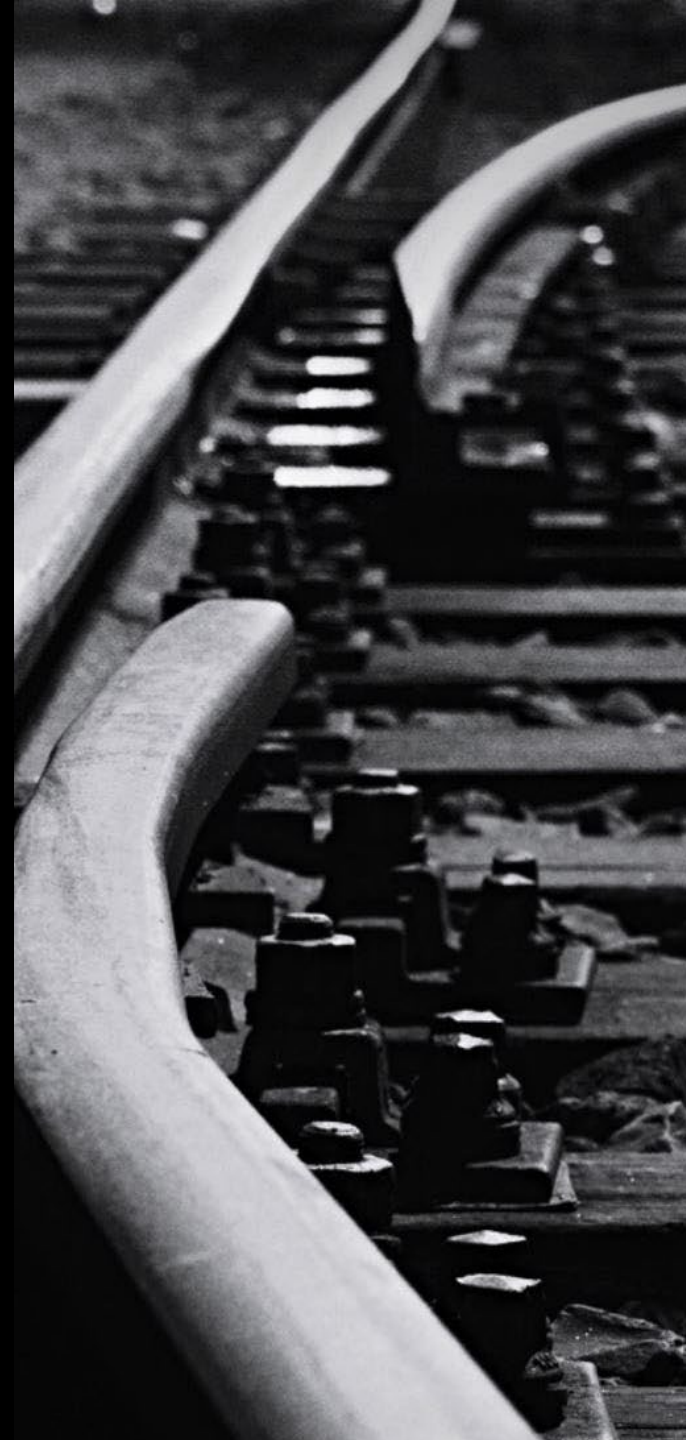

Rails 2021:

CP+KSU, CNI/TCI, the
STB..plus REAL-RR bidness

REF LIVE! (2022) | The Desert

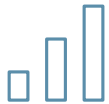


Rails Top 10

Pandemic/Recovery '2-122

- 1 | COVID (duh) – Delta Blues-Not done quite yet
- 2 | The Shark's Tooth – How RRs handled the down & the ups in 2020 - and now everyone knows what a “supply chain” is! – to “crisis”
- 3 | Uncertainty/ Visibility/ (Lack of) Guidance – Getting Clearer (or is it?)
- 4 | Accelerated (Not Altered) Trends
- 5 | Intermodal! (see #4)
- 6 | Zooms and (Rail) Trends (now we're going back Live!)
- 7 | Technology – from Portals to Pulses: Tu Simple!
- 8 | ESG
- 9 | Ag - from the Savior back to the Riddler
- 10 | Globalization/ Slowballization/ De-Globalization – but follow the TEUs

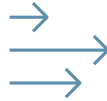
Recurring and Accelerating Rail Trends



The Mix Shift
Towards Higher
Levels of Service



The Parallel Faster
Decline of Coal



The Continuation and
Success of PSR



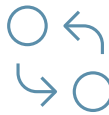
The Continuing “Cult
of the OR”



The Continuing Fight
over FCF – Share
Buybacks “vs” Capex



The Consistent
“Hype” of EV & AV
Highway
Competition
(response?)



The Remaining
Importance of Trade
(and Tariffs Remain)



Solid Financial
Results/ Good Cash
Flow & Capital
Access



The Continued Lure
of M&A in short
lines/ regionals



The Continued
“Hype” on the Value-
Trap of Rail
Consolidation

5 Enduring (?) Railroad Competitive Advantages

- 1 Labor Advantage**
(ex: Double-stack LA-Chi – or Rupert-Toronto)¹

 - 2 Fuel Advantage (2A)**
(4:1 ton/ mile; AAR)² – So 2B is Environmental Advantage (see .WMRT, Unilever, etc.)

 - 3 Infrastructure Advantage**
(after the IHS buildout; user-pay and capex to support changing logistics patterns – ex: transcon)³

 - 4 Railroads' Excellent Financial Condition, Liquidity, Free Cash flow**

 - 5 Railroads' Historic Ability to Reduce Expenses in a Known Slowdown (2009, 2020)⁴**
-

1. AV trucking?; 2. EV Trucking?; 3. Infrastructure Bill? (LOL); 4. Newly Added (in response to C19)

Administration: Return to “Normalcy”?



STB Impact? Even more relevant



Infrastructure? At long last...



Crew Size!! (FAST Act Re-auth. etc)



Emissions, etc? Plays to RRs/ ESG



Ethanol?



Amtrak & Passenger?



Trade!! The only unequivocal good (?)



Foreign Relations

Dealers' Choice? Deal-Fever in Short Lines (still)

- Many small recent deals (by OmniTRAX, RJ Corman, etc.)
- Watco-Dow deal a new prototype?
- On the market: US Steel lines, many others BTR
- Off Market & Smaller Deals (ex. SLGW)
- Spanner in the works? Problematic STB?
 - Massena Line & lawsuits
 - Amtrak in the Gulf (& elsewhere)
 - Pan Am still “incomplete” (NEARS)
 - WC-Watco finally finished
 - KSU? A Slam Dunk?
- Buyers (all with different CoC, time frames, ROI expectations):
 - Strategic (above)
 - PE (and PE/ partner)
 - Infrastructure Firms
 - Class Ones as sellers (CN?) and/ or Buyers (CP-CMQ, CSX-PAR?)

Rails 2022 – Realities & Perceptions

- RR investing themes (managers & investors) move from “Cult of the OR”(alone) to
 - Growth
 - Technology
 - ESG
 - COMPARISONS – mostly useless and about to get harder in H2/ 21
 - Rails modestly trail the market H1/ 21
- Rails get unofficial “B+” for H2/ 20 Recovery (both operationally & financially)- and by ASCE for the condition of their network (Highways got their usual “D”)
- But..2021 and Today it’s a “C” as Rail Service is an issue (again)– perception & reality
 - ACC and other Shipper groups
 - House T&I Committee
 - STB commentary
 - Churchill: “never let a good crisis go unused!”
 - Rail metrics improving by the end of the quarter into summer – **RR service metrics remain a major issue**
- Rail Q4/ 21 EPS – 4 “wins”2 “losses”(slight – but from CP & KSU, interestingly)financial strength
- As Supply Chain “fragility”tests globalization, sparks inflation, makes headlines
 - A truly world-wide issue , and labor based– ocean, ports, rails & trucks, warehouses, shippers
 - JIT to JIC actually benefits rails
 - Near-shoring?
 - Front page news!
- Add Consolidation to the mix..giving the STB an opportunity to pontificate ..and now Hearings!
- Add the White House to the mix...

Rail Themes Emerging from the Cold Winter

- Supply chain and labor issues remain; politics a headwind
- Rails promise *growth pivot* (“*Talking the Talk*”) but the year starts poorly to say the least...
- Capex budgets are up (so is inflation)
- Split on *coal* outlook (CSX vs NSC) for ‘22 after starring in ‘21 – future decline unchallenged
- STB grabbing headlines (Pan Am/ Amtrak/ Access Hearings)
- Rails tout benefits of *single-line* service (CSX-PAR, CPKC)!
- Rail-Rail competition heating up (BNSFvUP; CPKC plans) as truck gains IM share
- No news (which doesn’t = good news) on national labor bargaining
- Rail cars set for (modest?) recovery
- New leadership transitions, one big succession plan unresolved (CSX), one resolved in favor of a growth focus (CN)

Executive Order (&Leak) Sows Confusion

- Biden's EO against power consolidation/ BIG business includes rail
- Clearly a late addition
- Leaked as "part 2" to the WSJ, the scoop send sends RRs stocks down
- So...2 paragraphs/ page 9 (*"Is That All There Is?"*) – only an *Encouragement* (STB is "very, very independent")
 - *Advises freight rail to work with Amtrak (remember the POTUS nickname)*
 - *Suggests "fairness"*
 - *NO mention of current M&A (KSU); almost definitely coincidental*
 - *DOES provide "cover" for the STB opposition to the merger (if..)*
 - *DOES support the consistently public statements by the STB/ Chairman that RRs have too much power and are:*
 - *Monopolistic (EO suggested Duopoly)*
 - *Overly focused on cost - & headcount – reduction*
 - *"In bed with Wall Street", in thrall with PSR*
 - *So consistent with existing STB viewpoints*
- *Most likely outcome: HEARINGS!*



STB says “NYET” to CN’s VT; TCI gets Active

- When the STB *unanimously* turned down the VT application, with nods to “Downstream Effects” that was game-over for CN proposal (but looking back, CN *never had a chance under 2 sets of rules*)
- I expect that’s game-over for *any* future C1 consolidation (on *this* I agree with Marty!)
- So *Introducing CPKC*– filed the application – reveals revenue benefits from **rail share** opportunity higher than publicly discussed; STB timing?
- This move relieves some industry pressure – but *succession issues* remain
- TCI (remember them?) owns 5% of CN (and shades of Jay Gould, 8% of CP!) and issues a challenge:
 - Jim Vena to replace JJ? JJ to retire
 - OR “gap” must be closed, pivot *away from* growth!
 - Letter seems rushed (typos) & inaccurate (in OR accounting)
 - But activists, including TCI-CSX, are 3-0 in the modern era
 - New vote is March 2022

To meet coming “existential threats”, Rail Tech/Innovation is Accelerating (T10) – 2022 Budgets will be critical

1

Inspection Portals
(from CN to the world)

2

Track Inspection Cars (at speed) and other preventive MoW

3

New loco power (BN-WAB, PHL, CP!)

4

Rail Pulse – a game-changer (and other EODB efforts)

5

Moving Blocks/ Quasi-moving Blocks (BNSF) – unlocking PTC

6

Outside Investments – CN/ UP+Tu Simple; KSU (etc?)

7

Big New Hires at CN (WAB) and UNP (WMRT); Innovation; LOS to the CEO?

8

Simulation (UP’s “Train Builder”)

9

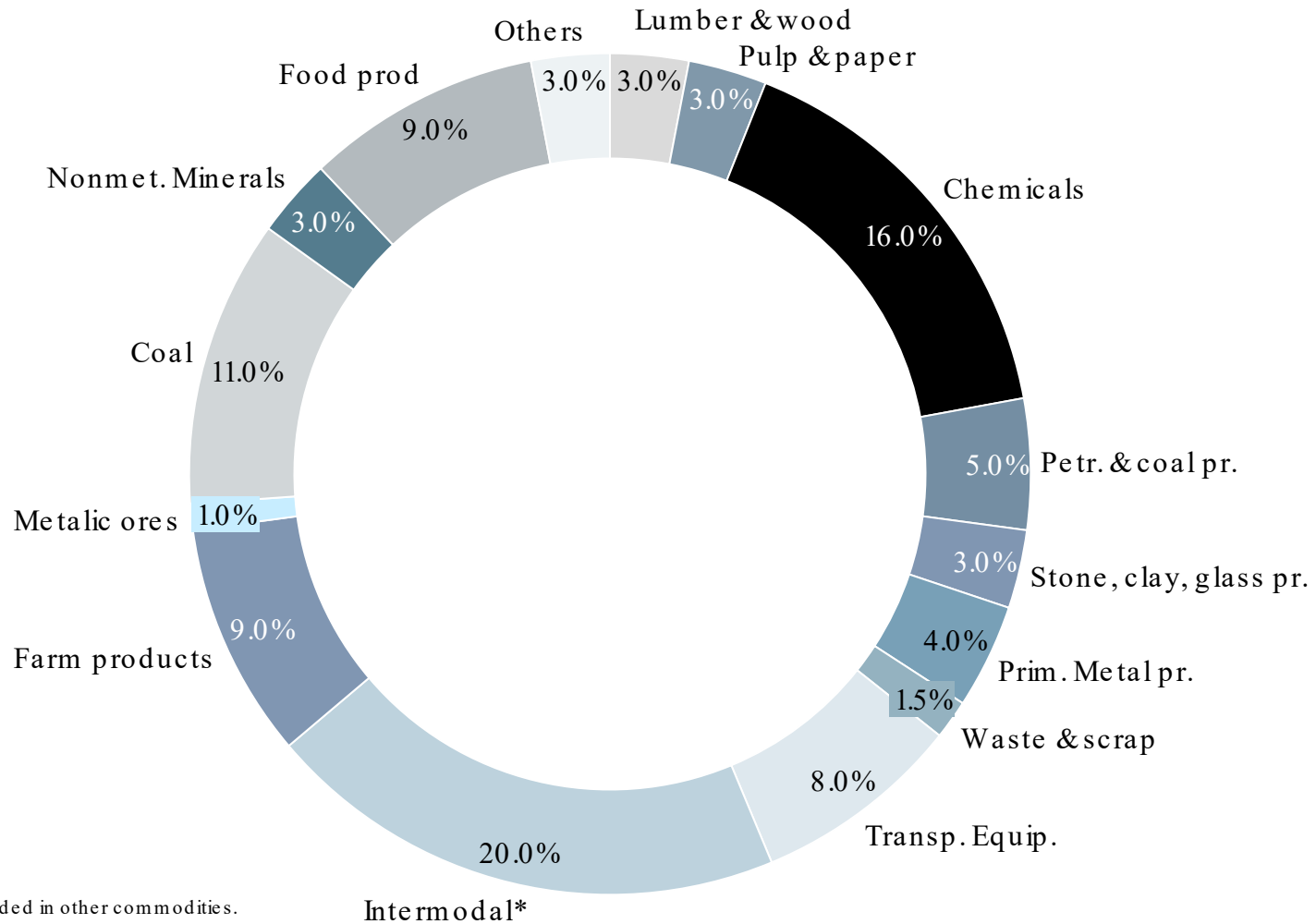
Remote meetings, virtual crew offices, zoom (sigh)

10

AVR – the “Holy Grail”, change the RR strategy? Terminals...

