong demand for Intermodal, Industrial Products and Agricultural Products, somewhat offset by lower than anticipated coal volumes. First quarter operations benefited from mild winter weather, network management initiatives and capacity improvements, which combined to improve margins. Estimates for the full year are now $4.80 to $5.00 per diluted share, reflecting higher first quarter expectations.

Morgan Stanley's Jim Valentine writes, "Our thesis is unfolding earlier than expected. The upward guidance further confirms our long-term view that it has the most upside potential of any major railroad as it has the most under-priced contracts and the most operational turnaround potential. Identifying exactly when these two tenets will unfold is difficult to pinpoint, which is why we've suggested investors look at the stock with a 2-3 year view. We've never questioned if these trends would unfold but rather the speed, which appear to be playing out sooner than expected."

Over at Credit Suisse rail analyst Jason Seidl writes, "Pricing and demand continue to be strong in 2006, and we are confident that there is still room for additional upside. Despite a setback from lower than anticipated coal volumes, UP has leveraged strong demand in other commodities and spun it directly into margin improvement and, as a result, expected earnings growth. Things can get a lot better from here. Investors should note that we are merely scratching the surface when it comes to the underlying earnings leverage that exists at UP."

Union Pacific stock (UNP) gapped up 7% to $91 at the open Wednesday and stayed up for the week. A very good sign as so often a stock will gap up on good news and fall back by half or more after reality hits the buyers. Taking a longer view, UNP's 52-week low was $60.85 and it traded in a range of $60-70 until late Oct 2005 when it took off.

From Nov thru Jan the weekly chart rides the high edge of a Bollinger Band based on a 20-week moving average plus or minus two standard deviations. Then in early Feb the stock started moving sideways again and after hitting $90 Mar 7, tanked to a low of $83.50 on Mar 8. The present gap up gets us back to where we were two weeks ago, only with one important difference: positive guidance. And best of all, it rubbed off on the other rails.

Ken Hoexter, Merrill's rail guy, upped his estimates on five buy-rated rails citing the potential further upside surprises in the group making the names "solid investments." Before the end of trading Wed UNP was up 5.4%, BNI up 5.4%, CSX 3.8%, NSC 3.7%, CNI 1.4% and CP up 1%.

Class I revenue units increased 2.4% yoy in Week 10 driven exclusively by intermodal, up 8.7%, offsetting declines in merch carload and coal. Observes Morgan Stanley's Jim Valentine, "Economically-sensitive traffic was down 0.7% year-over-year in Week 10, which was better than the 2.3% year-over-year decline for the last four weeks, but down 2.2% sequentially." The big losers percentage-wise were nonmetallic minerals, metallic ores, chemicals and forest products, though combined they account for less than 7% of all carload freight.

Ed Wolfe at Bear Stearns writes, “Overall volumes had declined yoy in the prior four weeks, driven by weather-related network congestion and tougher yoy comps. While we believe that the cold weather effects from February are no longer a headwind, our sense is that volume growth remains somewhat depressed as a result of several company-specific issues that continue to drive softer volumes. We note that the yoy comparison was easier this week than last, particularly in the intermodal segment.”

Valentine also reports that service metrics are on the mend. The tables in his March 16 note show that in the train speed department CP and CN have done exceptionally well with yoy improvements of 16.5% and 7.9% respectively. BNSF fared least well, down 6.6%, followed by NS slowing down average train speed by 1.2%. CP and CN also took the honors in terminal dwell improvement, down 32.4% and 18.2% respectively. Third place went to CSX, down 12.7%. BNSF again fared least well with terminal dwells up 4.6% thus far in 2006 vs the same period in 2005.

Genesee & Wyoming stock (GWR) split 3:2 before the open on Wed and as announced in the Feb 14 earnings release. The new price is right around $32, which means that anybody buying GWR in mid-May 2005 would have doubled their money by now. Nice. Know any dot-coms doing as well?

Elsewhere, North America revenue loads (US, Canada, Mex) for Feb 2006 increased by 11,011 units or 20.7% largely on gains from the June 2005 Rail Management Corp (RMC) acquisition. Excluding 1,091 carloads from the First Coast Railroad which GWI started operating April 9, 2005, and 10,472 RMC carloads, North American traffic in February 2006 decreased by 552 carloads, or 1.0%.

