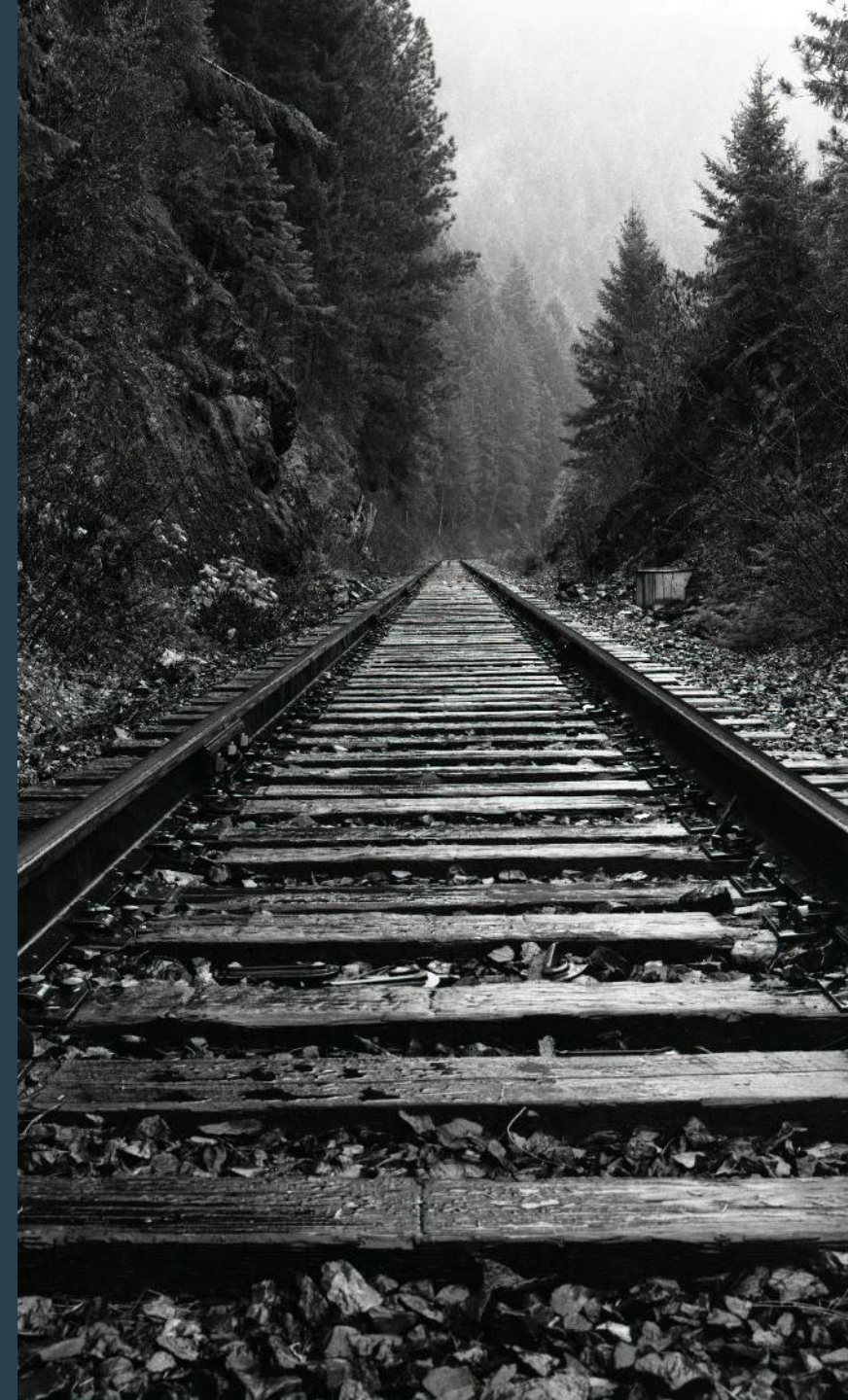


# 2025: Rails at the Crossroads – Burning Down the House?!?

## Trends and Insights

Anthony B Hatch  
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SANDHOUSE HOLIDAY 2025