U.S. Class I RR Gross Revenue in 2021

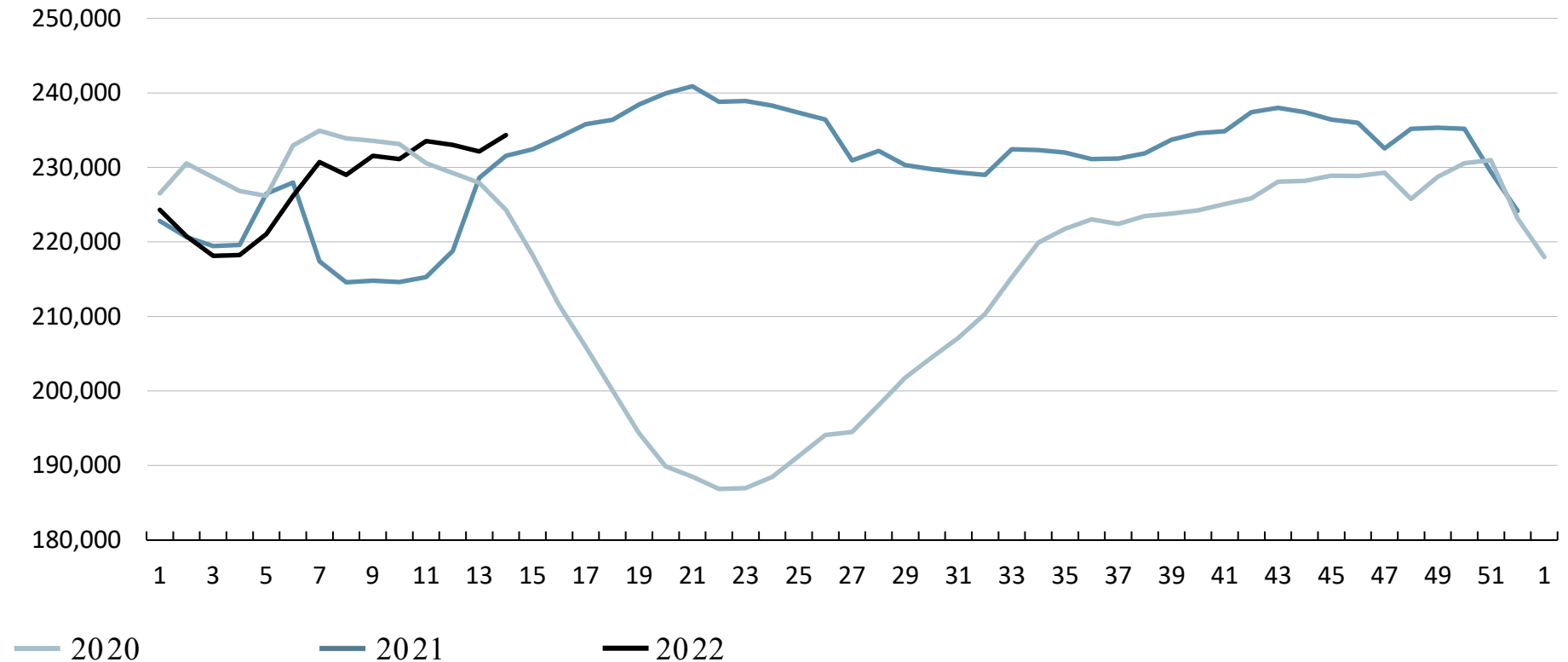
(\$ billions)



*Some intermodal is included in other commodities.
Source: AAR (FCS)

Total U.S. Rail Carloads

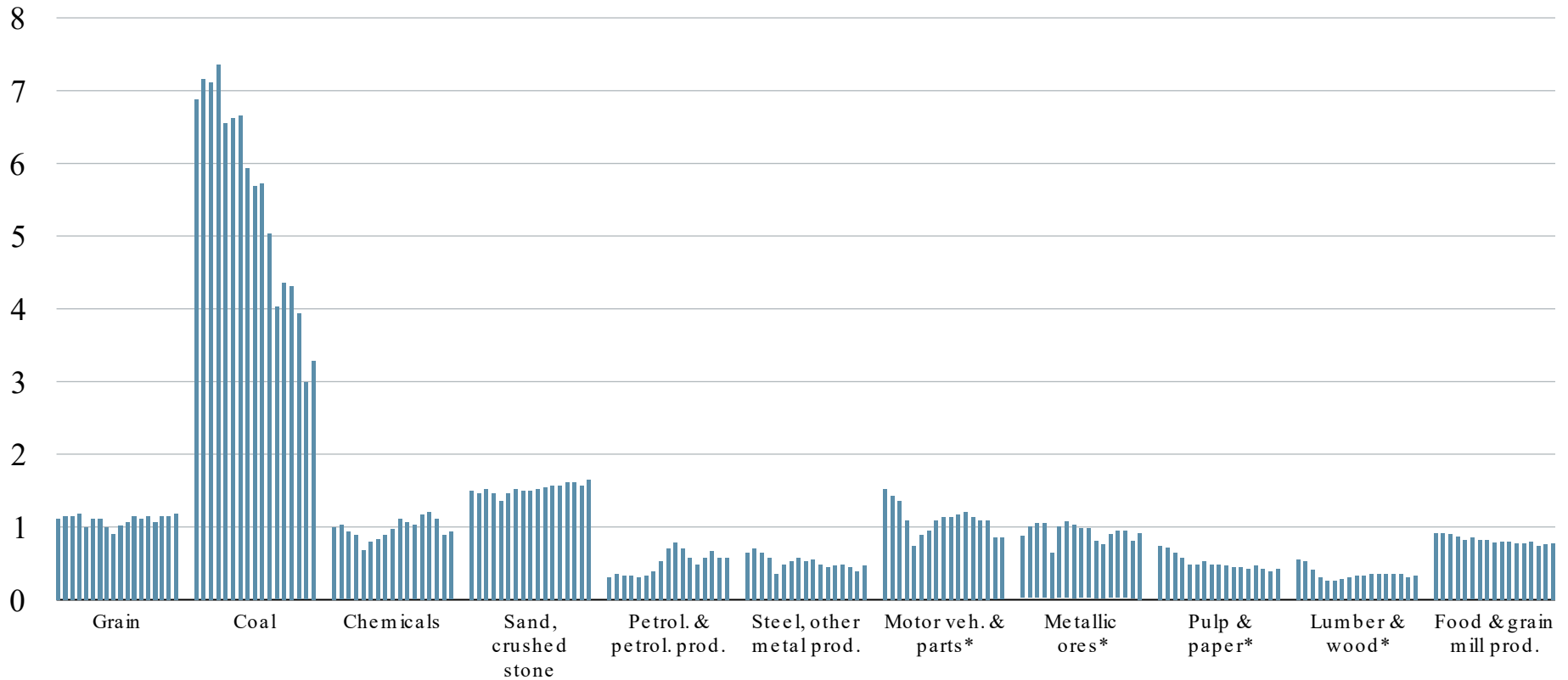
(6-week moving average)



Data are originations, do not include intermodal, and do not include the U.S. operations of CN, CP, and GMXT. Source: AAR Rail Time Indicators

Constantly Changing Markets

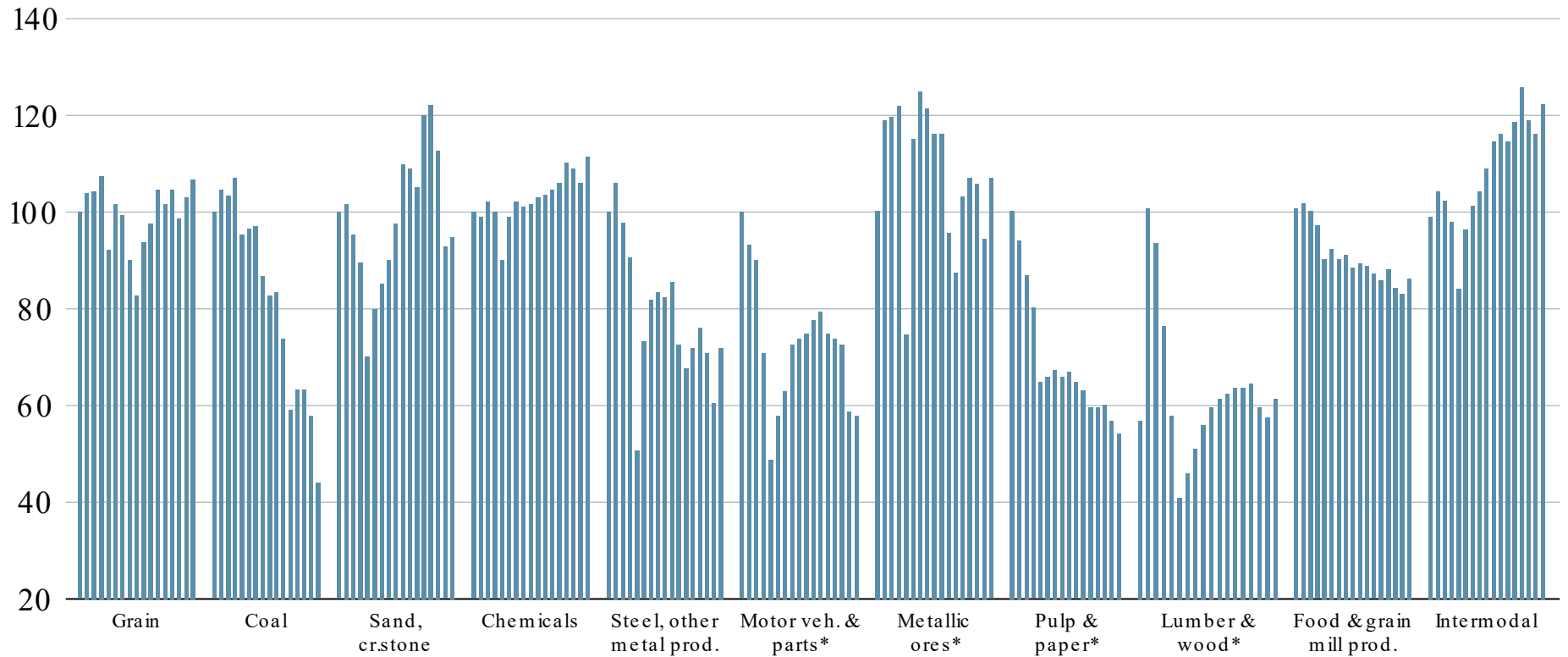
Annual Rail Carloads by Commodity: 2000-2021
(Millions)



*Combined U.S. +Canadian carloads. If intermodal were shown on this chart, it would rise from 11.5 million units in 2005 to 14.5 million in 2018 then down to 14.1 million in 2021. Source: AAR Rail Time Indicators

Constantly Changing Markets

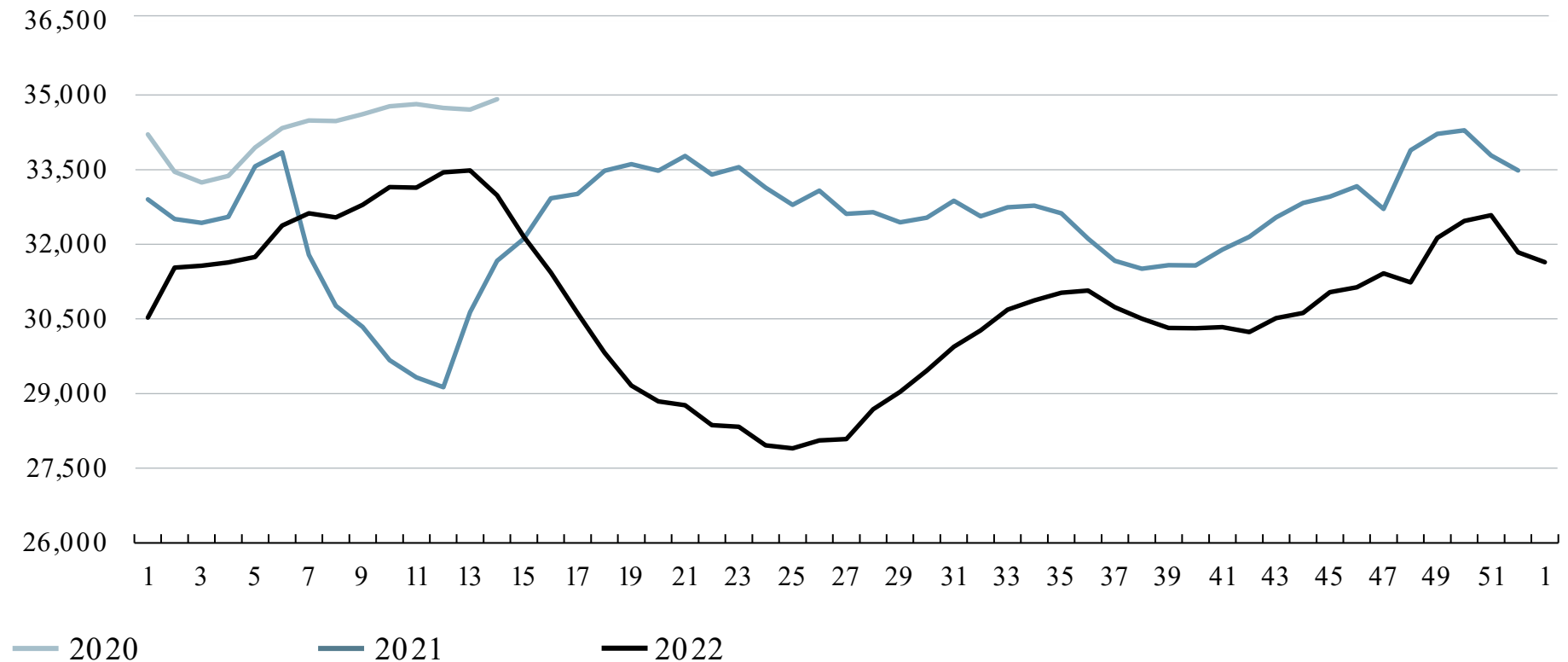
Annual Rail Carloads by Commodity: 2000-2021
(Index 2005 = 100)



*Combined U.S. + Canadian carloads. If petroleum products were shown on this chart, its index would rise from 108.1 in 2010 to 259.4 in 2014 down to 161.9 in 2017 and up to 214.73 in 2019.
Source: AAR Rail Time Indicators