This decrease was primarily due to a 729-carload decrease in U.S. lumber & forest products traffic and a 584-carload decrease in GWI's Mexico region, which continues to be negatively affected by the impact of Hurricane Stan. These decreases were partially offset by an 805-carload increase in coal coke & ores traffic. All other commodities decreased by a net 44 cars. Also, starting in February 2006 GWI is including former RMC haulage traffic within the other commodity groups and which had not previously been included in the revenue unit totals. See Table 1.

RailAmerica revenue units for Feb 2006 were 103,249, down 2.8% from 106,256 in February 2005. The acquisition of the Alcoa railroads and the Fremont line in Michigan net of the impact of the sale of the San Luis and Rio Grande Railroad and the three Alberta properties accounted for a decrease of 1,772 of the carloads. On a “same railroad” basis, February 2006 carloads decreased 1.2% to 100,367, from 101,602 in February 2005.

Nine out of fourteen commodity groups had decreased shipments in February 2006. The 1,235 carload decrease was driven primarily by lower shipments of Chemicals, Paper Products and Intermodal. On a “same railroad” basis for the same period, carloads were 207,537 up 2.3% from 202,846 in 2005. “Same railroad” totals exclude carloads associated with railroads, or portions of railroads, sold or acquired by the company after January 1, 2005. See Table 1.

RMI’s RailConnect Index for Week 8 ending 2/25/2006 puts shortline cars up 2% for the month and 6% YTD with 247 railroads reporting. Farm and Food (ex grain) loads more than doubled yoy to 64,200 units. The other double-digit increases came in STCCs 14 and 32 (15.6% YTD) and intermodal, most of which is for port-serving shortlines that report through RMI. By way of comparison the AAR reported combined US and Canadian carloads ex-IM on 13 properties up 0.5% yoy and intermodal up 4.2%.

Once again, shortline merch carload percentage gains look better than what the trunk lines are getting. The reason, I think, and based on what I’m hearing from shortline operators, is their greater ability to customize service to meet the inbound logistics and inventory management needs of their customers. Take for example…

The Livonia Avon & Lakeville in upstate NY. The LAL has a reputation for taking care of its customers, so much so that Barilla America, the world's largest maker of pasta products, has chosen to site a new $96 mm pasta plant and distribution facility on LAL in Avon, NY. Says LAL President Bill Burt, "The presence of an independent, locally-managed short line railroad with multiple Class I railroad connections and a good safety record played an important role in the selection."

Burt adds, "Feeling at home in Avon was much emphasized. Part of that is that LAL is already habituated to the service requirements of food manufacturers. In Avon and Lakeville we provide Sweeteners Plus, ADM, Frank Perdue, Kraft General Foods, and Howlett Farms with some of the most intensive rail service available anywhere."

Construction starts in June. The pasta plant will be approximately 100,000 square feet and the warehouse and distribution facility (in partnership with Jacobson Warehouse) will be 200,000 square feet. It is estimated that 120 jobs will be created. Operations are expected to begin in 2007 and full production will start in 2009. Barilla is headquartered in Italy

Unrelated to Barilla, LAL anticipates a summer 2006 completion if its welded-rail project between Lakeville and Avon as well as a complete upgrade to CWR between Avon and Henrietta. The projects are part of a $4.2 million rehabilitation program is being funded by the company and grants from New York State DOT.

Dakota Minnesota & Eastern is featured in the March 2006 issue of Fortune. I think the writer did a great job capturing the essence of goals and the challenges and I recommend it highly. The title of the piece is "What it Takes to Build a (21st Century) Railroad" and it changed my way of thinking about using RRIF loans to build new railroad.

Capacity expansion is the buzzword today, and the perceptions of coal buyers (see Monday's WSJ) is there isn't enough rail capacity between BNSF and UP to move all the coal the utilities want moved. The DME project (see also www.demrail.com) adds capacity and the purpose of RRIF loans is to add capacity, albeit mainly by fixing deferred-maintenance lines, though the DME's goal is a logical extension. Give it a read and see what you think. To be continued.

FreightCar America (RAIL) gapped up four points in early trading Wed after languishing in the low $60s for the past two weeks. Also on Wed the *WSJ* ran a Page One feature on the railroads' travails in meeting the coal needs of the utilities they serve, particularly from the PRB. The sub-head, "A 5,833 Hopper-Car Deficit," may have been taken by some as a sign that more cars are to be built in a hurry. Actually, that number, buried deep in the run-over on page A15, refers to the number of carloads needed to bring one particular plant up to its normal reserves.

