

# RAILROAD WEEK IN REVIEW

May 31, 2024

*“Generally, transport fundamentals continue to bounce along the bottom with nobody citing clear signs of improvement outside of some normal seasonality as we progress through 2Q. That said, nobody cited incremental weakness, and nobody explicitly talked down expectations or cut their guidance (unlike last year’s conference).” — Scott Group notes on Wolfe Transportation Conference, May 28*

*“ ‘Safety First’ is the oft-repeated refrain on our nation’s railroads, and it rings true for short lines. The Jake Safety Award program is one way we honor and recognize short line railroads that achieve exemplary safety records... The Association congratulates the 385 Jake Safety Award winners that performed better than the industry-average reportable injury frequency rate for railroads.” — ASLRRRA Views & News, May 29*

*“BNSF delivers thousands of gallons of water a month, moving 1,200 miles by rail to the New Mexico Navajo Nation from Mississippi. Water scarcity is serious — some 30% of residents there lack reliable drinking water. They did half a million gallons of water total in 2023; hoping to reach two million this year.” — Business Insider, undated (Origin is Helena, MS on Mississippi Export short line)*

**Commodity carloads, supply chains, and the business cycle** are inextricably linked. The AAR’s *Rail Time Indicators* publication sets the stage: “The Manufacturing PMI®, from the Institute for Supply Management (ISM®), is created by directly surveying manufacturers throughout the U.S., and measures the direction (rather than actual output) of manufacturing.”

Where manufacturing is headed is often a good indication of where the U.S. economy as a whole is headed. The index is constructed such that above fifty percent means manufacturing as a whole is expanding; below fifty percent means manufacturing as a whole is contracting.

The red line in this bar chart is manufacturing. See how the dip at the end of 2022 is reflected in the carload

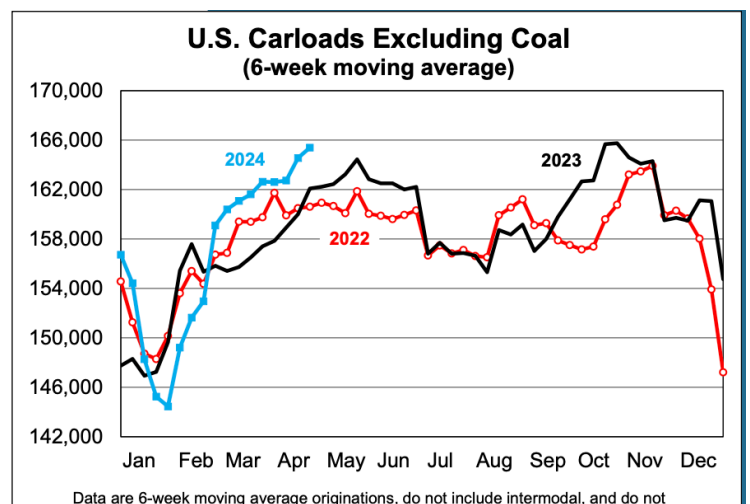


chart above. The ISM Manufacturing sort of muddles along in 2023, as do the AAR carloads —black line at the right. This is why AAR commodity carloads and the Manufacturing ISM are joined at the hip.

Also joined at the hip are the Manufacturing ISM and the business cycle. You'll note coal is excluded. That's because, as the AAR explains, "Coal carloads are down for reasons that have little to do with the state of the economy, so excluding them provides a better idea of current economic conditions. In April 2024, carloads excluding coal were up two percent over April 2023."

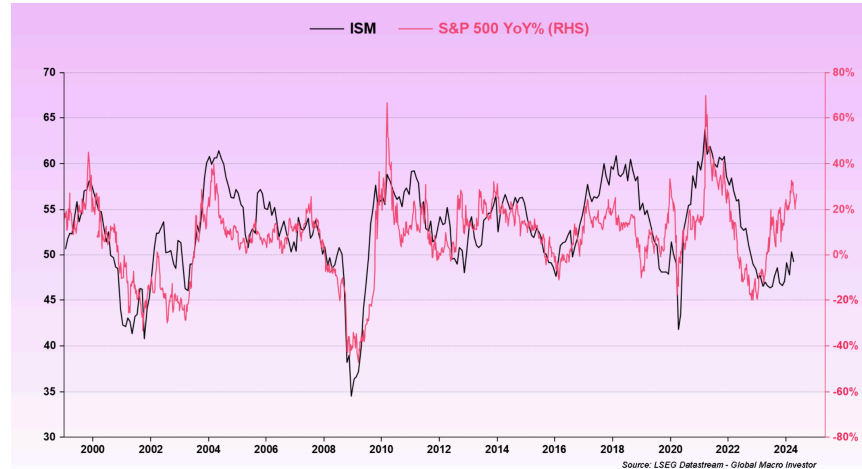
See the green line in the chart above. The Manufacturing ISM drop in April suggests the carload gains were from existing inventory being moved out or an increase in raw materials inbound against anticipated demand increases for finished goods. But at the end of the day the railroad take is if you know where the economy is in the business cycle you can predict future carload volumes to a degree.

As for predictability, see how the ISM Manufacturing Index rises and falls in four-year cycles. This chart below goes back to 2018, showing how the cyclical pattern repeats. The 2023 AAR carload curve above mirrors the 2023 curve here. The 2024 AAR carload curve above is supported by the 2024 uptick below.



But let's suppose you don't have access to the ISM charts but you do watch the stock market. There's a perfect correlation here as well.

Drilling down still further, let's take just one railroad stock. I'm using UP because it's the biggest Listed US railroad, is the oldest, and is the only US railroad whose name has gone unchanged from Day One. This five-year chart mirrors the ISM chart above, starting with the 2021 increases, continuing with 2022's declines, a flat 2023, and the beginnings of recovery in 2024.



Putting it all together, I hope I've shown how — in my opinion — the ISM Manufacturing trends, the stock market, and the direction of individual railroad share prices can help predict industry trends in terms of carload volumes. Using this information, one can take appropriate actions, whether running a regional railroad, being a railroad customer or shareholder, or being a serious industry watcher.

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