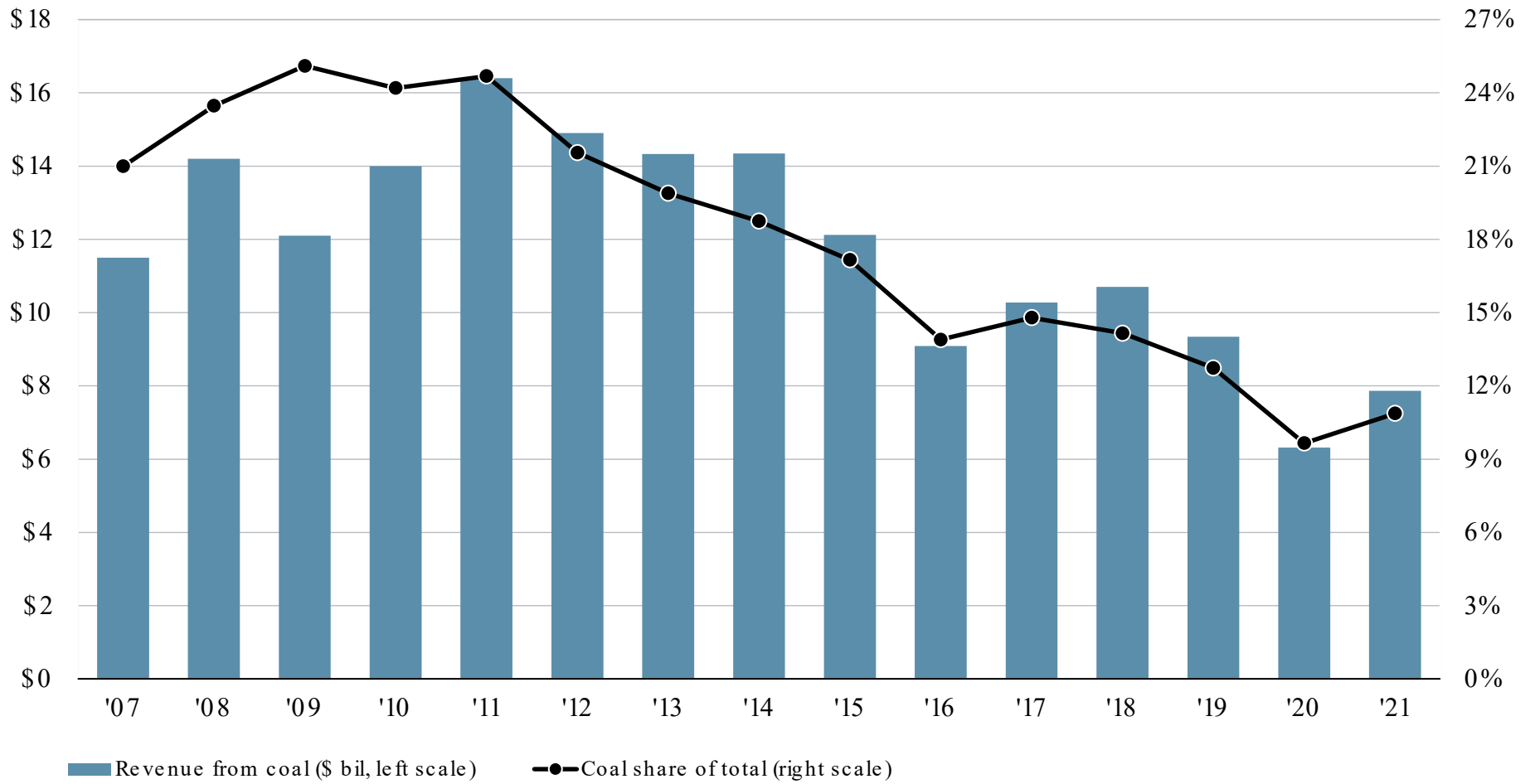
U.S. Rail Carloads of Chemicals

(6-week moving average)



Data are originations, do not include intermodal, and do not include the U.S. operations of CN, CP, and GMXT. Source: AAR Rail Time Indicators

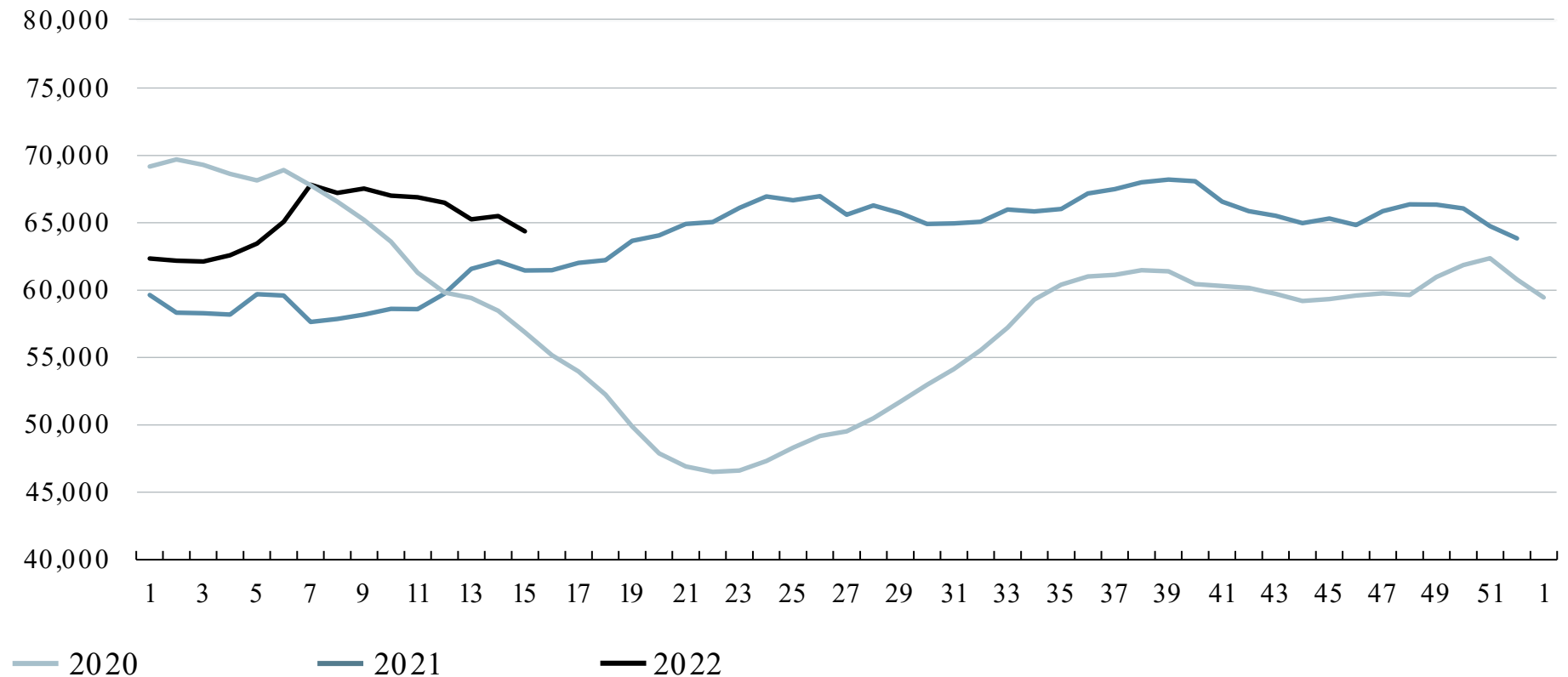
U.S. Rail Revenue From Coal



Source: AAR Freight Commodity Statistics

U.S. Rail Carloads of Coal

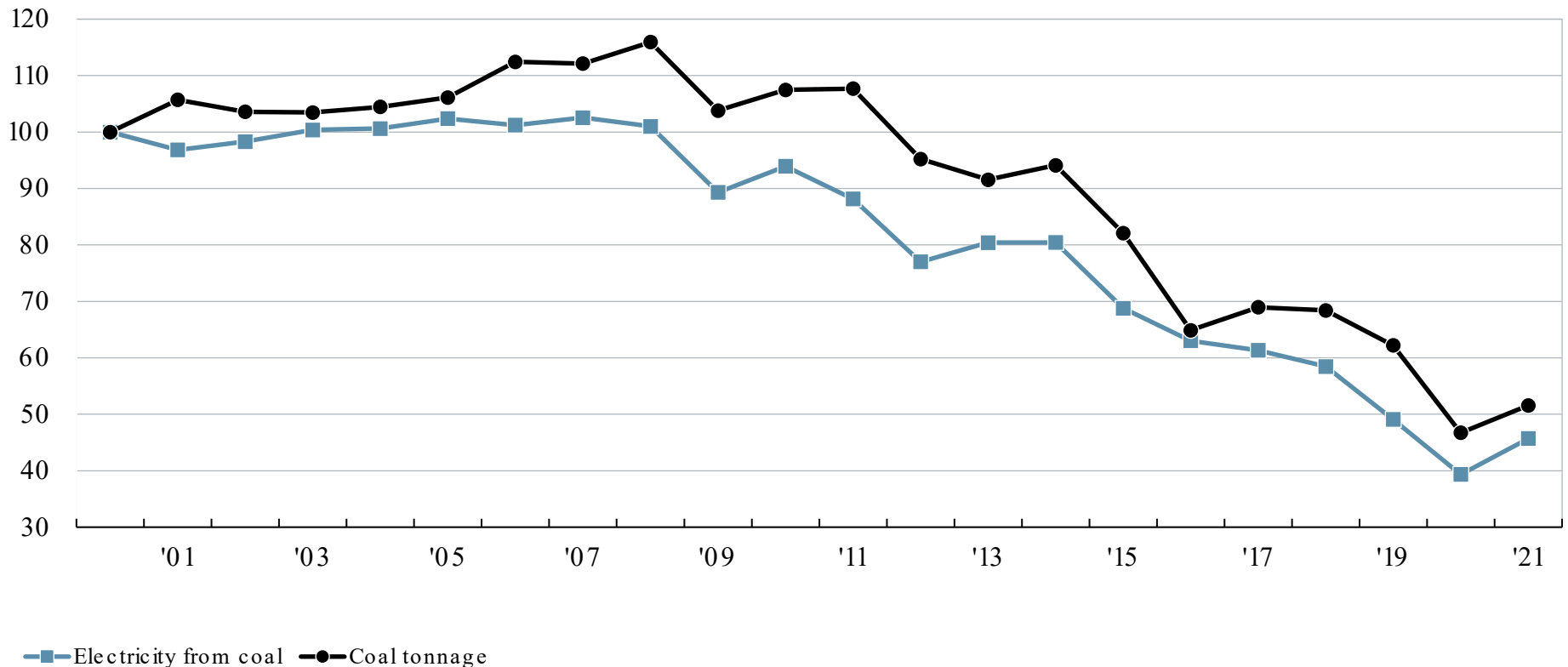
(6-week moving average)



Data are originations, do not include intermodal, and do not include the U.S. operations of CN, CP, and GMXT. Source: AAR Rail Time Indicators

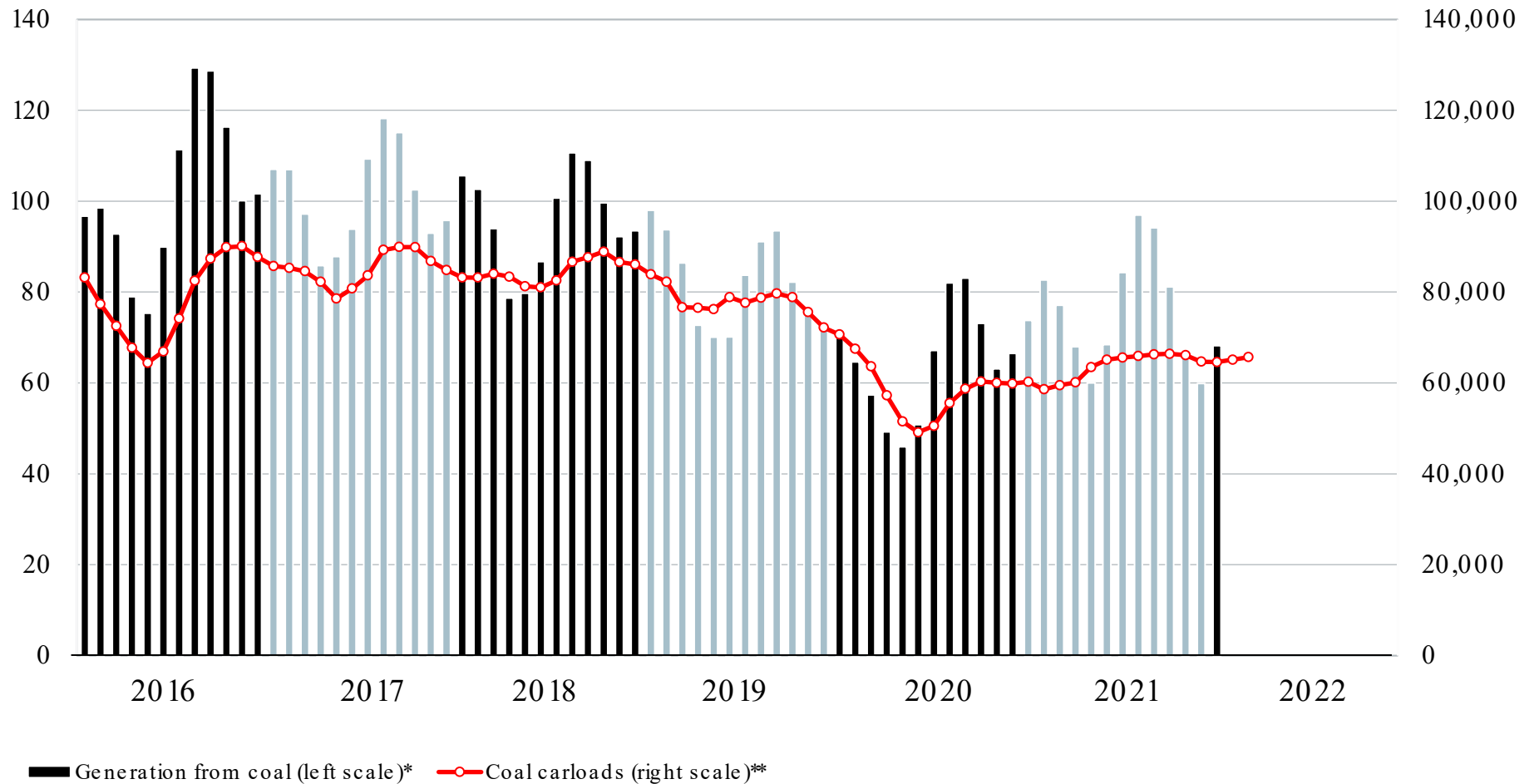
Rail Coal Volumes Are Closely Tied to Electricity Generation From Coal

(2000 = 100)



Coal tonnage based on originated tons by U.S. Class Railroads.
Sources: Energy Information Administration, Association of American Railroads

