THE RAILROAD WEEK IN REVIEW

December 20, 2013

"Our infrastructure takes a beating from freight. The Rail Freight project will include replacing rail, culverts and switches." — Steve Weaver, Strasburg RR Superintendent

Pennsylvania has 67 short lines, more than any other state in the country, and the State Transportation Commission is doing its part to keep them healthy. The state has earmarked nearly $26 million for rail-freight projects, most of which is for track improvements on existing lines. But the largest award, $10 million, is for a new crude-oil receiving terminal on the grounds of the old Eddystone electric generating station just south of the Phil airport. The site is in the Conrail Shared Assets area served directly by both NS and CSX. See table following disclaimer.

Two of the three "govt" projects will benefit short lines. The Pennsylvania Northeast Rail Authority contracts with GVT Rail's Delaware Lackawanna Railroad for freight operations and the Lycoming Valley project is on the North Shore Rail Group's Lycoming Valley Railroad. All the projects will add value to the state's vast single-car railroading franchise; Norfolk Southern is the chief Class I beneficiary with CP and CSX each capturing niche markets in agricultural and industrial products.

Though the $16 million for short lines and their customers looks good on the surface, I have to wonder how much of it will result in additional carloads. The general AAR trend for industrial products carloads — that is, just about everything except coal and intermodal but including crude and auto — shows small year-over-year improvement since the 2009 low point. The December 6 Rail Time Indicators has the group's average weekly Nov loads for the US rails hovering around 95,000 for every month every year starting in Nov 2011 through Nov 2013.

Non-Class I industrial products carloads also declined over that period. RMI's Week 48 (end of Nov) RailConnect report for 2013 shows a nine percent decline from what it was in 2011, to 94,000 units from 103,000 units. Metals are down 2,000 units; chems, ex-STCC 291 petroleum and STCC 131 crude, down 500; waste down 1,200; paper off 1,400; aggregates off 2,700 units. Let's hope these track rehab projects support new business niches as opposed to dragging out what seems to be a going-out-of-business sale.

Success in the grant-getting business takes flexibility and creativity. Take the WNYP in NY, where a new rail bridge on its former Erie right-of-way near Falconer in is nearly complete, on-time and under budget. The bridge in question had failed a 2011 inspection for the minimum federal weight requirements. At the same time, WNYP had won $1.6 million in state funding for tie replacement. But, says railroad President Carl Belke, the need to replace the bridge trumped the tie job and, "After receiving permission from the NYDOT, we moved the funding from replacement of the ties to the construction of a new bridge."

Wrap-up work includes construction of a walkway and the restoration of a 1½-acre site classified as wetlands, says Belke. Work should be completed by next May. Being under budget means about half a $million remains for other work, which Belke would like to apply to its original purpose, tie replacement, between Olean and the Pennsylvania state line.

Strasburg Rail Road, well-known for its steam train operations, finds itself in the enviable position of having to add track capacity for a blossoming freight business. A year or so ago Superintendent Steve Weaver told me it was coming and showed me how and where they were running out of room in the existing track footprint.

The freight franchise, while still in its infancy, has grown from fewer than ten cars a year to several hundred. The freight cars are significantly heavier than the historic passenger cars in regular service, increasing GTM exposure significantly. Thus the Rail Freight Assistance Program grant.

In a separate Pennsylvania shortline development, Reading & Northern has filed a lawsuit seeking to stop the Pennsylvania Northeast Regional Rail Authority from extending its operating contract with the existing operator for another five years. In its press release, R&N says the Authority took the action "without notice and with no opportunity for public comment."

From the wording of the press release, it would appear the R&N asked for permission to submit a bid to replace the current operator but was rebuffed. R&N maintains that for the past 20 years the Authority "has continually renewed the contract with the current operator without notice." Says R&N President Wayne Michel,"We realize that given an open process with fair bidding that there may be others who win the right to operate. However, we know taxpayers and shippers will be better off as a result of this process and we will have had a fair opportunity to participate."

