RAILROAD WEEK IN REVIEW

March 5, 2021

"However, the Board does have serious concerns about section 5.14(b) of the Purchase and Sale Agreement, which restricts B&LE from ***ever*** *seeking access to FGLK and NYSW—whether directly or indirectly, before or after the Transaction, even through means other than the Transaction." — STB Decision on CSX sale of Massena Line to CN (emphasis theirs)*

"Norfolk Southern will obtain trackage rights over existing lines owned by four railroads (CSX, PAR Railroads, a GWI subsidiary, and PAS) to allow NS additional flexibility with respect to its existing service to intermodal and automotive facilities at Ayer, MA, and Berkshire & Eastern, currently a Class III rail carrier and a wholly-owned subsidiary of GWI, will replace Springfield Terminal as the operator of PAS." — CSX filing for Pan Am Rail, FD-36472

"Our second and third most valuable assets – it's pretty much a toss-up at this point – are Berkshire's 100% ownership of BNSF, America's largest railroad measured by freight volume, and our 5.4% ownership of Apple… Your railroad carries about 15% of all non-local ton-miles (a ton of freight moved one mile) of goods that move in the United States, whether by rail, truck, pipeline, barge or aircraft. By a significant margin, BNSF's loads top those of any other carrier." — Warren Buffett, Chairman's Letter, February 7, 2021

Another flag in New England railroading has fallen. With the acquisition of Pan Am Rail by CSX, the only long-time constant railroad ownership on the New England railroad map has gone. Yes, the name Pan Am Railways only appeared in 2006, but that was a mere name change for the Boston & Maine and the Maine Central as the same ownership had been in place since 1981. Only Vermont Rail is older, dating back to 1964 as the *operator* (not owner) of the Vermont-owned former Rutland as the result of its acquisition of the property in 1961.

In that year, 1981, Timothy Mellon, heir of the Mellon family of Guilford, Connecticut, teamed up with ex-Penn Central employee Dave Fink (father of PAR president David Fink) and formed Guilford Transportation as a vehicle to acquire railroads following the 1980 Staggers Act. In short order they acquired both the Maine Central and the B&M, forming a single-line haul of more that 400 Miles between Rotterdam Jct., NY, and Mattawamkeag, Maine, as well as a number of New England branch lines.

The Pan Am moniker came in 1998 when Guilford bought the name, colors and logo of Pan American World Airways, with an eye toward entering the airline business. That didn't work out, and in In March 2006, Guilford Transportation Industries changed its name to Pan Am Systems, and the Guilford Rail System was rebranded as Pan Am Railways (PAR).

In the meantime, Canadian National had sold its Central Vermont to RailTex, in turn bought by by RailAmerica and then GWR with its acquisition of RA. CN's Portland, Maine line went to

Emons Transportation as the St Lawrence & Atlantic, thence to RA and GWR. Canadian Pacific exited its Saint John Line across northern Maine with its 1995 sale to Canadian American Railroad, buying it back in 2019 after a succession of shortline operators had not done well. And in 2016, GWR bought the Providence & Worcester, further solidifying its New England presence.

The New Haven Railroad and New York Central's Boston & Albany became Penn Central in 1968 and Conrail in 1976. Both went to CSX as part of the 1999 Conrail spit between CSX and NS. In short order CSX sold the Springfield-New Haven line and Waterbury branch to RailAmerica as the Connecticut Southern (CSO), which also went to GWR in the RA transaction.

The Pan Am Southern joint venture of 2008 between Pan Am Rail and NS was the latter's attempt to re-enter the New England Market, using a structure very much patterned after Norfolk's successful Meridian Speedway partnership with KCS. PAS operates between Mechanicville, NY, and Ayer, Mass, on the former B&M. it also operates as far south as New Haven with a combination of ownership and trackage rights.