See new IANA White Paper "***Intermodal at the Crossroads***" wherever railway reports are sold! Updates covering Tade Wars and Transcons! Get yours today! Impress your friends! And....Coming Soon, new White Paper on ***SHORT LINES/3<sup>rd</sup> Golden Age!!***

# 5+ Enduring (?) Railroad Competitive Advantages

- 1 **Labor Advantage**  
(ex: Double-stack LA-Chi – or Rupert-Toronto)<sup>1</sup>
- 2 **Fuel Advantage (2A)**  
(4:1 ton/mile; AAR)<sup>2</sup> – So 2B is **EMISSIONS**/Environmental Advantage (see...WMRT, Unilever, etc.)
- 3
- 4 **Infrastructure Advantage**  
(ASCE Grade B- after the IHS buildout; user-pay and capex to support changing logistics patterns – ex: transcon)<sup>3</sup>
- 5 **Railroads' Excellent Financial Condition, Liquidity, Free Cash flow**
- ? **Railroads' Historic Ability to Reduce Expenses in a Known Slowdown** (2009, 2020)<sup>4</sup>

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

# The Growth Pivot vs the Cult of the OR

- Rails are back to stability in operations
- Two outliers returning to the pack
- High 50s OR may be new peak performance given new labor contracts
- Gains from improvement from peak margin are increasingly de minimis in terms of earnings/cash flow....
- The ONLY option is Growth
- But gaining share will lead to improvements in revenues, EBITDA – and ROIC
- And maybe even in OR (per Oliver Wyman/STB testimony)
- AND, the OR is “the outcome of a process” (Keith Creel, CPKC, 2014 and 2024 ***RailTrends*** *Innovator of the Year*)
- Short-term investors and activists have targeted Intermodal as an inflator of the OR
- Railroads pivoting to growth in the longest *freight recession in living memory*
- Proxy fights, management pressures and change-outs a threat to long term thinking, resiliency
- The Race is ON!

# The CN Mothership and the Diaspora

- Is it ***Band of Brothers*** (positive) or ***Game of Thrones*** (not so positive)?
- Vena the man at UP
  - after UP's regulatory relationship deteriorated, its messaging unclear, and disappointing results/not fulfilling "greatest franchise" potential
  - Initial improvements obvious
- House Creel plots the Red Wedding
- Cory replaces Boychuck at CSX COO
  - "Culture change" & team building
  - Similar pattern as at CN
- Orr at CPKC then....
- Orr at NSC! Building a team
- The return then retirement of the Old Guard at CN
- Ed Harris on the BNSF Board
- Still out there: Boychuck, others....

# Rail Transcon? Why Now – a Timeline

- 2000 – BNSF-CN rejected/"Merger Moratorium"
- CPKC – "old rules" – "**Maintain** competition", win – thought to be *the last merger ever (?)*
- CNKC – "*new rules*" – "**enhance Competition – loses (over VT)**"
- Peace in the valley – benefits of CPKC single-line service, extended LOH
  - But not (yet) in volumes (~9K trucks-off-highway/15% of target?)
  - Not much belief in "oversight" – see Laredo
- **RailTrends 2024** – Bailey/OW speech – "Rails must grow; if not, the choices are (in effect) shrink & share – or merge"
- Fear & Loathing begin to creep in:
  1. No CEOs save BNSF "came up from the ranks" – two are "not railroaders" (should that matter?; legacy issues, succession plans)
  2. No growth – in volumes, share – or market cap (pandemic/trade wars/freight recession – no real test of the Growth Pivot)
  3. New administration – anything goes? (Is that true? Ask Google, DoJ antitrust head)
- Arbs on the case, deal chasing, activists, misinformation
- **Initial talks, we now know, began last December**

# Rail Mergers – Clear (But undefined) Benefits

- Elimination of ***interline issues*** (as a concept); *crew* changes, to be sure, but not *carrier* changes (Oh, what a tacit admission of failure!)
- Service and capacity – and speed – increases
- Global not regional customers (allowing for product and geographic competition)
- Reduced SG&A
- Repurposed mid-continent hubs, yards & terminals
- More focused IT spend
- Faster decision making (one BoD, not two or three or....)
- The Watershed Opportunity (BUT, what is it?) The “Blind Man & The Elephant” analogy
- Could solve “problems” of legacy, succession (see BNSF & Krebs)
- 125-250bps (Oliver Wyman)
- All great – I’m a believer – IF unchallenged and not modified....