U.S. Rail Carloads of Coal vs. U.S. Electricity From Coal

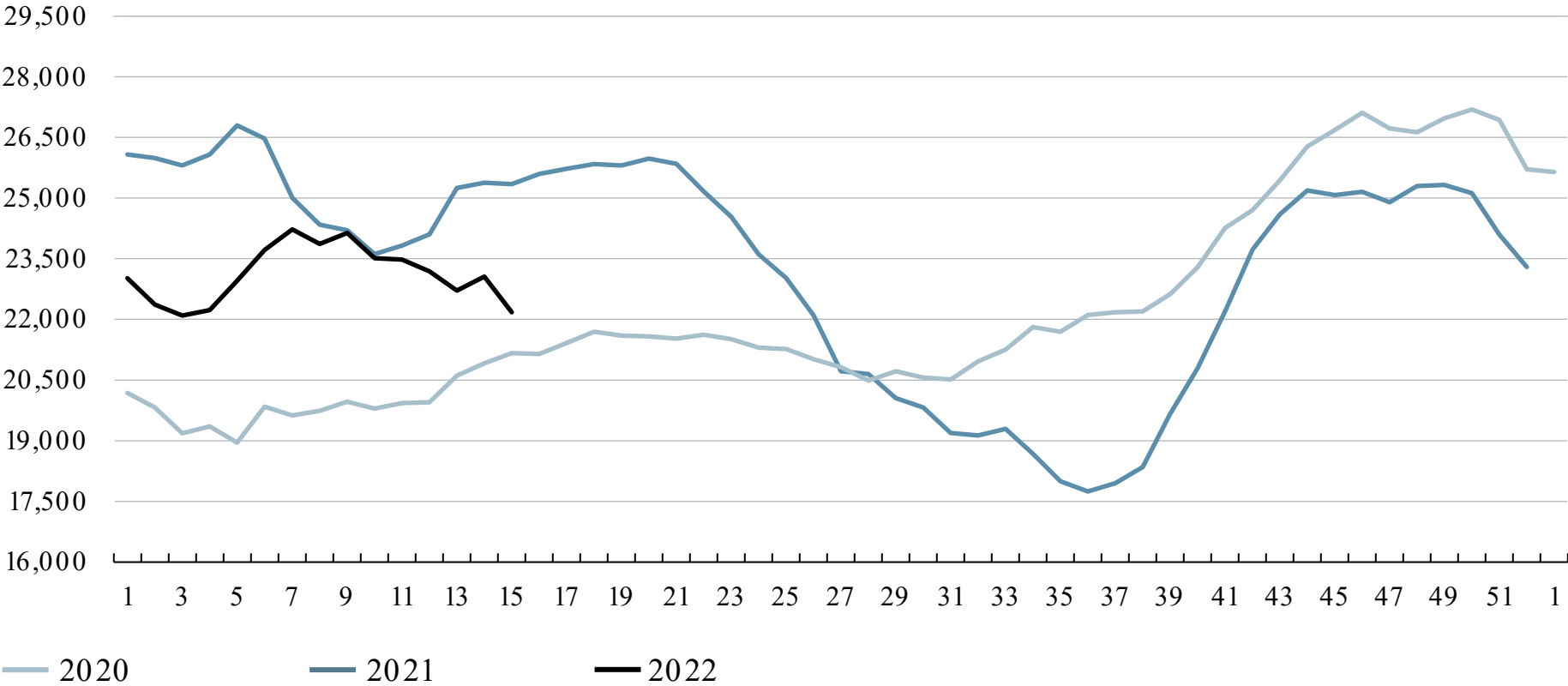


*3-month moving average, million megawatt-hours.

**3-month moving average based on weekly originations. Source: EIA, AAR

U.S. Rail Carloads of Grain

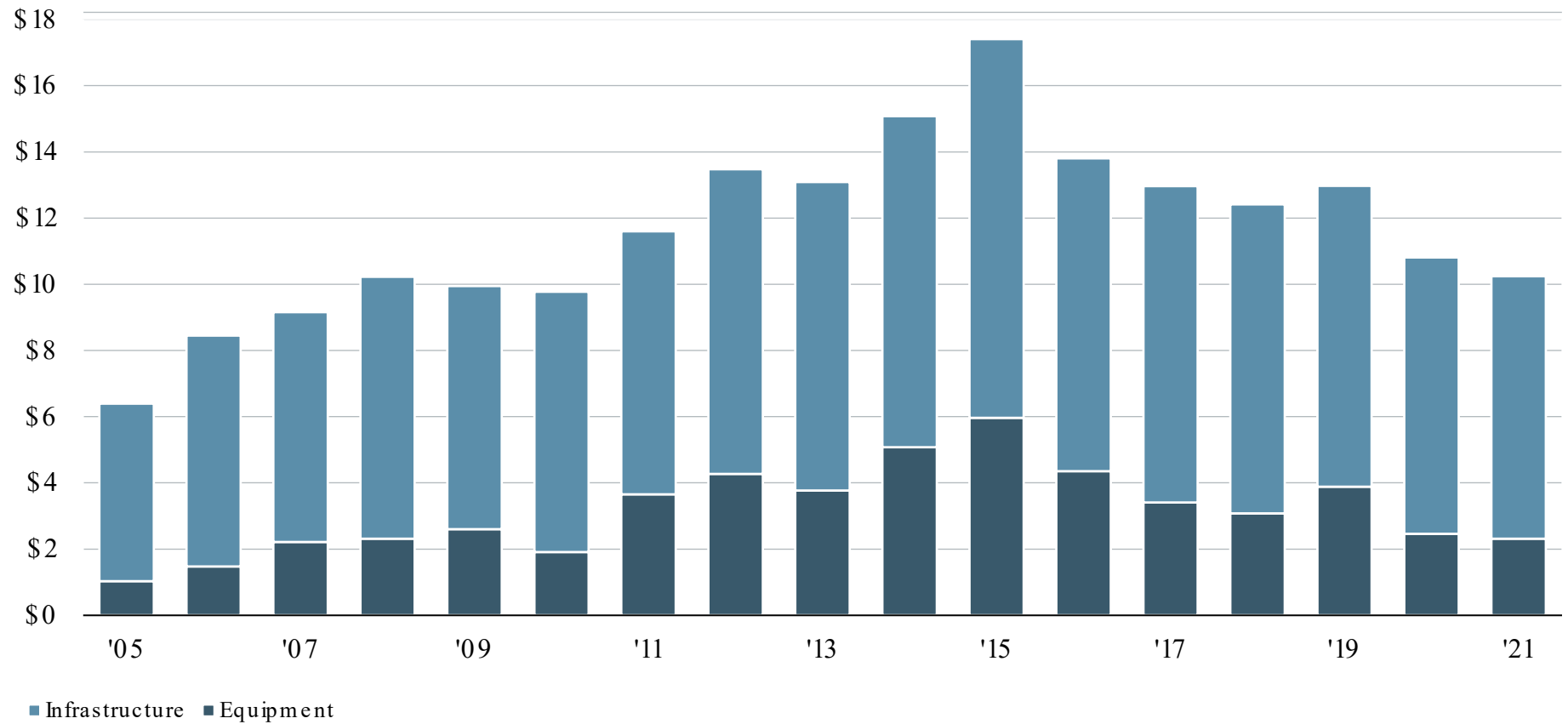
(6-week moving average)



Data are originations, do not include intermodal, and do not include the U.S. operations of CN, CP, and GMXT. Source: AAR Rail Time Indicators

Railroad Capital Spending

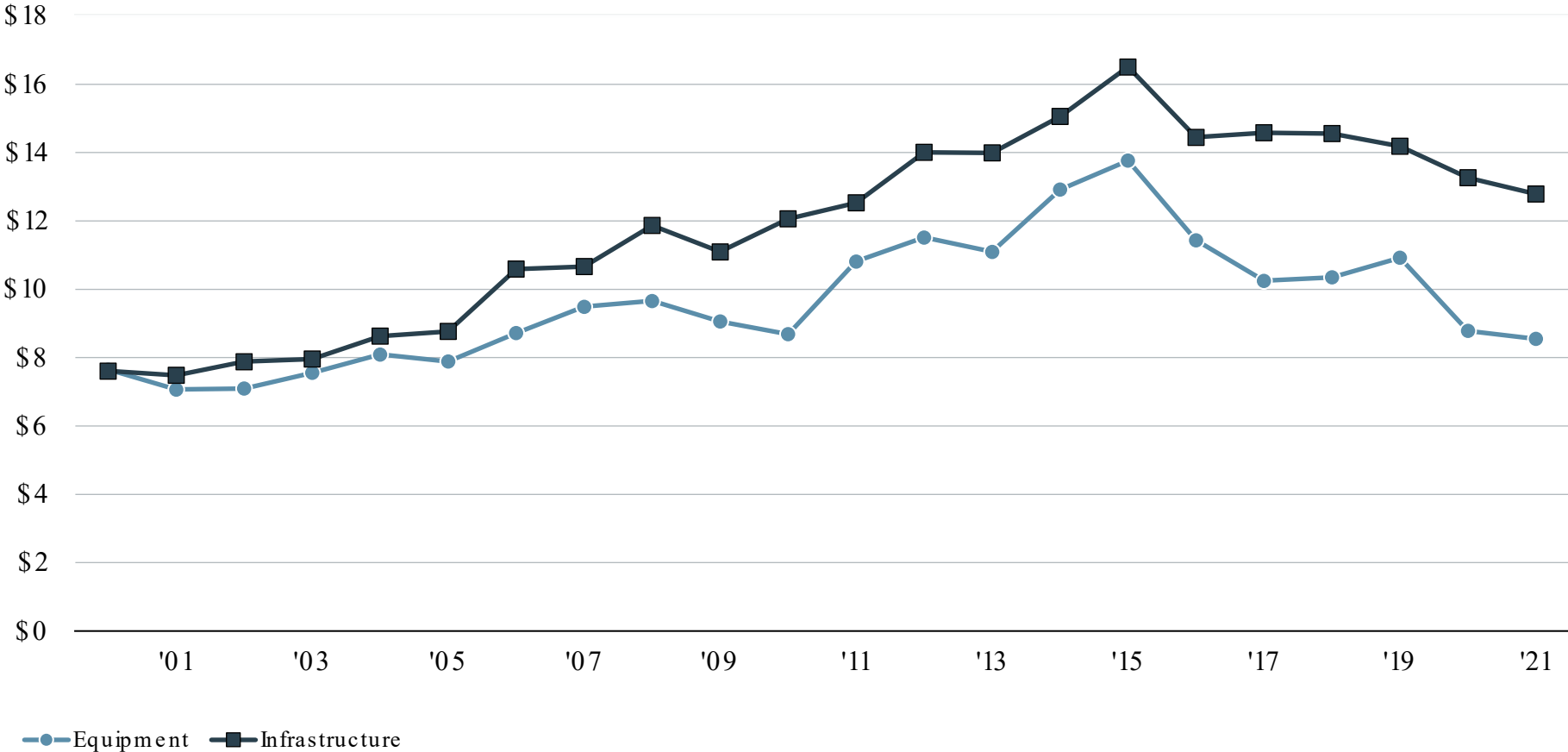
(\$ billions, current dollars)



Data are for Class I railroads. Source: AAR

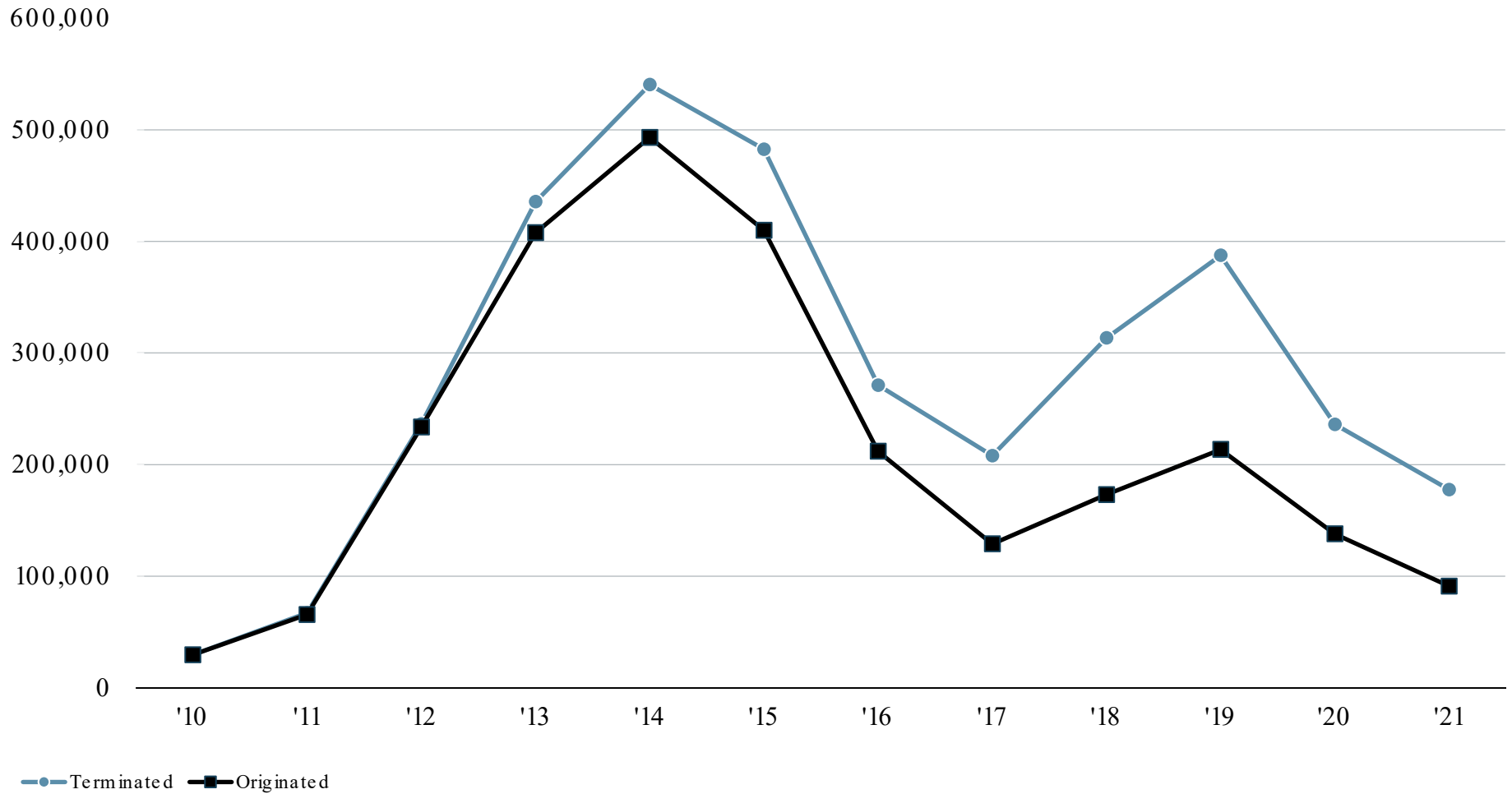
Railroad Spending on Infrastructure and Equipment

(\$ billions, current dollars)



