THE RAILROAD WEEK IN REVIEW

September 24, 2010

"Competition has been reduced to groveling for government intervention." -- Wall Street Journal*, Letters to the Editor, September 22*

The AAR's September 3 *Rail Time Indicators* publication has revenue units for August, 2010 up 5.7 percent over August 2009 yet still down 11.6 percent from from August 2008. The AAR says it's also the highest weekly average for any month since November, 2008 and reverses a string of three straight months in which average unadjusted carloads fell in absolute terms. The last week of August, 2010 saw the highest US carload total (302,358) of any week so far in 2010.

Combined August, 2010 US and Canadian carloads ex-intermodal but including coal increased 7.8 percent over August 2009 but were off 10.7 percent from August, 2010. The only positive 2010 vs 2008 number in the entire chart is for intermodal containers, up 6.6 percent, which is not surprising. For carload commodities, however, the "90 percent is the new normal" rule seems to be holding. Consider, for 2010 vs 2008: agricultural products and food down 5.8 percent; chemicals and petroleum down 4.3 percent; coal down 10.7 percent; forest products down 21.9 percent; metallic ores and metals down 16.0 percent; automotive down 9.1 percent; non-metallic minerals and products down 9.8 percent, other (including waste and scrap) down 21.2 percent.

RMI's RailConnect Index for Week 34 (August 28) has some better comps over 2009, up 8.7 percent including intermodal; ex-intermodal (where most short lines live) it's even better, up nearly 10 percent. Next look at the August and year-to-date volumes for GWR and RailAmerica. Both are running in the 70,000 unis per month range, though GWR includes its Australian food and aggregates business in the total. GWR August loads increased 11.6 percent where half the gain was Australian grain, and a sixth was new chemicals business on the B&P/Ohio Central. The month was up 3.0 percent over July and loads through August gained 6.7 percent.

At RailAmerica, August carloads increased 3.5 percent year over year and slipped 1.2 percent compared to July, 2010. Year-to-date loads grew 6.8 percent, a virtual tie with GWR; the July-August, 2010 delta was -1.2 percent. At RA, 50.7 percent of total loads are spread across just three commodities: coal, agricultural products and chemicals. The chemicals group was up 16.0 percent over August, 2009 while coal slipped 4.6 percent and ag products barely held its own.

In sum, the short lines as a group lagged the Class Is in year-to-date comps in coal, chemicals, metallic ores and metals, while maintaining an edge in forest products including paper, grain, aggregates and scrap. Drilling down still further, GWR and RA were both up in more commodity groups than down. What this tells me is the short lines are saving the class Is' bacon in the lower-rated, non-unit train commodities. It also tells me that as more Class Is move to the Eyeris pricing model they will find their legacy cost assumptions at risk, meaning more opportunities for the short lines that can make money in forest products, aggregates, non-unit grain trains and

-- who knows -- maybe even in lanes where intermodal isn't the low-cost provider it's cracked up to be.

The Kindness of Strangers comes in many forms where short lines are concerned, and there is none stranger than the dog's breakfast of funding programs from state to state. Happily, the American Association of State Highway and Transportation Officials (AASHTO), in collaboration with the American Short Line and Regional Railroad Association (ASRRA) has prepared a website that compares the offerings.

The profiles are sorted by state so you can compare things like the type of financing, the program objectives and criteria, project eligibility, qualifications for applicants, procedures and links and contacts for more information. Here's the link: http://www.aslrra.org/legislative/Short%5FLine%5FFunding%5FAlternatives/ . For additional information on this potential resource for public funding needs, contact Keith Borman at kborman@aslrra.org .

And while we're on the subject of handouts, the FRA has published a Notice of Funds Availability (NOFA) to fund rail line relocation and improvement projects. Approximately $20 million, rooted in SAFETEA-LU Act appropriations, will be made available for construction projects undertaken for the improvement of the route or structure of a rail line that either, 1) are carried out for the purpose of mitigating the adverse effects of rail traffic on safety, motor vehicle traffic flow, community quality of life, or economic development; or 2) involve a lateral or vertical relocation of any portion of a rail line.

