THE RAILROAD WEEK IN REVIEW
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"Apparently 'tis better to be politically correct and to avoid Washington's wrath than it is to be economically correct and invite that wrath." Dennis Gartman, Gartman Letter, Dec 15

Now that RailAmerica has gone public, we can see the monthly carload-commodity progress reports. I must say they are encouraging if only because the results are indicative of the changes the Giles team hath wrought since buying the company three years ago.

Total carloads for November 2009 were 67,834, down 8.3 percent from 73,953 in November 2008. In the second quarter of 2009, the Company restructured a customer contract, which resulted in the Company recording the revenue derived from that contract as non-freight revenue instead of freight revenue and carloads. Excluding the effect of this contract, carloads were down approximately two percent for November 2009 compared to November 2008.

Three of RA's 12 commodity segments showed year-over-year growth for November 2009 when compared to November 2008. Agricultural Products were up 28 percent primarily due to a delayed harvest in the Midwest. [*RailAmerica is using the same commodity groups and nomenclature as the AAR, so "ag products" includes all STCC 01 grains plus 204, grain mill products, and 20 923, soy meal -- rhb*]. Motor Vehicles were up 56 percent due to a new production facility in the Midwest and a general increase in the movement of new automobiles. Waste & Scrap materials were up three percent.

Year-over-year carloads decreased in the other nine commodity groups. The largest decline was in the Other commodity group and was primarily due to the restructured contract mentioned above. Continued softness in residential construction took down the Non-Metallic Minerals & Products and Forest Products commodity groups and reduced demand for Metallic Ores & Metals hit that group.

Things appear to be improving on a sequential basis. October was down 20 percent year-over-year while November slipped but eight percent in the same period. And November was off only three percent from October's count. The quarter-to-date is off 15 percent from 2008.

The AAR reports US November freight rail carloadings were down eight percent compared with the same month last year and down 17 percent compared with November of 2007. However, if Thanksgiving week were excluded, November would have been the highest volume month of the year for US railroads.

While rail carloads are still down overall, December's Rail Time Indicators report illustrates that the recovery in US manufacturing seems to be continuing. The Purchasing Managers Index (PMI), which measures how U.S. manufacturing is faring, was at 53.6 in November (PMI over 50 is thought to indicate growth in the manufacturing sector.) If manufacturing is growing, improvement in rail carloads of raw materials, like chemicals and steel which are used in the production of goods, could be seen next month.

Though not particularly germane to short lines, US intermodal traffic was down seven percent compared with November 2008, and down 14 percent compared to November 2007. Consumer confidence rose to 49.5 in November 2009 from 48.7 in October 2009. Since much of rail intermodal traffic consists of consumer goods, the strong positive correlation between consumer confidence and consumer spending indicates that rail intermodal traffic could increase in the coming months should consumer confidence continue to trend upward.

“November’s traffic numbers, when considering the effect of the Thanksgiving week, are generally positive,” said AAR Senior Vice President of Policy and Economics John Gray. “Rail traffic is still down significantly in comparison to 2007 numbers, but the economic indicators in December’s report lead us to believe that our nation’s economy continues to improve.”

Jason Seidl at Dahlman & Rose writes, "Volume growth is within reach. Week 48 traffic represented the fifth consecutive single digit volume decline. The latest weekly decline of five percent is largely in-line with the prior week’s six percent and confirms further stabilization which is likely to be followed by growth before year end. Looking forward, we believe that volume improvement is likely to continue over the next few weeks with changes in rail traffic possibly turning positive in any given week in the remainder of the year, especially in weeks 50 and 51.”

Looking at Week 48 vs Week 47, ag products were essentially unchanged, chems rose 11 percent against up seven percent the week before, and coal slipped a point to minus 15 percent versus the prior week’s decline of 14 percent. QTD rail volumes were down tenp percent and YTD volumes were down 17 percent, unchanged from the prior week.

On the truckload side, RW Baird’s Jon Langenfeld writes, “Truck freight remains stable, but signs of month end spot activity. Truckload demand showing seasonal build in October and November as inventory destocking stopped, auto production demand continued and seasonal imports increased. Industry anecdotes reflect stronger spot market activity to end the month, which was likely a function of lean inventories. We look for trends to turn sustainably positive yoy in 1Q 2010.