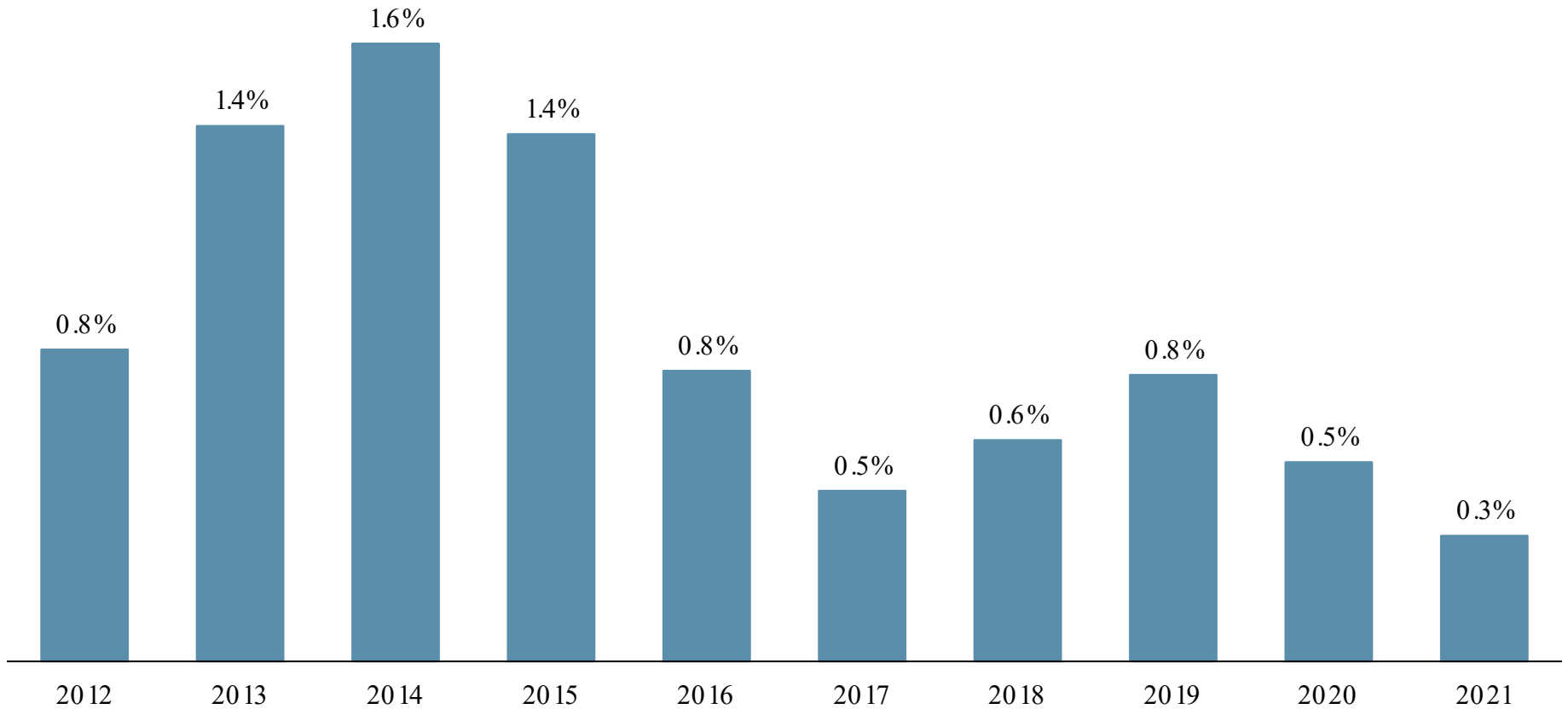
Data are for Class I railroads. Source: AAR

U.S. Rail Carloads of Crude Oil



Data are for Class I railroads. Source: AAR Freight Commodity Statistics

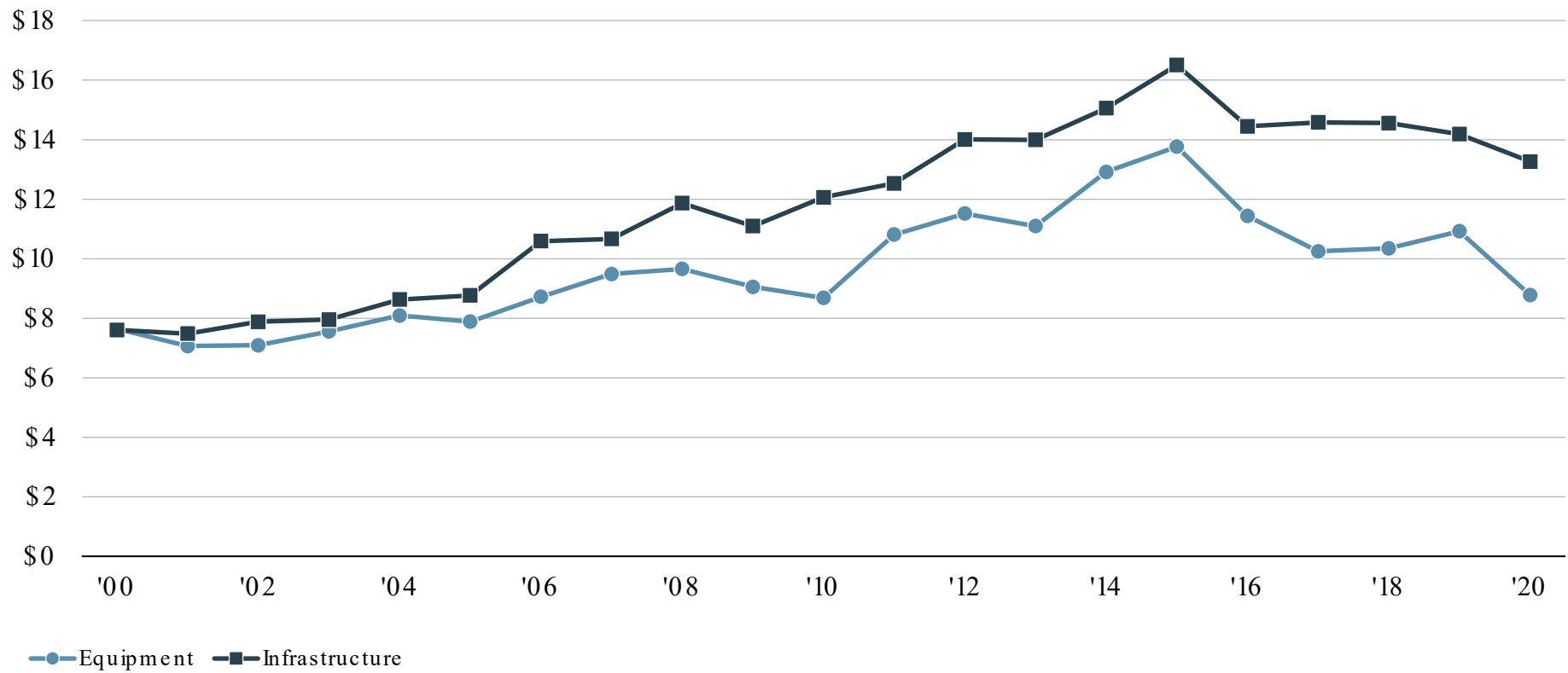
Crude Oil's Share of U.S. Rail Carloads



Source: AAR Freight Commodity Statistics

Railroad Spending on Infrastructure and Equipment

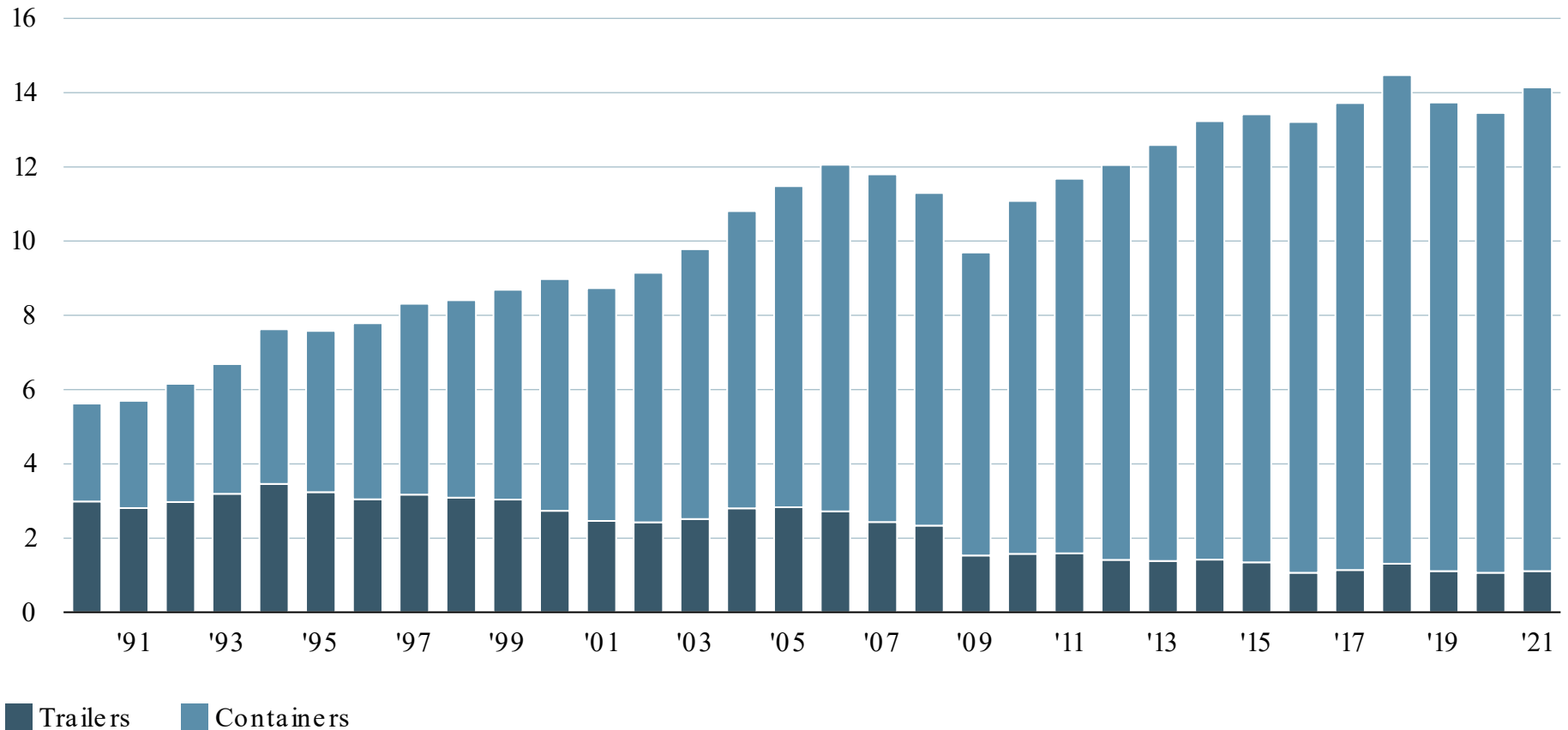
RR CAPEX \$ billions, current dollars
TONY, THIS CHART IS NOT JUST CAP EX – ALSO INCLUDES MAINTENANCE EXPENSES



Data are for Class I railroads.
Source: AAR

Rapid Intermodal Growth

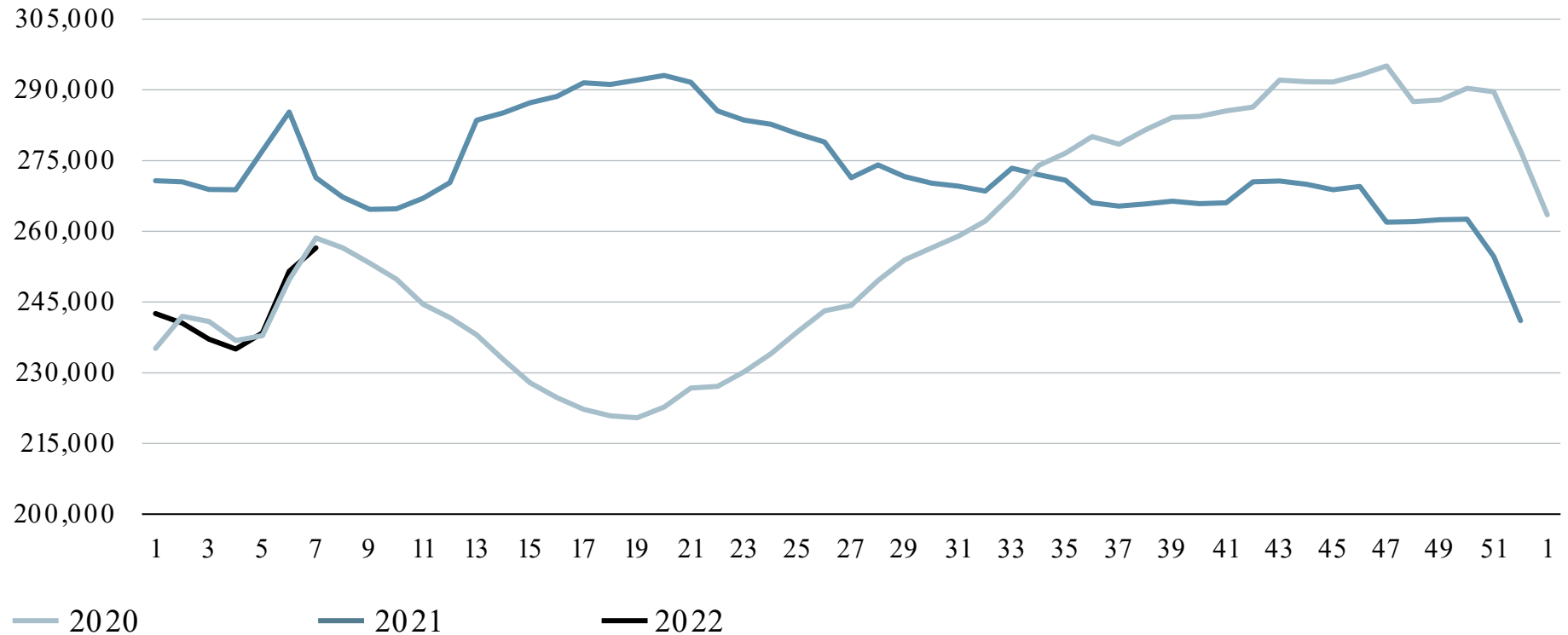
Millions



Source: AAR Rail Time Indicators

U.S. Rail Intermodal

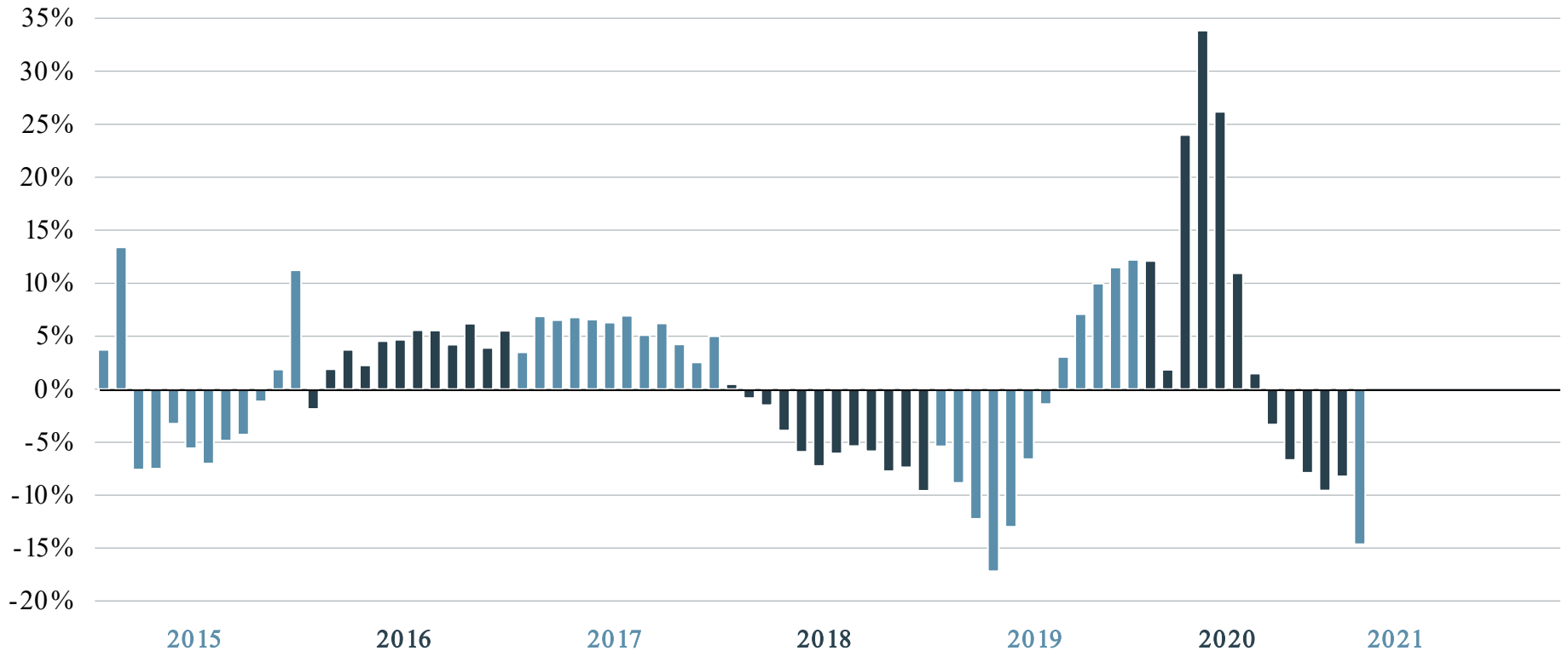
(6-week moving average)



Data are originations, do not include intermodal, and do not include the U.S. operations of CN, CP, and GMXT.