CSX now takes direct ownership all Pan Am Rail properties, splitting PAS ownership with Norfolk Southern, contracting with GWR to operate the former Pan Am Southern as the Berkshire & Eastern through its Pittsburg & Shawmut subsidiary. The STB filing is FD 36472, dated February 25, 2016. Pertinent points:

** This is a "minor" transaction because it does not involve the merger or control of two Class I railroads;
** CSX obtains control of all PAR railroads, eventually merging all but one into CSX;
** GWR's Berkshire & Eastern assumes the role of PAS operator; CSX assumes PAR's 50% ownership of PAS, NS retains the balance;
** B&E must set PAS rate levels "that are competitively neutral" to connecting rail carriers;
** NS reroutes one intermodal/automotive train pair per day[1] over the B&A, connecting to Ayer over the for P&W/B&M line between Worcester and Ayer;
** No railroad customer will see a reduction in its number of serving carriers;
** Shortline connections are unchanged;
** Existing gateways will be preserved;
** CSX is "not able to quantify the benefits but expects that rail traffic will increase organically" over time;
** CSX acquires the PAR properties with a combination of cash and CSX stock;

[1] The trackage rights will give NS a faster and fully-cleared route for intermodal trains which currently run as single-stack trains east of the NS intermodal terminal at Mechanicville, N.Y., due to clearance restrictions in Pan Am Southern's 4.75-mile Hoosac Tunnel in western Massachusetts. On the B&A max train length is 9,000 feet due to siding lengths. The re-route cuts running time by three hours and eliminates the dwell added by the single-stacking operation now required at Mechanicville.

** CSX may “at any time” sell all of its 50 percent interest in PAS to NS or a third party. NS may after seven years sell its half-ownership of PAS to a third party (*Could a “third party” be GWR? — rhb*) ;
** The STB serves its final decision in 180 days and it becomes effective in 210 days.

And so it begins. The proposed transaction will allows CSX “to improve rail service and to provide efficient, competitive rail service within New England” and beyond with single-line CSX service to its local customers and to those served by connecting Class I railroads. Moreover, “CSX will be able to offer rail customers in New England… to track and manage their shipments with much greater precision and confidence.”

I should hope so. PAR president David Fink in his October 2020 virtual NEARS presentation outlined a robust program of commercial growth across a broadening commodity base. For example, paper mills are converting to packaging from printing, bringing in LPG and biodiesel and taking out aggregates and MSW. The myriad letters of customer support attached to the filing cite the supply chain benefits of the transaction to shippers. Suffice to say this could be the right transaction at the right time and has all the ingredients of being successful. I wish them well.

BNSF fourth quarter revenue units were 2.6 million, up 2.6 percent, with double-digit jumps in grains and intermodal offsetting negatives elsewhere. RPU dropped 5.8 percent on decreases everywhere but grain. Total revenue was $5.7 billion, off 2.8 percent, but operating income increased 3.4 percent to $2.2 billion thanks in part to lower labor, fuel, and car hire costs. The operating ratio shed 230 basis points to 61.6. Net income was $2.2 billion, up 3.4 percent.

Merchandise carloads ex-auto were essentially unchanged as gains on the ag side offset losses on the industrial side, where lumber/wood was the only double-digit gainer. Every other commodity group was off vs. a year ago, with double-digit hits in aggregates, metals, met ores, petroleum, and non-metallic minerals. Coal, not surprisingly, was off 20.5 percent.

The sale of the CSX Massena line to CN (WIR 9/6/2019) may not happen after all. The STB in FD 36347 took offense with the provision that the property being transferred stops just short of the Syracuse, giving CN rights into the Syracuse “solely for the purpose of effectuating interchange with CSX… and expressly prohibits CN from seeking access” to the Susquehanna and the Finger Lakes.

In its May, 2020 Decision, the STB writes, “The Board has serious concerns about [the language] restricting CN from *ever s*eeking access” to the NYSW and FGLK (emphasis the STB’s). Accordingly, the STB wrote that “approval of the transaction is subject to the provision” that the parties “modify or eliminate” the offending language and resubmit the application. That never happened.

And so it was that the STB decided Feb 24 that the paragraph prohibiting interchange with FGLK and NYSW has to go, writing that the parties' "requests for reconsideration are denied." Says to me the Board is finally getting serious about paper barriers, something they've had on the back burner for years. Paper barriers are one way to keep short lines at arm's length and the STB sees them not in the public interest.

I see the class Is de-emphasizing shortline "partnerships" in several ways. First, the focus is on point to point trains with no intermediate stops. Second, they're building longer trains to fewer OD pairs. Third, they're closing classification yards. Fourth, if the move can't support a target revenue/variable cost (RVC) ratio they turn it down (BNSF and CP may be the exceptions here.) Fifth, there's little sense in supporting a short line with a 90 OR when the Class I can do it for 60 or less.

The way I see it, in transactions like this, the language wants to make sure every move stays in the Class I account from start to finish. If it can't, well, maybe we won't do the move.