RAILROAD WEEK IN REVIEW
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"There are a lot of socialists out there wearing capitalist suits" – Larry Kaufman in Argus Rail Business re some rail shippers' efforts to persuade Congress to re-regulate railroads.

What do Mexican truckers, major league baseball and some shortlines have in common? Each is embroiled in situations where special interests are trying to get Congress to interfere with market forces. Seven years ago the terms of NAFTA were supposed to open US access for Mexican long-haul truckers, eliminating the requirement to transfer loads to US truckers with 25 miles of the border. The week the Administration moved to make good on treaty commitments. Needless to say the Teamsters are not happy with real competition and so they care calling their chits on the Members bought and paid for in recent elections.

Major League Baseball wants to open TV access to games to more of its fans and so asked satellite carriers to bid on the opportunity to carry some 60 out-of-market games a week. Comcast was not happy and turned to Senators Kerry and Specter (Boston and Phila are two franchises where Comcast dominates) to intervene. Thus as MLB seeks to open access to more games to more people, the Members are being asked to protect the interests of established Big Money.

Meanwhile some short line railroad owners are turning up the heat on Congress to subsidize their businesses where the markets cannot. As those who follow – and invest in – the railroads know, this is a capital-intensive business of wasting assets. Keeping tracks, locomotives and office machines in good repair requires revenue that in turn comes from offering customers a competitive advantage no other supplier can offer. Lose that competitive advantage and revenue falls off, depriving the enterprise of the capital necessary to offset the wasting effects of running a railroad. Thus the appeal to congress is to preserve a service that customers find *un*appealing.

The Teamsters cannot offer a competitive advantage to shippers sufficient to offset the economies of Mexican truckers operating deep in the heart of Texas and elsewhere. Comcast and Time Warner cannot offer a competitive advantage over DirecTV for fans who want to watch more games. Many shortlines cannot offer a competitive advantage over trucks or Class I transloads. Does this mean the taxpayers have an obligation to protect the status quo?

I think not. The first task of any business owner is meeting the Marketing 101 requirement to "find a need and fill it." The business bookshelves are filled with how-to books on the subject: Michael Porters *Competitive Advantage*, Tom Peters' *Thriving on Chaos*, and of course the Peter Drucker door-stop classic, *Management – Tasks, Responsibilities, Practices*. Happily, there are many [iron] horses that when led to this water have drunk deeply: Indiana Rail Road, Watco, GWR, North Shore Group, Ohio Central, Anacostia & Pacific and others.

And it's a continuing education. Every week I talk with shortline marketeers who are looking for ways to enhance their competitive advantage. They follow market trends, national economic forecasts, railroad analysts' client notes and magazines from *Fortune* to *Railway Age* to *TRAINS*. But the number of these aggressive, creative market managers pales next to the number of short line operators who ignore their customers then come crying to the ASLRRA for help shouldering their way to the federal trough.

If there is one place the shortline community needs help it's in Marketing 101. Yet there is only one 40-minute breakout session (before lunch on Tuesday) on the ASLRRA Annual Meeting program that addresses this dire need. Yes, there are five other "marketing" sessions however they deal with specialty markets, rate-making (which the typical handling line can't control anyway), and the award winners. Congress ain't the answer, guys. Pull up your marketing socks and get on with it.

Canadian National First Quarter earnings are expected to be off 5-10% yoy as a result of severe weather, strike impact and operational disruptions during the period. CEO and President Hunter Harrison puts it this way: "The first quarter of 2007 has been an extremely challenging one for CN. Severe weather conditions in western Canada in January and February disrupted operations of CN and many of its customers.

"We then had a 15-day strike by 2,800 members of the United Transportation Union in Canada, followed by another bout of harsh weather, which caused landslides that have interrupted operations of both major railways in British Columbia. We expect a tough first quarter, but our recovery program is ongoing and we will continue to make every effort to deliver diluted earnings per share growth of 10 per cent-plus for the full-year 2007." The 1Q07 earnings call will be 4/23 at 1630 EDT.

Sometimes the blogosphere offers insights one does not get in press releases. Posting on *Seeking Alpha*, George Gutowski writes, "Once management starts to warn, there is a tendency to wash out an assortment of other problems under the guise of previously-announced problems. Right now in the executive suite you have both forward momentum pressure and increasing operational friction. This will eventually cause financial brake failure. When Q1 is released, listen to how any forward statements are hedged. Unless they are complete kamikaze pilots, they will start loading up the caveats and looking for cover." We'll see in a couple of weeks.