U.S. Rail Intermodal

(% change from same month previous year)

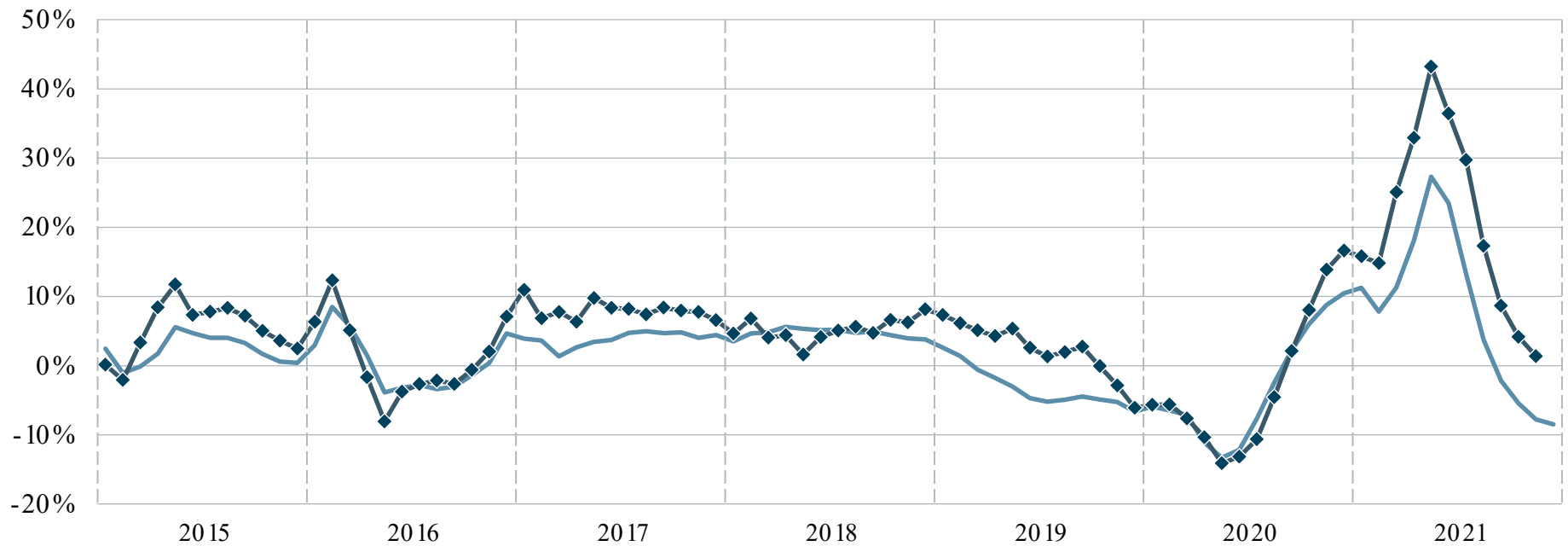


Data are based on originations, are not seasonally adjusted, don't include intermodal, and don't include the U.S. operations of CN, CP, and GMXT.
Source: AAR Rail Time Indicators

As Ports Go, So Goes Intermodal

(year -over-year % change*)

Correlation =91%



— Originated Containers on U.S. RRs*

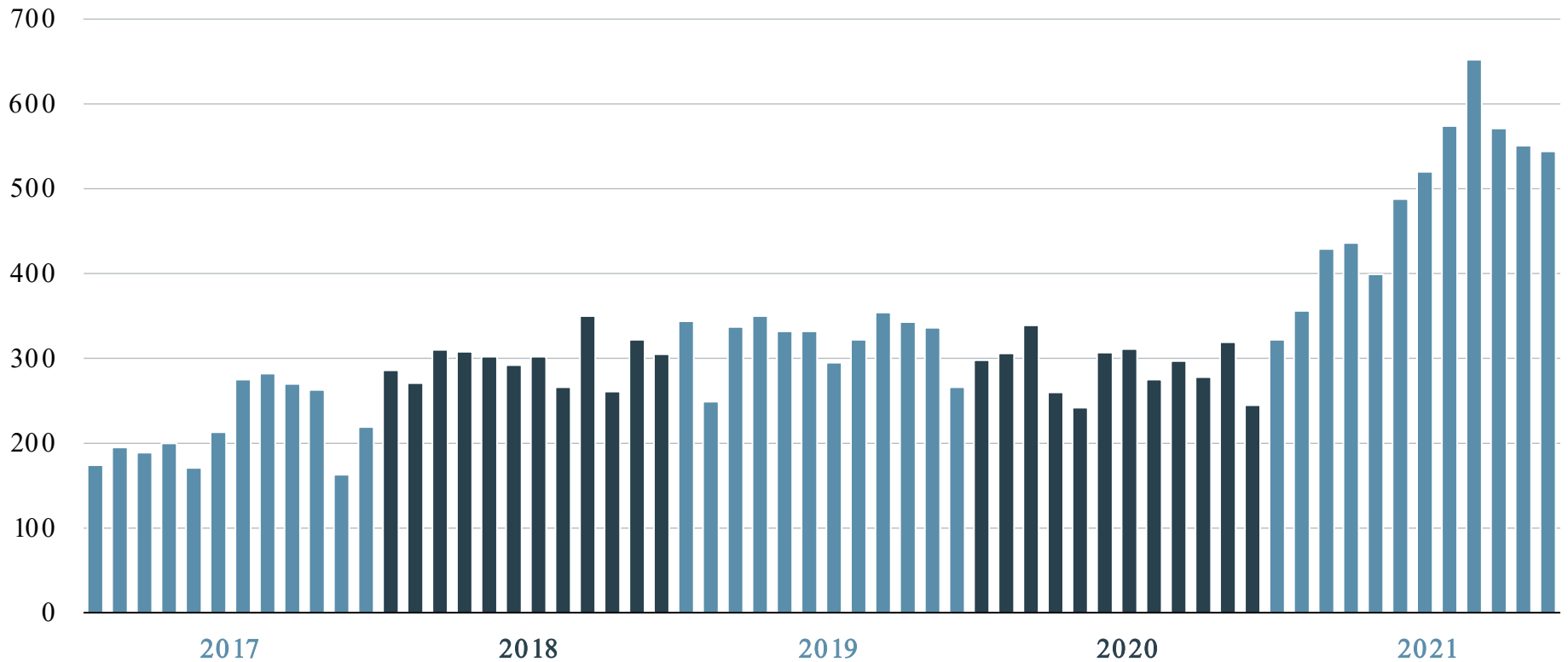
*BNSF, CSX, KCS, NS and UP combined.

**Combined loaded +empty TEUs at Baltimore, Charleston, Houston, Long Beach, Los Angeles, New York/ New Jersey, Oakland, and Savannah, Seattle/ Tacoma, and Virginia. Data are based on 3-month averages.

Source: AAR, individual ports

Job Openings: Transportation, Warehousing, & Utilities

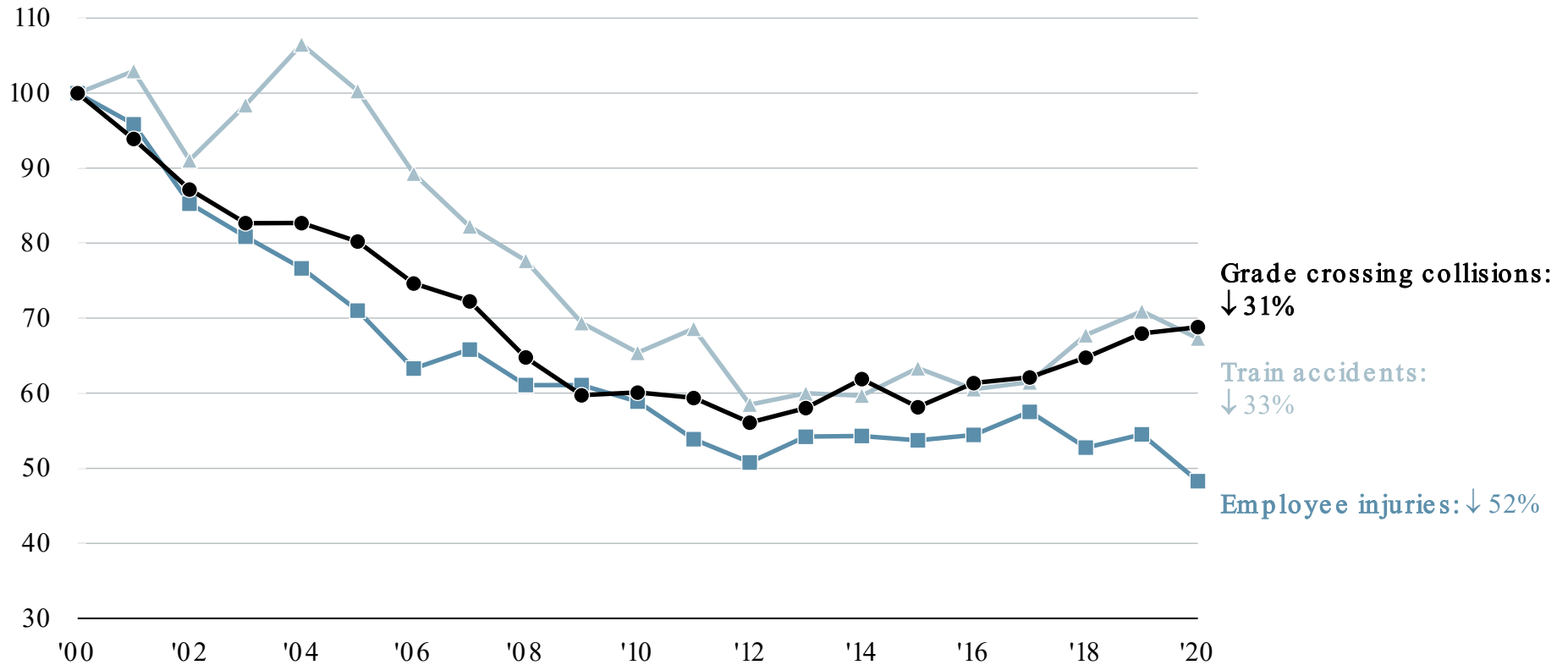
(000s)



Source: Bureau of Labor Statistics

Recent Decade Was Safest Ever

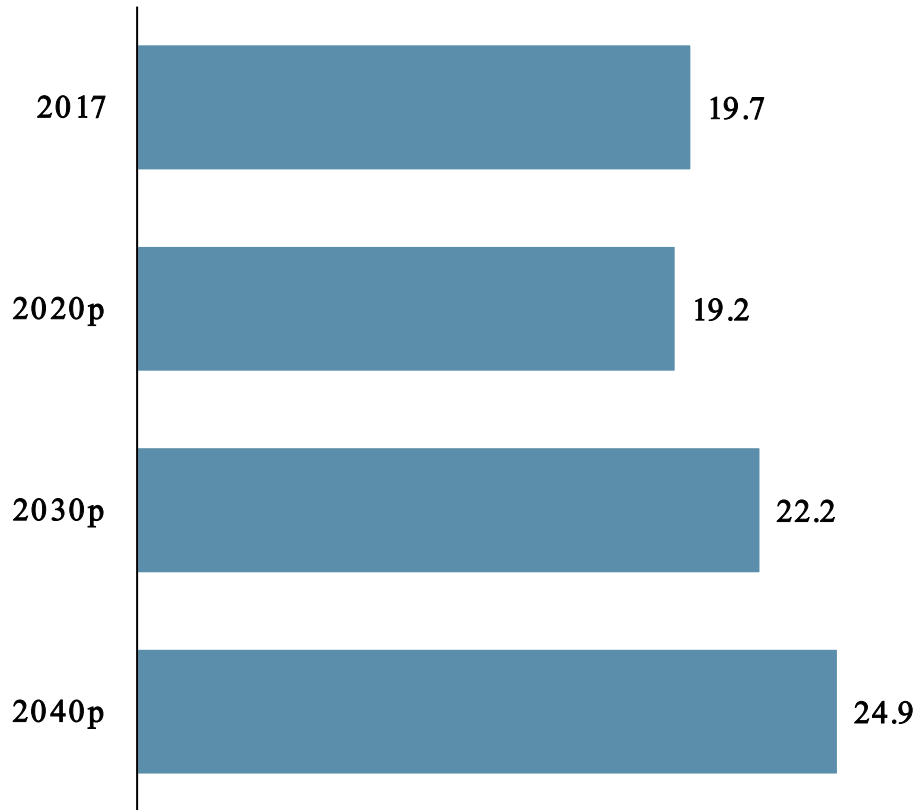
(Index 2000 = 100)



%=change in rate from 2000-2020. 2020 is preliminary.
Source: FRA

Long-Term Demand for Freight Transportation Will Grow

Billions of Tons of Freight Transported in the U.S.