Signs of the times. Greenbrier and GE have renegotiated their railcar manufacturing agreement to decrease the number of new tank cars and hopper cars to 6,000 units from 11,900 to be delivered over an eight-year period. Thus far only 600 units have delivered under the original contract. According to a press release, "Greenbrier will build the first 3,800 tank cars and hopper cars by July 2013. The remaining 2,200 tank and hopper cars are subject to fulfillment of certain contractual conditions by both parties in their sole discretion and would occur over the next five-year period."

The announcement does not specify open-top or covered hoppers but either way the meaning is clear. If open-top, coal demand is down, there are few if any new coal-fired gen-stas on the books, and the cars that remain are turning faster thus reducing the number of units required to sustain a given basic load. As for tank cars and covered hoppers, we're talking chemicals and grain.

Taking Year through Week 48 numbers, 2009 grain loads, excluding grain mill products like soy oil and soy meal, are off 12 percent. Chemicals, excluding petroleum, are down ten percent. Given the volumes at hand, we're looking at a quarter of a million loads. Add to that the railroads' trend to running faster and smarter, taking days out of car cycle times, and one can quickly see fewer cars are needed to move a given amount of product tonnage. Take tonnage out of the supply chain and the number of cars diminishes yet further. So it's not hard to see why car builders are challenged.

Greenbrier said its total firm new railcar manufacturing backlog as of Nov. 30 is 4,900 units valued at approximately $430 million. This figure excludes the contingent production of 2,200 units for GE. Based on current production plans, 2,000 units in backlog are scheduled for delivery in Greenbrier’s fiscal year ending Aug. 31, 2010. Greenbrier delivered 350 new railcars during its first fiscal quarter ended Nov. 30, 2009.

Anecdotally we're hearing from some short lines that are on the mend car-wise. Pennsylvania's Reading & Blue Mountain writes to say they are seeing gains across a broad spectrum of commodity groups including wood pulp, beverages, fertilzers and plastics. My sources add that carload decreases in commodity groups are being offset by gains in frac sand destined for the Marcellus Shale gas fields, a growth business in this part of the world for a number of area short lines.

And finally, North Shore Rail Group's Todd Hunter sent along these shots of G. O. Hawbaker's new salt transload facilty (WIR 10/17/2009) on the Nittany & Bald Eagle Railroad at Pleasant Gap, PA. By way of review, this is Penn DOT rock salt from American Rock Salt Co. -- a relatively short-haul move off the Rochester & Southern in upstate NY.

Here the new 42-inch belt radial telescoping stacker literally dwarfs a standard hopper car. But that's not all. Hawbaker is in the process of installing two 4.7 million gallon asphalt tanks for railroad transload here as well. Todd says they've done 300 cars of salt to date and expects another 300 cars before this season's end.

Fertilizer is another commodity that cries out for transloads on short lines. I've seen piles of the stuff at ports like Tampa, so why not replicate the Hawbaker infrasctructure in places like Kansas? The time may be right, too.

A "Morning Call" note from Monday deals with CF Industries' proposed takeover of Terra Industries, however the important thread for our use is CF Board's opinion that the fertilizer sector has strengthened significantly in recent months. CF concludes, "Moderate gas costs and the broader recovery among Terra's agricultural and industrial customer base is expected to drive rising demand and improving margins for Terra's upgraded nitrogen products [and] market consensus is shifting to reflect the brighter near-and long-term prospects for the entire sector."

The Reading & Northern's recent AN experience may be the tip of that particular iceberg. Elsewhere in fertizer land, a note from UBS says potash prices in Brazil have recently declined from $485 per metrric-ton landed to $400 per metric-ton as non-Canadian suppliers chase volume. UBS says this equates to $370 per metric-ton fob Vancouver. It appears that producers have been trying to lower investor expectations to $320-350 a metric-ton for the Chinese contract, so a price above $350 a meric-tom might be seen as a positive.

Robert Easton, Treasurer of the Providence & Worcester Railroad, retired this month. The Form 8-K filed with the SEC used the word 'resigned', leading a number of us watching the New Railroad scene to what Chop Hardenbergh aptly called "a flurry of speculation." In response to my note questiong the language, P&W President writes, "Bob Easton worked at P&W for more than 23 years, most of them as the Company's Treasurer and CFO. Bob decided to retire, and P&W appreciates his many years of hard work and dedication. Elizabeth Deforge, assistant controller for nine years, has been appointed Treasurer of the Providence and Worcester Railroad Company.

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