# Rail Transcon M&A – The Risks (Sailing off into the Great Unknown–Off the Map or New Discoveries?)

- “Enhanced competition” is not defined (see MAD example)
- Mergers “open the books” on railroad practices
- New breed of shipper would get involved (think Amazon, Walmart, UPS/Fedex, Target, etc) for the first time
- “Death by 1000 cuts” or “deep structural changes”?
- ***UP pegs the cost of remedies at \$750mm*** – still a guess, and a form of socialism?
- Environmental reviews slow major routing changes (“\* trains/day rule”)
- *Open Access* – “Bring it on”? Don’t believe it! Wherefore Capex? BIG, etc – a huge wealth transfer to shippers (Europe)
- *Wither the Canadians and Grupo Mexico?*
- Hostility unwelcome
- First-mover advantage? Not really....I believe in ***2<sup>nd</sup> Mover Advantage***
- Un-known Watershed effect
- Wildly over-optimistic Street estimates (for example, studies of interline ignore short lines)
- Could transcon M&A lead to *more regulation*?
- ***Is that worth it for 125bps?***



# Recent Events – Going off the Rails on the Crazy Train (RIP Ozzy)

- Vena talks....Zampi talks....Claude walks....(replaced by Anderson – important; and the Ancora 3 remain)
- Someone (inside the house? Activists? CEO?) that UP has engaged Morgan Stanley, traditionally NS' banker!
- Someone (else) leaks that UP is talking to NS – *now labeled “advanced discussions”!*
- *Can't anyone anywhere keep a secret?? Even if they're paid \$200mm?!?*
- “Sources” say BNSF has hired Goldman (because of Rishi?) Warren states that “sources” lie
- Same or other “sources” state that CSX is looking for an advisor (what – NOW?)
- BNSF and CSX only two railroads without financial advisors, strategists
- *Berkshire has never issued stock for deals, giving BNSF some limits and encouraging, perhaps, a “wait & see” strategy*
- Massive misinterpretation of Commissioner Hedlund's remarks (“Bring it on”) – about STB capacity for deals not favorability
- ***Critical – define or evade public interest, enhanced competition – historically applied to rails only.***
- UP-NS announce, decide to not even bother, no VT

# Rails Transcon M&A– Is this *really* happening?

- **From “advanced talks” to a UP-NS deal! Some thoughts:**

- This is a straight take-over
- No Voting Trust!
- \$2.5B breakup fee! (So too late to back out now, “in it to win it”?)
- \$1B in economies
- \$1.75B in EBITDA gains from synergies
- \$750mm in “remedies”
- No big reduction in Chicago? See Environmental Review Regs - *gradualism*
- To be filed ~ by/before January 29, 2026/likely Q4/Starts STB clock for the next 16-18 months

**Now we await reactions and try to tally the costs vs benefits (with what we know)**

- Initial shipper/labor opposition – is it real or a bargaining position?
- CPKC goes off! Canadians on the outside, but not at the bargaining tables
- CSX puts on its best dress
- BNSF in stony silence – no shares to offer, but BH has ~\$344B in cash. Will they
  - Start a bidding war? **NO**
  - Fight? Wait? **Unclear**
- How much momentum lost, distraction, morale issues at target carriers etc?
- Public vs private negotiations
- Reciprocal switching/open access; crew size, train length, remedies, etc

**What does STB do after 30-day review of files application?** *Critical to all future negotiations, posturings*

# “Phony War” more early action than expected

BNSF & CSX announce new intermodal partnership

- A sign of competitive reaction that supports M&A
- Or a sign that you “don’t have to merge to benefit”
- In the works (remember BNSF-NS deal) but clearly accelerated
- Berkshire Hathaway says “no deal”/CPKC says “no deal” (exposing Ancora)
- No positions written in stone; shippers ante
- But after 3 “wins” for the opposition, STB Commissioner Primus was fired (deal related or DC dirty tricks?); Kloster nominated, Schultz extended (both subject to Senate confirmation)
- Battle of the press release and conference remarks
- Primus!
- CEO Joe!
- UP SMART agrees to support the deal (without getting 2-man concession)
- All await the Application – Vanilla or Tutti Fruity?
- STB then has 30 days, and awaaaaay we go!