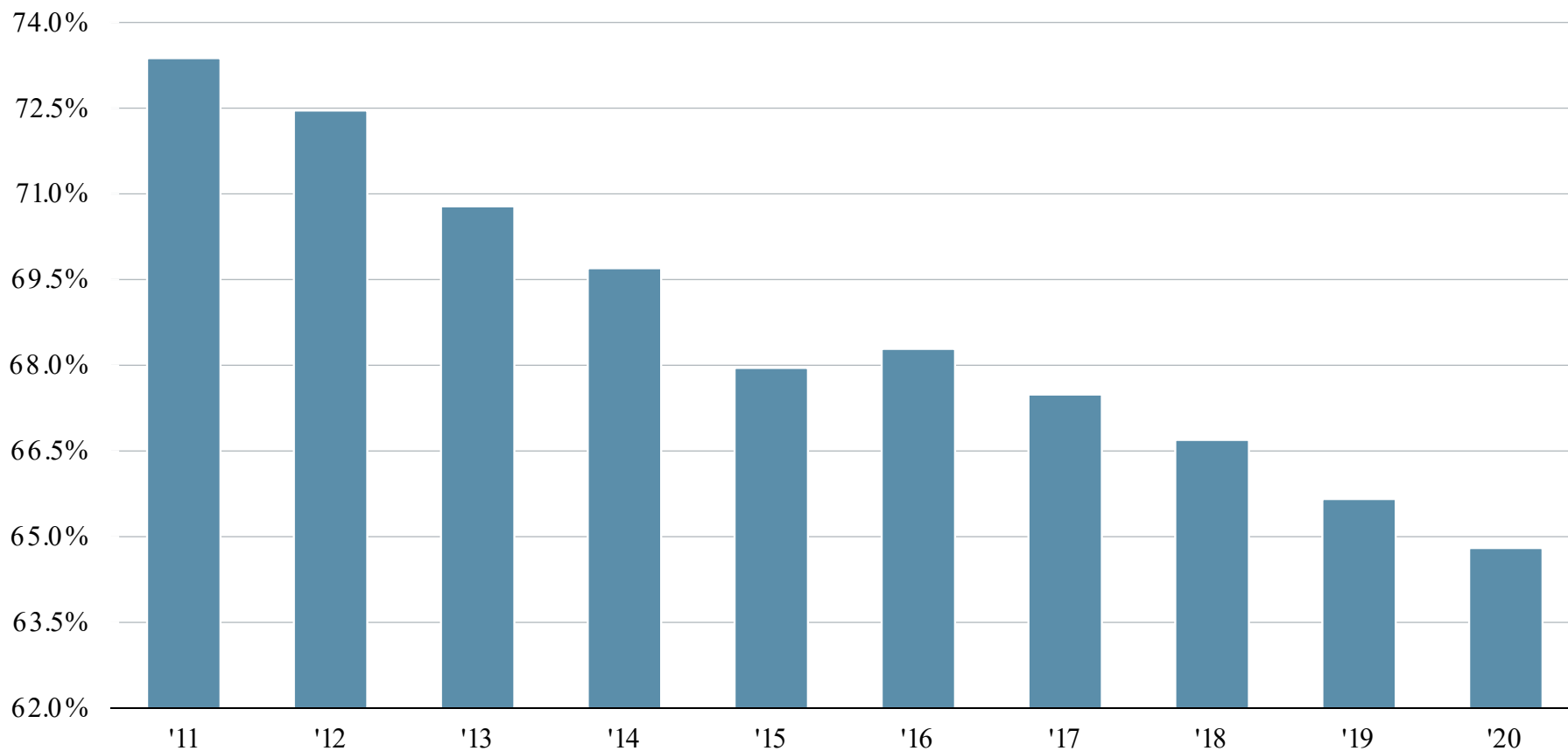


U.S. DOT estimates that total U.S. freight movements **will rise from around 19.2 billion tons in 2020 to around 24.9 billion tons in 2040 – a 30% increase.**

Summary/Winter Themes

- CP+KSU *will be approved* (under the old rules); the Last Merger
- CNI & TCI resolved about as well as could be hoped after chaos
- RailTrends in November; Christmas will happen (*again*) in December
- RRs must improve metrics – in the face of losing business, share and (any) govt. support
- Expect Hearings all year! Discussions of Reciprocal Switching, Demurrage, headcount..etc
 - Easy sound-bites on “Street Influence”/ Buybacks/ OR/ Duopoly?
 - 5/ 7 US RRs “earn CoC” – in 2020
- Other STB Issues: Massena/ PAR/ Amtrak/ PSR/ *train length?*
- Succession/ Transition issues
- Key Themes to re-emerge: Growth/ Tech/ ESG
- Coal – the last stand?
- Strong H2 Recovery (?)

RR OR – Worthy of “Cult” Status?

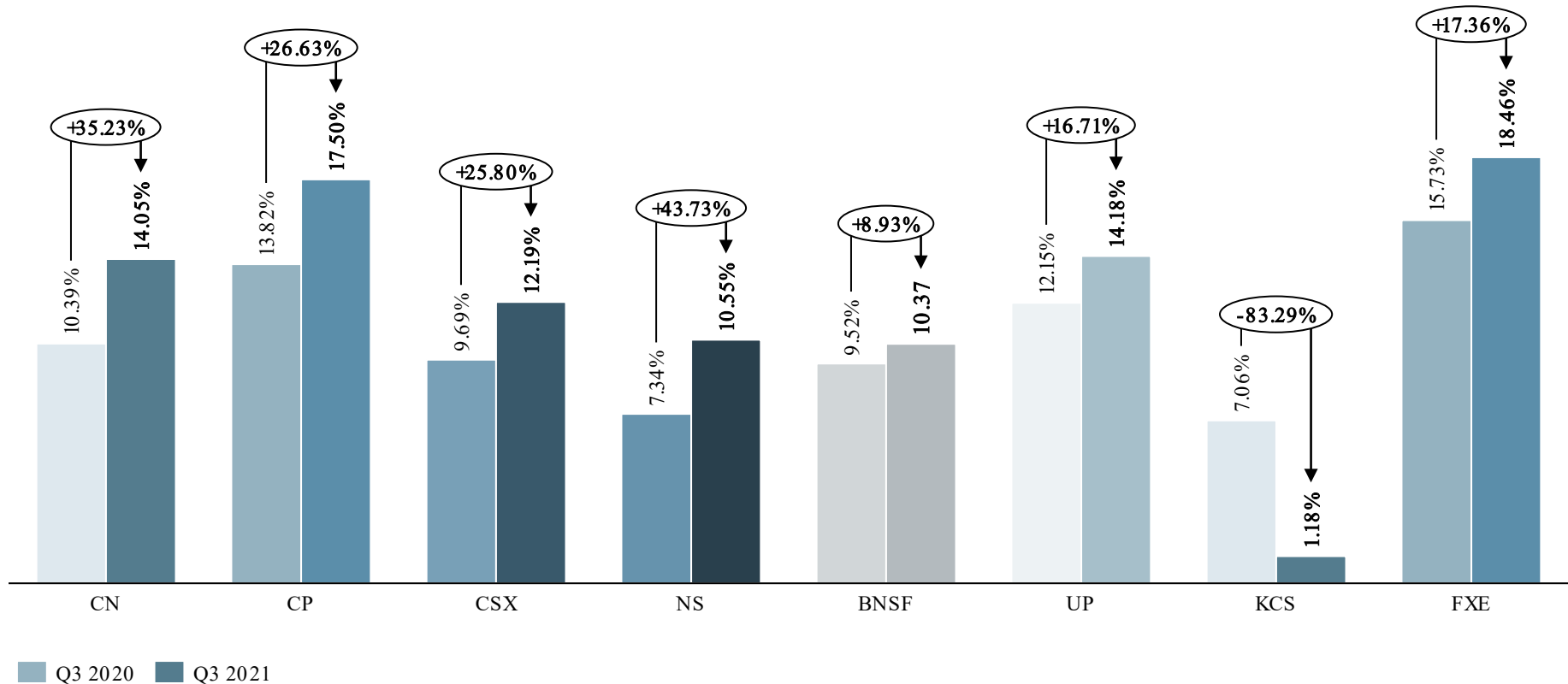


*OR – US-ONLY - Operating expenses as a percentage of operating revenue.
Source: AAR

Return on invested capital (ROIC)

All carriers, save KCS, saw a year-over-year increase in ROIC. KCS's decline was due to merger-related charges \$720.8 million and \$36.5 million taken in the second and third quarters of 2021, respectively.

Return on invested capital Q3 2021 compared to Q3 2020



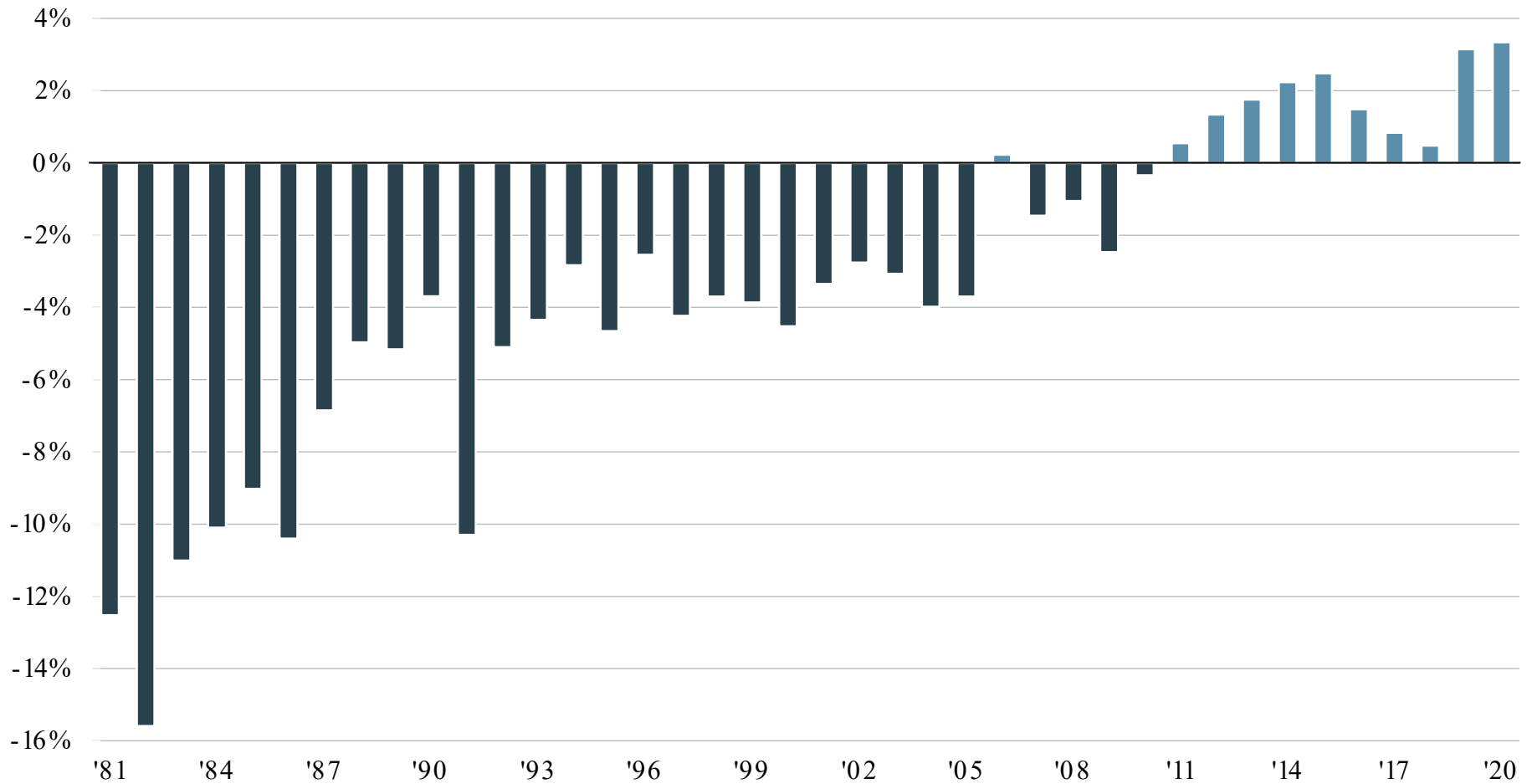
Note: BNSF is BNSF Railway, not BNSF, LLC

Note: KCS's return on invested capital figure reflects the company's operations in both the US and Mexico

Sources: Industry financial reports, Ycharts.com, press releases, and Oliver Wyman analysis

Spread Between RR's RPIC and WACC

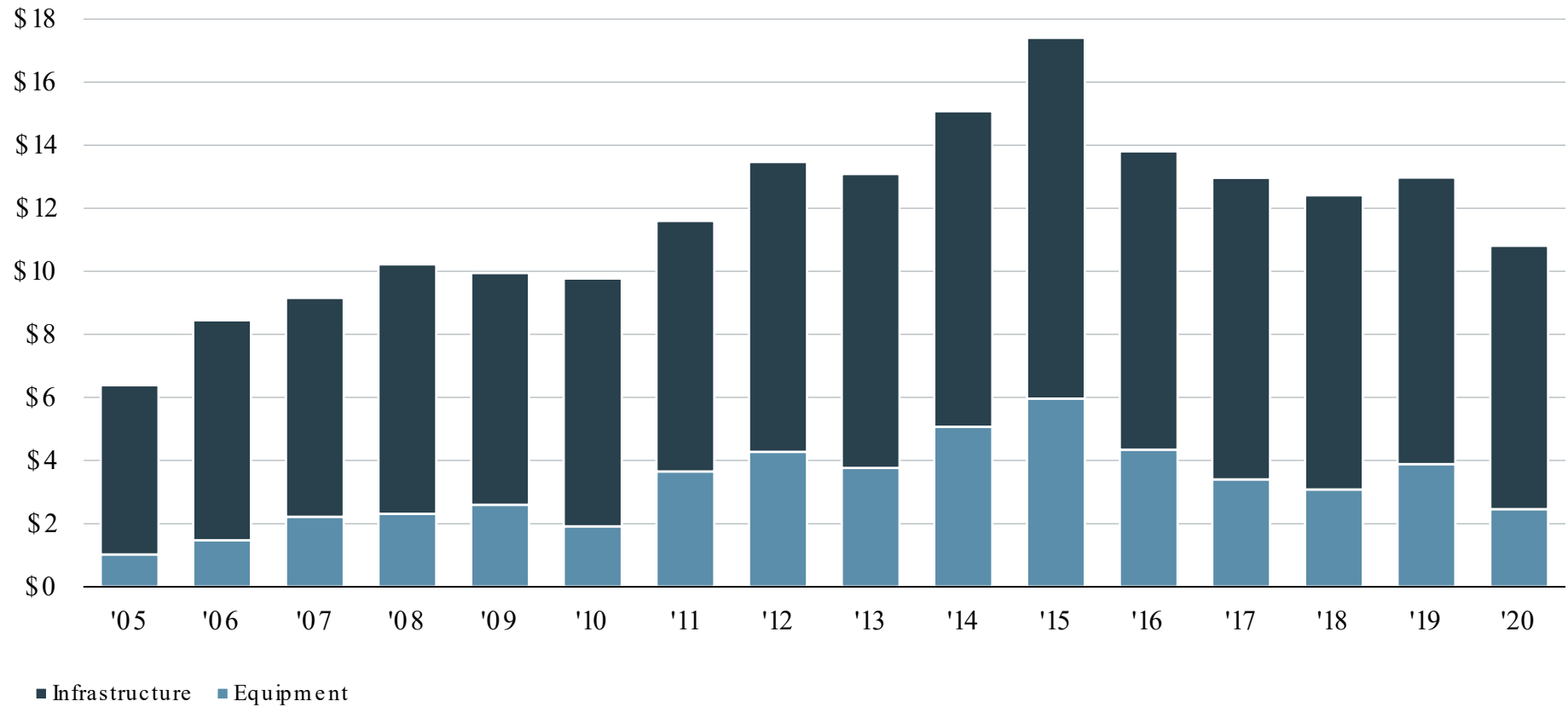
Using STB Data, US ONLY



*In 2006, the Surface Transportation Board significantly changed the method by which it calculates the rail industry cost of capital.
Source: STB

