RAILROAD WEEK IN REVIEW

February 7, 2020

"These new models are by far the best iPhones we've ever shipped with advanced technologies and unprecedented leap in battery life and our best-in-class camera experience. We have been wild with the photos customers have shared in our all-new Night Mode photo challenge this month." — Tim Cook, CEO, Apple

"We're anticipating a high energy level at the March 9 event, which will be the first Short Line Workshop since our Sales & Marketing realignment in 2019. You'll hear from Mark Wallace, EVP Sales & Marketing; Jamie Boychuk, EVP Operations; and Farrukh Bezar, SVP Sales & Marketing." — Tom Tisa, Head of Business Development, CSX

"Goldman Sachs is nearing a deal with Amazon to offer ***loans to small- and medium-sized businesses*** *over the e-commerce giant's platform. Goldman, which has begun building technology to facilitate the project, could launch by the end of March."(Emphasis added.) — Almost Daily Grant's, Feb 4*

"What's actually happening is incremental. What matters most is what happens on the margin. With Consumer Discretionary showing 24 out of the 63 companies reported, they have now recorded negative earnings for the third quarter in a row." — Keith McCulloch, Hedgeye.com

What do Apple and the railroad industry have in common? A core mission to create customers. What do they not have in common? A customer focus on earnings calls. Case in point: Apple CEO Tim Cook opened his December quarter earnings call saying, "Our active installed base of devices reached a new all-time high for each of our main product categories and geographic segments," adding,

> The iPhone 11 was our top-selling model every week during the December quarter and the three new models were our three most popular iPhones. We had double-digit growth in many developed markets. We saw double-digit growth in all five of our geographic segments and established new all-time records from multiple categories as well as setting a December quarter record for the App Store and AppleCare.

Contrast that with any Class I railroad opening remarks on any earnings call. Norfolk's Jim Squires would be a good example.

> 2019 was a remarkable year of transformation at Norfolk Southern. We launched our TOP21 operating plan to transform our railroad while fulfilling our commitment to dramatically improve our service product as we become more efficient. Our results today demonstrate this organization's strong momentum in streamlining our operations and making substantial progress toward our long-term commitments.

And even though both audiences were financial analysts, Cook put his focus on what Apple is and how it increases earnings whereas the railroad guys start with earnings and back into customer benefits. Squires ends his opening remarks by saying that, despite revenue unit declines for the quarter and year, “We remained focused on running our railroad as efficiently as possible and with a high level of customer service.”

BNSF has announced a $3.4 billion capex program for 2020, down five percent from the $3.6 billion investment made in 2019. According to the January 31 Customer Notification, the plan “reflects our emphasis on keeping the network in the best condition it has ever been as well as expansion projects aimed at meeting customer demands.” Moreover,

> The largest component of this year’s plan, approximately $2.55 billion, will primarily be for replacing and upgrading rail, rail ties and ballast and maintaining our rolling stock. This year’s maintenance program will include approximately 11,000 miles of track surfacing and/or undercutting work and the replacement of approximately 489 miles of rail and nearly 2.7 million rail ties.
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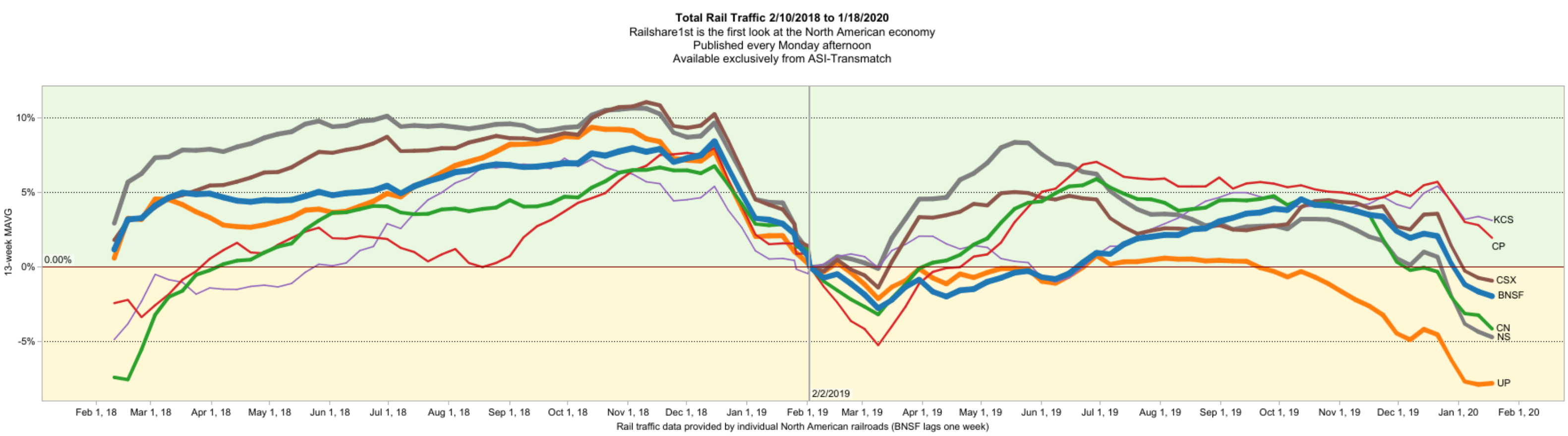
> Approximately $581 million of this year’s capital plan has been allocated for expansion and efficiency projects. Most of these projects are focused on key growth areas along BNSF’s Southern and Northern Transcon routes.

This track bed excavation is for a siding extension project on the Phoenix line at Ash Fork, Arizona, just south of the Williams junction on the ex-Santa Fe transcon. Genesee & Wyoming’s Arizona & California short line, winner of the BNSF Short line of the Year award, joins the Phoenix line at Wickenburg.

BNSF did not have a good 2019. For the full year, the railroad handled 10.7 million revenue units, down 4.5 percent. Industrial products and ag were off 3.7 percent at 2.9 million revenue units. Intermodal was off 4.5 percent and auto dropped 3.8 percent. Coal plus coke slid 5.9 percent. Consumer Products (auto+intermodal) is the largest commodity group at 53.2 percent total volume, followed by merchandise (ag+industrial) at 28.9 percent and coal/coke has slipped to 17.9 percent.

Of the 16 merchandise commodities, only Petroleum Products, Grain Mill, Waste and Other posted year-over-year YOY increases. Of these, Petroleum Products (4.5 percent of total units) was the most significant increase, and that was mostly crude oil. In short, the ag and industrial commodities where short lines and regional railroads live were all down. We'll have the official full-year details when Berkshire reports in a few weeks.

This downdraft has hit everybody in this chart that sets all to zero a year ago. BNSF is the dark blue line in the middle; KCS is on top with CP hot its heels; UP fares least well. I think it's significant that the middle of 2019 sort of flattened out, only to take a dive starting Oct 1.



The pundits are saying we're not out of the woods yet, though we ought to see some relief starting July-ish. AAR Senior Vice President John Gray tells *Railway Age*, "Nine of the 20 carload categories we track had year-over-year gains in January, the most in a year, and several other commodities had carload declines in January that were less pronounced than they've been in recent months. It's too early to say if the worst is behind us, but railroads are hopeful that 2020 will see an improved business climate and rising volumes across much of their traffic base."

Color my fingers crossed.