THE RAILROAD WEEK IN REVIEW

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"Whether it's our DNA of innovation or the benefit of our supply-chain collaboration, you can see that it's driving very strong and solid results." -- Claude Mongeau

The Canadian National short line meeting in Montreal on Wednesday was a brief affair, as shortline meetings go. CN had set the morning aside for one-on-one meetings between shortline managers and their CN marketing counterparts in the latters' offices, something I've not seen before in this venue. We then kicked off the formal proceedings with a terrific buffet lunch and off to the meeting room for the presentations du jour.

CEO Claude Mongeau opened the session, stressing CN leadership in taking a supply chain approach to transportation management. He said CN is actively engaged building a franchise that gives customers a competitive edge in their own markets. And the short lines, with their crucial first and last mile services, are key. And to prove his point, each of the afternoon's speakers drilled down into the myriad ways CN's shortline partners -- a term used repeatedly -- can support the supply chain model.

Chief Commercial Officer Jean-Jacques Ruest took the dais next and with no slides and a few notes held forth on how CN differentiates itself by railroading for customers and not necessarily the operating ratio. They do it by knowing where the supply chain starts and where it ends, designing transportation services that serve the needs of both.

Take coal: how much is ready to move at origin, how much is needed at destination, and what CN must do to pick up and deliver the right amount at what time. For export coal, vendors in Australia and the United States are courting the same Pacific Rim customers as the Canadian mines. As an active supply chain participant, CN aims to give its coal customers the competitive advantage needed to win that Pacific Rim business. [This just in: CN on Thursday announced an agreement with Coalspur Mines to develop a logistics supply chain for transporting thermal coal from Coalspur's Vista coal project in Alberta to Western Canadian ports starting in 2015.]

Whether coal, grain, ferts, autos or frack sand, the same process applies. Lather, rinse, repeat. Being flexible, said JJ, is paramount. With only six months' visibility, one lacks the luxury of long-term predictions for specific commodity O-D pairs. But with a menu of options from unit trains to single-car, dock-to-dock or transload, CN-direct or with a partner short line, what JJ called "One CN" offers one-stop shopping. And to do it right, one must know the customer's buying behavior. It's here the Short lines shine.

Building on what JJ said about "One CN" and Claude's observations on the franchise, Corporate VP for Marketing Doug MacDonald showed how the supply chain solution process begins with "smart stakeholder engagement," or getting all supply chain participants to buy into the concept that time is money, that velocity drives asset utilization and that low incremental cost is really a "supply chain enabler," in Doug's words.

Short lines can help the enabling process along by helping customers look at their supply chains backwards, starting with destination requirements and working back to what must happen when at origin to meet those destination needs. Believe me, this is a far cry from trying to win single-car moves with the lowest rates and a box of cigars.

To tie the whole supply chain package together, General Service Delivery Manager Shauntelle Paul briefed us on CN's CustomerFIRST initiative, finding "touch points" and "pain points" in customer relationships through a series of customer surveys. (During the Q&A, Ed Foley of the SLR suggested that CN partner short lines be part of this survey. Applause.) The three biggest pain points, she said, are communications lapses, inconsistent service delivery and not warning customers about service failures or what's being done to fix them.

"Getting it right the first time is absolutely essential in the first-mile, last-mile world where short lines live," she said, "and being able use customer touch points to drill to down to root causes of performance failure is a powerful supply chain tool." However, stepping outside Shauntelle's remarks for a moment, getting to root causes requires accurate event reporting, an area where I find some at CN sense that not all short lines are performing equally well.

I got the same message at the recent BNSF shortline meeting, a point writ large by their "Velocity" initiative that keeps cars moving but depends on accurate shortline event reporting to be of any value. Moreover, proper short line event stats show at a glance where customer behavior is adding to variable costs, impeding velocity and degrading asset utilization.

But I digress. The afternoon's presentations were refreshingly brief, kept the number of individual power point slides to a minimum, kept what slides there were simple with a few talking points easily visible from the back of the room, and spoken in a conversational manner. And no jargon. The singular supply chain partnership message was abundantly clear and I for one was glad to hear it.

CSX export coal continues to generate comment from the analyst community. JP Morgan rail analyst Tom Wadewitz spent a few days interviewing CSX senior managers in Jax recently and comes away saying, "Looking to 2012, management is expecting ... flat to up export coal volumes....Underlying CSX's constructive view on their export coal business in 2012 is the expectation of about five percent growth (driven by China and India) in the total seaborne coal market (met and steam coal). This in turn provides room for Central Appalachian coal exports to sustain the 2011 strength even as Australian production returns to a more normal level."

The way I see it, export coal is the tail wagging the corporate dog. Year-to-date export coal is less than a quarter of total coal tonnage (see chart). Coal is less than 20 percent of total RTMs and 32 percent of total YTD revenues. By this measure, increasing export coal tonnage by five percent adds roughly 45,000 tons (five percent of nine million tons) a quarter.

CSX						
Coal split - mm tons						
3Q2011	**3Q2010**	**Change**	Domestic	**YTD 2011**	**YTD 2010**	**Change**
28.5	30.2	-5.6%	Util	83.40	90.50	-7.8%
3.7	4.2	-11.9%	Other	10.20	10.70	-4.7%
32.2	34.4	-6.4%	Total Domestic	93.6	101.2	-7.5%
8.8	6.6	33.3%	Export	29.80	21.90	36.1%
41.0	41.0	0.0%	Total coal	123.4	123.1	0.2%
2.3	2.3	0.0%	Coke & Iron Ore	5.8	6.0	-3.3%
43.3	43.3	0.0%	Total coal commod grp	129.2	129.1	0.1%

CSX total YTD coal revs were $2.8 billion; call it $3.7 billion for the year across 164 million tons (123.4 over three times four). At this rate, adding 5 percent more export coal increases total coal tonnage to 166 million, an increase of less than two percent. Hardly a rounding error.

Much better we focus on CSX's merchandise business, 53 percent of total revenues. Buried deep in Tom's note at the bottom of page six is this important observation: "CSX's efficiency program focused on local carload operations is a notable productivity driver. Essentially, the program is focused on making the local pick-up and delivery more efficient. We believe that this is an area of real cost savings opportunity [yet] it is one of the most complex operational challenges as it also requires input and flexibility from the customer in order to drive improvement."

That's why scoring shortline interchange performance against the ISA and measuring on- off-shortline dwell time are critical.

The STB has dodged the Open Access bullet -- for the moment. On Friday the STB took the position that it would "defer a decision on NITL's petition to institute a rule-making pending our review of the issues and arguments presented in EP 705" (*Competition in the Railroad Industry*, served Jan. 11, 2011). In the notice, the Board urged the parties to focus on, among other things, reciprocal switching. In July NITL filed a petition for rule-making, in which it proposes revised competitive switching rules and urges the Board to seek public comment on its proposal.

There are those who see this deferral as chickening out. A reader suggests, "We have a de facto monopoly working. With no competition, there's no incentive for the carriers to provide better service. The STB's job is to oversee the railroads. There is a big difference between gridlock and just plain not doing your job. This is the latter." Comments welcome.