Railroad Capital Spending

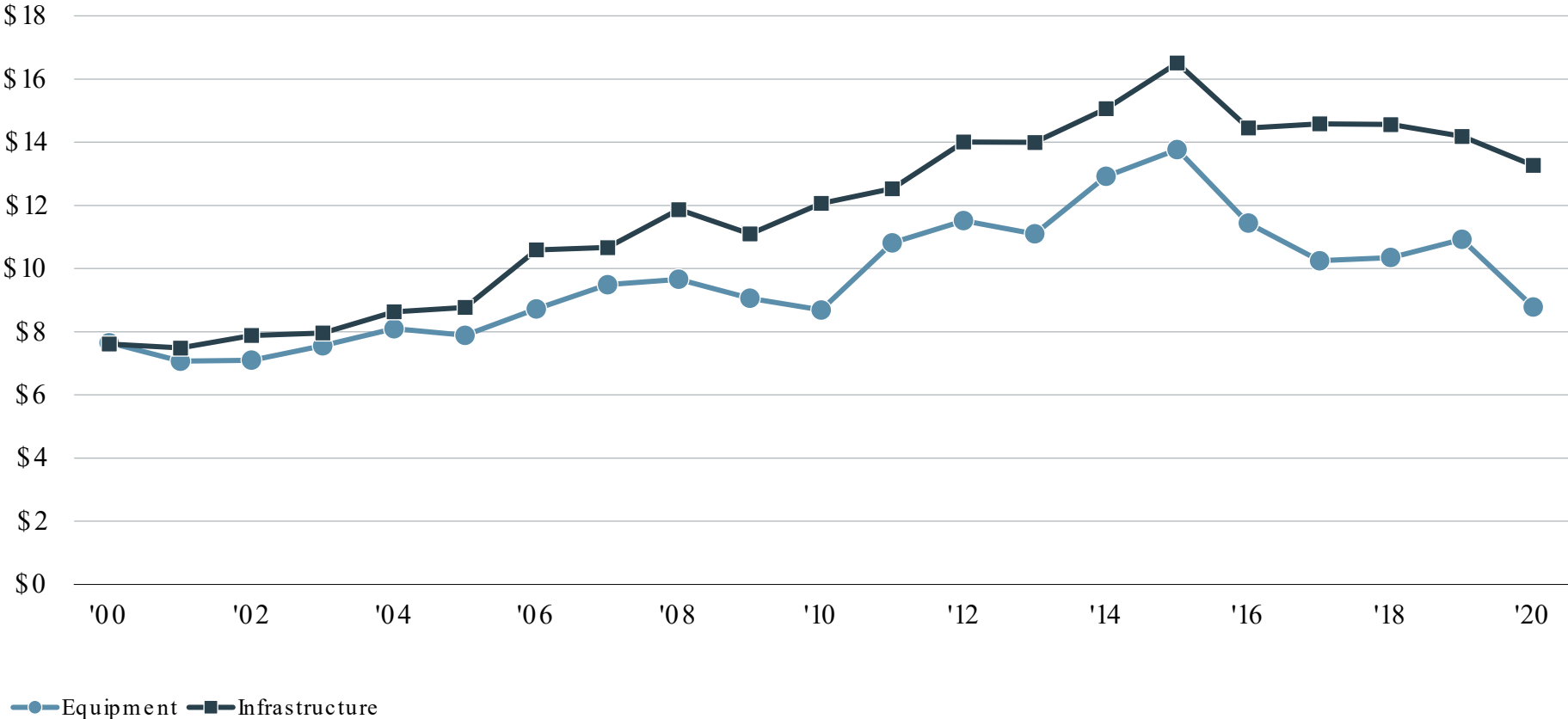
RR CAPEX \$ billions, current dollars



Data are for Class I railroads.
Source: AAR

Railroad Spending on Infrastructure and Equipment

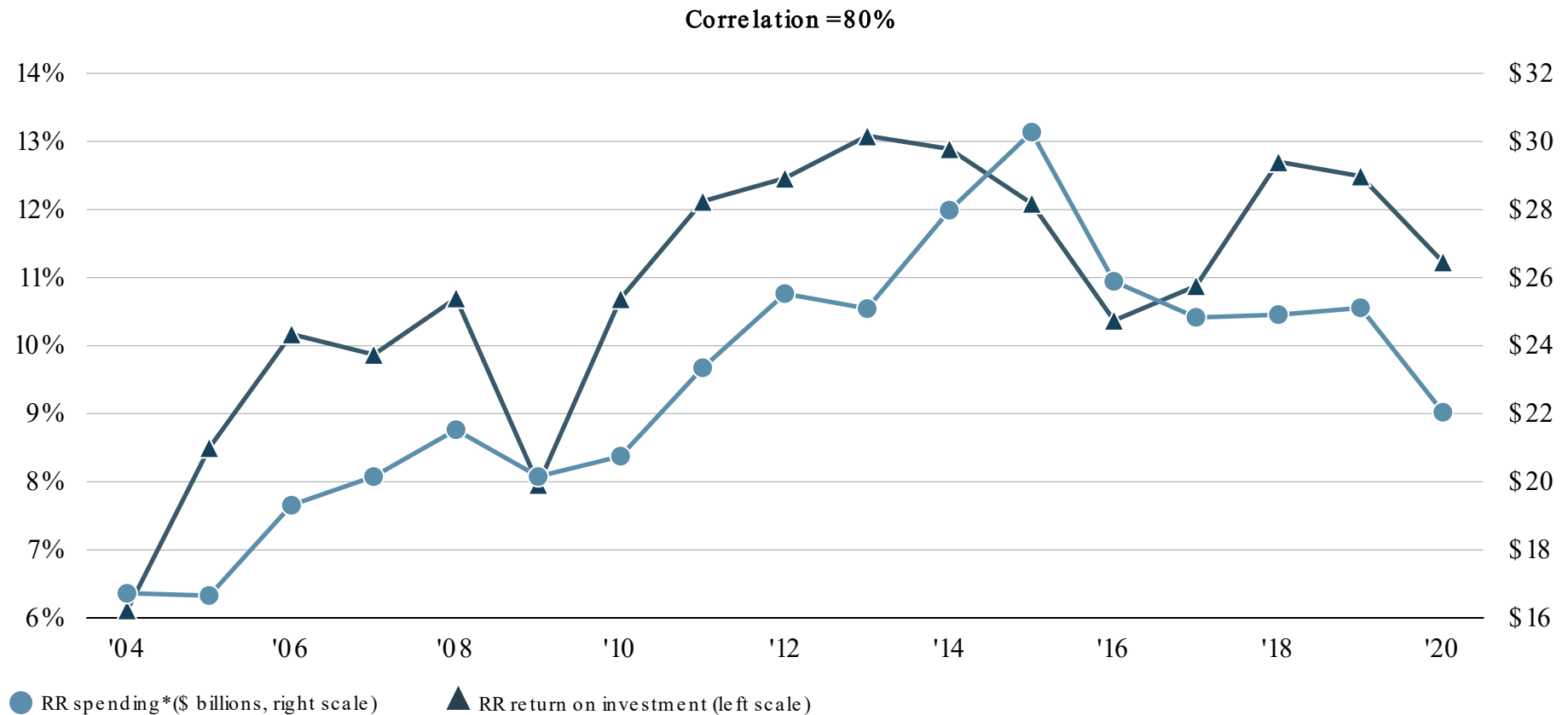
RR CAPEX \$ billions, current dollars



Data are for Class I railroads.
Source: AAR

There's a Strong Positive Correlation Between Railroad ROI and Spending

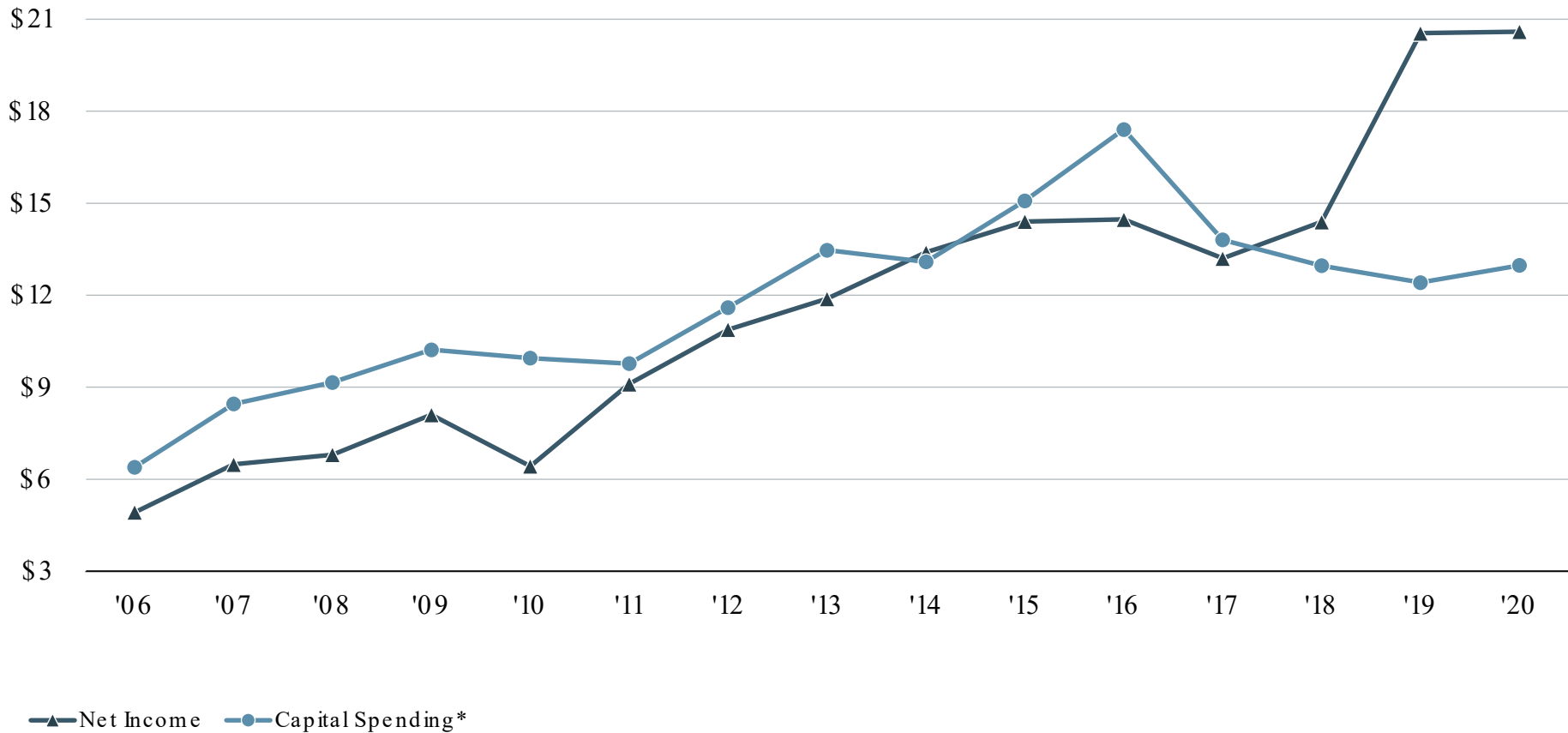
Railroad ROI & RR Spending



*Capital spending + maintenance expenses.
Source: AAR

Higher Rail Net Income and Higher Capital Spending

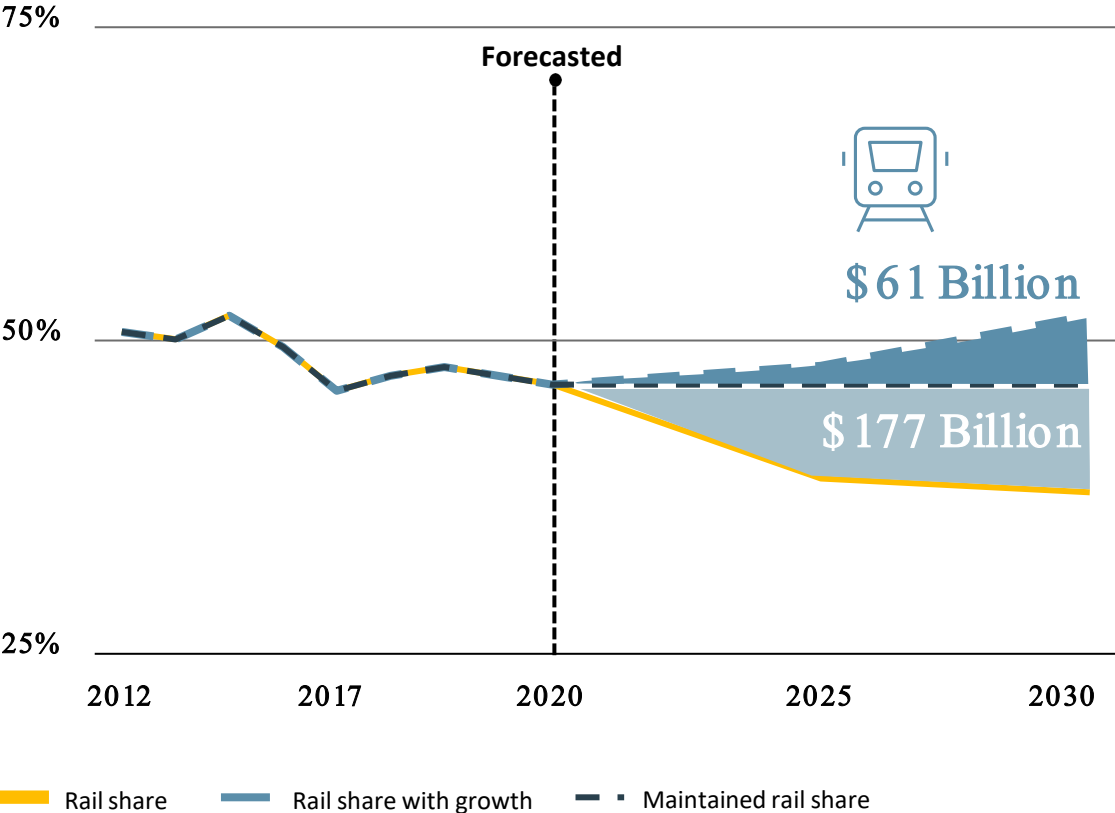
Correlation between net income and rr capex (\$ billions)



*Net income for 2017 has been adjusted to account for tax effects from the Tax Cuts and Jobs Act of 2017. Data are current dollars and are for U.S. Class I railroads.
Source: AAR

By using available capacity, railroads could add

Freight market share analysis and forecast by ton-mile



Gaining a half point of share per year delivers growth that by year ten fills current available capacity



Assumes no material technology advancements

Source: © Oliver Wyman



NARS recognizes

Tony Hatch

with the

**NARS 2019 Person of the Year Award
for his steadfast support of NARS and
its regional associations.**

*Thank you Tony for your guidance, dedication and service
to NARS and its regional association!*

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