THE RAILROAD WEEK IN REVIEW

May 2, 2014

"In some Michigan locations we had more than 17 feet of snow and Ohio saw the coldest winter in 142 years." — GWR President Jack Hellmann

Genesee & Wyoming got hammered by the winter unpleasantness. Some 45 of GWR's 100-plus North American railroad names — 4,800 route-miles of railroad and a third the usual income stream — not only took direct hits from the storms themselves, but also took indirect hits from the connecting Class Is' own difficulties. GWR estimates they lost $15-20 million in revenues due to shipments not shipped and took on an extra $12 million in operating expense for, among other things, fuel, overtime, car hire and snow removal.

By the North American numbers: To begin, the GWR safety culture is paying off — even with the treacherous working conditions the first quarter PI index was 0.7 reportables per 200,000 hours worked; next target is 0.45. Revenues and revenue units both grew by four percent in the quarter; RPU was unchanged at $559. Merch cartloads including auto and ag were up two percent. The five biggest merch commodities by revenue — forest products, metals, chems (ex petrol prods but including ferts), and ag — were mostly up.

Total NA freight revs came to $229 million. Non-freight sales (primarily contract switching and the Atlas engineering support firm), added another $71 million for total NA sales of $300 million, unchanged year-over-year. NA operating expense was unchanged in spite of the weather effects and ops income was up two points to $56 million. The OR shed 24 basis points to 81.4.

Corporate revenues increased 40 basis points to $176 million and consolidated operating income was $75 million, down two points. Net income available to GWR shareholders was cut in half to $40 million (73 cents a share) thanks mainly to incomes taxes: a $25 million credit last year became a $23 million liability this year. Hellmann said on the call they don't expect to recover from "the significant first quarter weather shortfall," but do see 2014 pre-tax income growing by more than 20 percent including the DM&E acquisition, expected to close momentarily.

That's a credible growth target. On the call Hellman said they've seen "sharp increases in traffic levels in March." True. Up 18 percent over Feb, with Midwest and Ohio Valley coal up 15 percent. From WIR April 18:

Year-over-year, metals, 11 percent of vols, were up seven percent; pulp & paper, ten percent of vols, up eight percent; and minerals & stone, nine percent of vols, up nine percent. All-in, these four of the six commodity groups representing 79 percent of GWR vols (chems and wood products are the other two) increased year-over-year car-counts by more than five percent. Tells me the business is out there if you just go get it.

And go get it they will. North America generates 80 percent of sales yet only 75 percent of operating income, which indicates margins are higher elsewhere (the Aussie OR is 75). What GWR clearly needs to do is continue the March momentum to grow NA revenue carloads more quickly from the present portfolio, lest the "serial acquirer" — one who buys other companies to offset moribund organic results — label be applied. We know it's out there. Year-over-year GWR North American loads increased 5.4 percent in 2013, besting the best Class I (BNSF) by a point and on a par with the RMI shortline universe of 438 names.

This week's NEARS (North Eastern Assn of Rail Shippers) spring meeting in Providence broke all attendance records with more than 200 souls registered, split about evenly among people who make or can influence carrier selections, railroads, and vendors including car builders and leasing companies. As usual, topics were timely and wide-ranging. The shippers panel members represented the metals, minerals and petroleum products commodity groups and the message to the rails is simple and direct: be consistent, move my leased cars, do what's promised and tell us when you can't, and we look kindly on truck conversions — even to boxcar (!!) — when you consistently meet the above criteria.

That said, the speaker addressing mis-routings from data entry and planning moves ahead of time did not get a straight answer when shippers and logistics planners were asked about planning moves around transit times and tracking trip-plan compliance. Note to self: how can you beat up on the railroads for inconsistent transit times when you don't know when you launch a car what the trip plan requires? We know that not all trains run every day, so it's crucial to time the release so as to hit yards on days the connections are scheduled to run.

The Mexico Connection intermodal panel — possible government-caused rail service degradation and the auto companies, e.g. — was a perfect lead into the regional railroad panel, where the theme is look what we can do by ourselves and why the government is best ignored. Pan Am Rail SVP Mike Bostwick talked about new hires (50 percent more T&E, three out of five employees with fewer than ten years of service), coping with and building on business mix shifts, being an equal opportunity player with its connecting roads when it comes to putting together customer-friendly routes.

GWR's Ed Foley, newly promoted to VP Business Development for the eastern half of the Northeast Region, once again stressed the need to reduce asset dwell and measure everything. He said there is a role for government support with grant and loan money that can accelerate infrastructure improvements that enhance the rails' ability to support customer-specific supply chain needs.

Susquehanna's Jim Howarth rounded out the panel discussion with a different tack, saying his road's biggest opportunities lie in rail-truck transfer and proceeded with a number of unique, value-adding case histories: rail-to-truck asphalt; rail-to-container-export grain, and filling up the West New York service area with vest-pocket transloads for autos, forest products and even trash.

I chaired the railroads operations panel. We had no PowerPoints and took brief opening statements from the panelists: where you work, what keeps you up at night, and what customers can do to make the railroad interface work better. We zeroed in on the NEARS service area with John Gaylord, CSX Terminal superintendent out of Albany; Norbert Denzer, Northeast ops super for CP; and Robert Lewis, AGM for the NS Northern Region. We then went straight to the Q&A, and where there was a lull in the Q's I'd turn to specific audience members to draw out points I knew were there.

In a nutshell, the railroads need accurate carload volume forecasts with timely updates, being ready for railroad switch crews when they arrive at the gate (we'll tell you when we're on the way), reporting loaded and empty car releases promptly, keeping the industry track you own in good repair, and meet with our boots-on-the-ballast trainmasters to address mutual concerns before they become headaches. The shippers and third party logistics providers (TPLs) want the rails to show up as planned, tell us when you can't, and please get advance train consists from your connections (this from an ethanol shipper).

Happily, it's mostly common ground: Rails say tell us what you're putting on us and be ready for us when we get there. Beneficial owners and TPLs want consistent and reliable transit times that meet specific supply chain requirements. Sounds easy enough. Perhaps for the next NEARS outing I'll suggest a panel with speakers representing a Class I, a beneficial owner, and a regional or local rail carrier. We'll talk in terms of successful case histories with what worked and why, soliciting audience challenges during the Q&A.

Iowa Pacific Holdings and the Zell organization have filed a Notice of Exemption (FD 35816) with the STB that three Zell entities are to acquire an 80-percent equity interest in the railroad operating company. The remaining 20 percent "remains with Iowa Pacific senior management." The filing notes that none of the nine railroads under IPH control connect with each other, that the transaction does not lead up to making them connect, and that the transaction does not involve a Class I, so the 49 CFR prior approval requirements to not apply.

Personally, I see this as a great plus for Iowa Pacific. The group has opened previously light-density lines in Texas and NY to sizable new traffic flows and is adding value to several Class Is' shortline partnerships by adding capacity in terms of asset-management. IPH President Ed Ellis has always called himself a "work-out guy" — taking properties that others have shed and making them work. The Zell thesis appears to be much the same, only in real estate and newspapers. Ellis needs an equity hit to perpetuate his service business, Zell is in the business of assembling properties to create equity. Well done.