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Table 1. Feb 2006 and 2006 YTD Revenue Units

	2006	2005	2005	2005	Change	Change	2005
RRA	**Month**	**YTD**	**Month**	**YTD**	**Month**	**YTD**	**ch MTM**
Jan	112,829	112,829	105,507	105,507	6.9%	6.9%	
Feb	103,249	216,078	106,256	211,763	-2.8%	2.0%	0.7%
GWR							
Jan	69,114	69,114	52,705	52,705	31.1%	31.1%	
Feb (1)	64,327	137,594	53,316	106,021	20.7%	29.8%	1.2%

Source: Company material

(1) Starting in Feb 2006 GWR includes RMC haulage not previously reported in commodity groups.

Note: GWR revenue units do not include operations at the former RMC Port of Galveston and Port of Wilmington, accounted for as switching revenues (non-freight) along with GWI's other port operations.

RailConnect Index of Short Line Traffic

Traffic Type: All

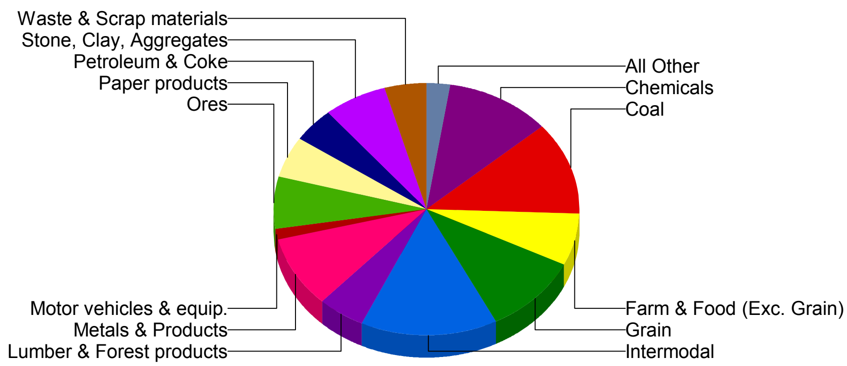
For the week ending: 2/25/2006

Week Number: 8

Carloads Handled	Current Week			Year-To-Date		
	2006	2005	% Change	2006	2005	% Change
Coal	14,201	13,641	4.11%	115,078	112,172	2.59%
Grain	12,241	12,339	-0.79%	97,807	91,802	6.54%
Farm & Food (Exc. Grain)	11,112	3,944	181.74%	64,200	30,040	113.72%
Ores	7,975	9,120	-12.55%	61,919	70,968	-12.75%
Stone, Clay, Aggregates	7,791	7,358	5.88%	63,402	54,841	15.61%
Lumber & Forest products	6,029	6,395	-5.72%	45,772	44,222	3.51%
Paper products	6,547	6,795	-3.65%	52,323	52,241	0.16%
Waste & Scrap materials	5,541	5,492	0.89%	42,272	41,249	2.48%
Chemicals	12,954	13,764	-5.88%	106,990	107,776	-0.73%
Petroleum & Coke	5,580	5,784	-3.53%	42,482	41,804	1.62%
Metals & Products	11,456	12,447	-7.96%	87,667	89,015	-1.51%
Motor vehicles & equip.	2,312	2,689	-14.02%	15,336	15,928	-3.72%
Intermodal	15,985	17,477	-8.54%	138,439	124,802	10.93%
All Other	3,269	3,288	-0.58%	23,424	23,982	-2.33%
Total	**122,993**	**120,533**	**2.04%**	**957,111**	**900,842**	**6.25%**

RailConnect Index

Year-To-Date



All Other	2.4%
Chemicals	11.2%
Coal	12.0%
Farm & Food (Exc. Grain)	6.7%
Grain	10.2%
Intermodal	14.5%
Lumber & Forest products	4.8%
Metals & Products	9.2%
Motor vehicles & equip.	1.6%
Ores	6.5%
Paper products	5.5%
Petroleum & Coke	4.4%
Stone, Clay, Aggregates	6.6%
Waste & Scrap materials	4.4%
Total:	100.0%