Reading & Northern's own operations are contiguous to and connect with the Authority's property. R&N has extensive operations in the area today, so there could be some benefit from economies of scale. I say this because one reason GWR has been so successful is its knack for assembling short lines that physically connect, as opposed the the "any railroad any place" MO of some no fallen-flag short lines like RailTex.

By way of background, R&N was one of the first Conrail Express short lines 20 years ago and has built a successful carload franchise over former CNJ, Reading, PRR and Lehigh Valley properties (I go back to the original fallen flags so you can get a sense of how everything fits and where the service area lies). Moreover, *Railway Age* has twice cited Reading & Northern as Regional Railroad of the Year since 2000. R&N is the only railroad in the country to win twice in that period of time.

Montreal, Maine & Atlantic Trustee Robert Keach has signed a sales agreement for the railroad assets to be purchased by Railroad Acquisition Holdings LLC for $14.25 million.

Though not confirmed, indications are that Holdings is affiliated with Fortress Investment Group in NY, owner of the Florida east Coast Railway and seller of RailAmerica to GWR.

The sale is not a done deal yet. Railroad Acquisition Holdings is what's known as a "stalking horse" bidder. In a bankruptcy auction, the stalking horse is a company that promises to buy the bankrupt company's assets for a certain price unless a better and higher bid is obtained during the auction process. This is anticipated to be the opening bid in an auction, Trustee Robert Keach told the *Bangor Daily News*.

Early in the bankruptcy process, Keach hired the Gordian Group, a New York investment bank specializing in financial restructurings, mergers and acquisitions, to help secure a potential buyer for the railroads assets. *BDN* reports that some 20 potential buyers emerged. Railroad Acquisition Holdings was one of those parties, signaling its intention to keep the MMA intact, continuing to operate the railroad on both sides of the border. The court must first approve the stalking horse sale agreement; if it does, other bidders will have until Jan 17 to get their bids in. The auction begins Jan 21.

MMA was set to resume operations in and around Lac-Mégantic last Wednesday, having pledged to carry no oil products through the town. And, based on my homework, it's doubtful they ever will. Sources say CN is now providing direct service into the Irving refinery at Saint John, Irving is buying Permian and Eagle Ford crude by the foreign-flag boatload from the Texas Gulf, CSX continues to deliver Bakken crude to the Buckeye Terminal at Albany for boat or barge beyond, and of course we have the established CSX-Pan Am Rail-Eastern Maine rail route direct to the Irvings. Given the number of superior alternatives, it's hard to see any competitive advantage for the MMA route.

This is the final Week in Review installment for 2013. I'll punch out a note for Jan 3 but will skip Jan 10 as I'll be out with 60 or so railroad professionals for the annual Moonlighter's ride on Via Rail's Canadian from Vancouver to Toronto Jan 10-14. We will surely see up close and personal how well CN's vaunted winter plans (WIR 11/15/2013) are really working. I'll pick up these and other pieces Jan 17 with 4Q earnings right behind.

	Owner	Amount (000)		For
Phila Energy Solutions	Indep	$	10,000	Crude-oil terminal
Corman/Pa	Corman	$	3,900	tunnels, yard exp.
WLE	Indep	$	2,800	Track rehab
Erie IDC	Govt	$	2,600	export wood pellets
AVR	Carload Express	$	1,300	Track rehab
Strasburg	Indep	$	1,100	Added freight vols
Three Rivers Marine	Indep	$	1,100	Frack sand term
WNYP	Indep	$	840	Track Rehab
ESPN	Regional Rail LLC	$	645	New Track
POHC	GWR	$	525	Track rehab
Penna NE Rail Auth	Govt	$	463	Track rehab
Lycoming Cty	Govt	$	370	Reactivate ind tk
York Rail	GWR	$	168	Track rehab
Totals		$	25,811	