The FRA further notes that, in order for a project to be considered, the rail line must be the element that is moved or improved. Grade separation projects that involve raising or lowering a road, for example, are not eligible. Similarly, quiet zone and stand-alone crossing improvement projects are not eligible, nor are station improvement projects where there is little or no related track work. But for short lines operating in commuter zones (Morristown& Erie, Chicago South Shore, NewYork & Atlantic, to name three), the commuter agency picks these us and always finds it necessary to move track when improving stations -- see the South Shore's gauntlet tracks for station platform clearance, e.g.

Speaking of passengers, the Looney Award for the week goes to the FRA and the federal government. According to a note in Chop Hardenbergh's excellent *Atlantic Northeast Rails & Ports* letter, the Northern New England Passenger Rail Authority (NNEPRA) is in line to get FRA funding for the Amtrak *Downeaster* service extension to run north from the present terminus in Portland. With this project Maine would be the first state in the country to begin construction using the high-speed rail federal stimulus funding. So far so good.

It now turns out the "Buy American" mandate Congress tied to the funding actually has teeth. Chop writes, "There has been no progress in the NNEPRA's application to the FRA for a waiver to use foreign-made [track] nuts. The UTU and the BLET filed complaints against the NNEPRA waiver application stating that American-made nuts can be found and purchased by the NNEPRA. The waiver request of the NNEPRA should be denied, because track-nut fasteners are readily available here in the homeland, produced by American workers."

I don't think that's any way to do business -- any buyer ought to be able to pick any vendor who can supply the right parts at the right price. If the feds think they can dictate the terms because it's their (really the taxpayers') money, forcing recipients to do business exclusively with "government-approved suppliers," then perhaps the price is too dear. Maybe Maine should say, "No thanks," and walk away. Let autos and buses on I-95 be the transport medium of choice.

Meanwhile, the Coalition Against Bigger Trucks (CABT) has formally opposed the Obama administration's call to make permanent the pilot program that allows trucks weighing up to 100,000 pounds to travel on federal interstate highways in Maine and Vermont. The provision was contained in the Administration's proposed "continuing resolution" plan for fiscal year 2011. So here we have one arm of Our Government saying you can't build that railroad unless you use our choice of vendor and another arm has, in the words of the CABT release, "proposed something that would undermine [further] investment in our roads and rails." Kinda puts the nut case in proper perspective.

Health Insurance costs are hitting short lines hard. At the recent ASLRRA Eastern Region meeting in Baltimore I spoke with a number of operators of short lines big and small and everybody was talking of health insurance costs in five figures and more per employee family. Moreover, they are budgeting for annual increases in the 10-15 percent range. My contacts also noted that health insurance generally does not cover work-related injuries because workers comp steps in. Except for railroads where there is no worker's comp thanks to FELA. The icing on the cake is the recent healthcare legislation that triggers certain benefit levels when payrolls reach 50 individuals. One chap told me he has 50 on the payroll right now, is resolved not to hire any more, and may even let one job go to stay under the dreaded 50.

Consider: allowance-based short lines average about $300 per car. Thus a short line with 20 employees and a heath care program costing $12,000 each needs the revenue from 800 carloads just to pay for health insurance. Roughly a third of shortline revenues go to comp and benefits on the income statement so a line with 10,000 cars a year and revenue of $3 million is paying out a $1 million in comp and benefits. With a payroll of 20, it works out to $50K fully-loaded payroll expense for each employee. Take $12,000 a year out of that and it leaves $38,000 for the pay envelope and Railroad Retirement. The chief accountant for a shortline group doing 36,000 loads a year says the anticipated hit of of another $12,000 in health insurance exposure is making them think hard about adding to payroll.

Closing tidbit: Over the pest ten months I've been able to observe first hand traffic volumes and operating practices on UP, CSX, NS and CP. I see a lot of freight moving and moving well so I have a problem with the gloom-n-doom pictures we get from econo-pundits. In fact, I think rail share prices are actually below intrinsic value. To be continued next week.

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