Meanwhile, CN is building a C$20-million transload operation and intermodal rail terminal at Prince George, B.C., to serve Pacific Rim markets starting this coming fall. Prince George, situated 500 miles east of Prince Rupert, is ideally located to tap backhaul export opportunities, filling empty containers moving to Asia via Prince Rupert with lumber, panels, wood-pulp and paper, as well as ores, plastics and some metals products.

CN's new Prince George transload facility, with an 84,000 square-foot warehouse and 10 acres of outside storage, is expected to open in fall 2007. It will load containers with products arriving at the facility by rail or truck. The loaded containers will then be lifted onto IM platforms at CN's new adjacent intermodal rail yard, and daily service will be offered from this terminal to the Port of Prince Rupert. The intermodal terminal will at the outset have a capacity of 500,000 TEUs.

It will be far-reaching, too. Chicago media maven Bill Fahrenwald writes that the Memphis *Commercial Appeal* picked the CN release, noting that "The up-tick in Memphis will be nearly immediate. About a third of the containers will come directly to the CN-CSX intermodal yard at Frank C. Pidgeon Industrial Park in Southwest Memphis, providing business for air freight carriers, barge lines and trucking companies. It also will provide options for Memphis exporters and importers who will now gain access to Asia through the less-congested Canadian port."

Norfolk Southern estimates that 1Q07 diluted eps will be down about 3% yoy or 70 cents vs 72 cents. Revenue units were off more than 4% reflecting declines in the automotive and housing sectors. Norfolk Southern also experienced winter weather conditions in first quarter 2007 that were more extreme than the comparatively mild weather a year earlier, resulting in a slowing of operations and increased costs. Analysts surveyed by Thomson Financial are currently forecasting first-quarter earnings of 75 cents a share on revenue of $2.35 billion.

A year ago, Norfolk posted a first-quarter profit of $305 million, or 72 cents a share, up from $194 million, or 47 cents a share, in the year-earlier period. Shares of Norfolk Southern were off 3.1% in after-hours trading to $49.47. Wall Street was not particularly worried with three leading analysts seeing minimal impact on NSC's valuation going forward. If somebody wants to sell me their NSC shares for $50 or less I'll take 'em as the company *still* has an intrinsic value of $73.

Adding insult to injury, the UMWU has gone on strike at two App coal mines served by NS and CSX. Credit Suisse metals & mining analyst David Gagliano notes these two represent 10% of total Northern Appalachia output with combined annual production run-rates north of 13 mm tons. To which Credit Suisse rail analyst Jason Seidl adds, "We are not adjusting our forecasts for NSC or CSX at this time [though] we do point out, however, that Eastern Class I railroad coal volumes (among other franchises) trended negatively throughout 1Q07 and today's events do not set the railroads out on the best footing for 2Q either."

Greenbrier (GBX) will likely post a loss in its fiscal second quarter on weak demand for some of its products, has withdrawn earnings guidance, and has announced plans to close its money-losing boxcar plant in Canada. For the quarter ended Feb. 28, Greenbrier posted a loss of $6.1 mm vs. a profit of $8.6 mm during the same period a year earlier. The results included a loss of $7.9 mm related to the planned fiscal third quarter closing of the Trenton Works, the rail car plant in Nova Scotia acquired in 1995.

Sales edged up 2% to $240 mm from $236.2 mm yoy though analysts expected $295 mm. Revenue from the company's core manufacturing segment fell 40% to $119.2 mm from $184.8 mm during the same period a year earlier. Greenbrier blamed a slowdown in demand for double-stack intermodal cars and forest products cars, losses at Trenton Works, and greater-than-expected labor costs on certain marine and railcar orders.

We had kind of expected this as faster railroads are getting more turns out of the existing intermodal fleet. BNSF has said it will get 20 more trains a day over its transcon once the double-track program is complete. NS has said it will start hauling more international Pacific Rim trade out of Savannah meaning shorter hauls port-receiver and better turn times. Prince Rupert (above) and Lázaro Cárdenas (WIR 3/16) will also impact platform utilization in North America.

Commenting on the announcement, Bear Stearns' Peter Nesvold writes in a client note, "Continuing manufacturing gross margins of 6% were better than our forecast of 5% [even though] restructuring noise muddies a deep analysis of the manufacturing margins. The consolidated gross margin of 14.8% appears to be better than expected with a potential for a FY2008 turnaround. Moreover, we were pleasantly surprised to see a backlog that was flattish sequentially at 14,300 cars -- particularly given that backlog visibility feels to be at trough-like levels industry-wide, with the exception of tank cars, and to a lesser degree covered hoppers."

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