# Key Givens & abh Assumptions/Rail Mergers

- There are *three – no, four* important “New Rules” boxes to tick to gain STB approval:
  1. *“In the public interest”* (for example, “trucks off the highway” fits here, but likely not for #2)
  2. *“Enhance competition”* – and by precedent, since the STB does not regulate trucks or barges, that means **RAIL** competition!
  3. *Benefits accomplished only by merger* – see BNSF-CSX, or Falcon! (It will be fun to watch the rails positional “flexibility”!)
  4. *“Downstream Effects” consideration* – more M&A?
- The STB is an **independent** entity not subject to White House decision making (we think); POTUS has done on to discuss UP and its un-named leader
- I have full faith in the Board and the Chairman
- **Rail regulation is completely, entirely dissimilar to other regulation** (environmental, labor, etc) – **Rail Regulation is NON-Partisan**
  - there is NO partisan position on rail regulation, an arbitration of market power between large companies/industries –
  - For example, there is no partisan take on ACC vs UP
  - Therefore, why assume that the GOP, or the White House supports this merger? Over the possible objections of bigger industries?
  - Does enhanced intermodal service for global customers fit with reshoring “strategy”?
  - *Shippers will decide, the STB will interpret, the White House will watch*
- *Who was President at the time of the “Golden Spike”? I’ll wager a \$50 bill....* **There is NO (logical) reason for the White House to intervene in B2B decisions; there is no political upside, only risk**
- *“Remedies” applied to the merger parties (UP+NS) do not apply to other carriers (access, etc)*
- **If** approved without a steep cost, **THEN** BNSF-CSX (+CP?) will follow forthwith, no matter who occupies the White House
  - Precedent will be set
  - “enhanced” will be defined
- *The benefits are real, if undefined – but what is the cost (dollars/time/distraction/concessions etc) to achieve them?*
- *If the costs prove to be too high, will UP (time, commitment, ego, \$2.5B) be able to walk away?*

# Meanwhile, back in the rail/real world, POLITICS overtakes ECONOMICS (for now)....

- Tariffs and trade wars, round two – new deadlines, constant confusion
- Rails trade weight significantly more than figures publicly discussed (38%/AAR; 25% CSX, etc) – Canada/Mexico, inputs to export commodities (fertilizers, etc), transloaded containers
- Uncertain goals means uncertain reactions, no crystal balls – CN ramps down?
- Rails (transport) is a *derived-demand* business
- Uncertainty breeds stasis
- Near-shoring on hold (AMTI); political risk south of the border now greatly outweighed by risk *north* of the border
- Re-shoring a fantasy – but a transcon sales aid?
- “Landbridge” is not a solution
- Freight recession extended
- This too shall pass!
- But the FRA/technological revolution that may unfold partially (only partially) compensates for the top line risks

# My Plea in 2021-22: “Short Lines To the Rescue of Class Ones?”

## ***Class One service crisis and the impact on/of regulators (STB/FRA) and Legislators***

- New focus, data on First Mile/Last Mile (and it ain't pretty!) – made more intense with Reciprocal Switching?
- Service failures are manna to STB concerned about rail market power (price)
- STB use of *common carrier obligations* as a lever (UP/Foster Farms), focused on weekly switches
- Declining Class One carload growth since the 2008-9 Financial Crisis

## **SOLUTION?**

### **Increased use/creation of Short Lines!!**

- Short lines have consistently out-grown C1 in carloads
- Short lines offer tailored, customizable switching services
- Short Lines have better work rules, less severe labor shortages
- Short Lines are looked upon quite favorably by regulators and legislators!
- Watco's Dow and especially Dutchtown Southern (Louisiana/CN) increased weekly switching from 3-5 to 7+ and grew carloads by over *one third* in the first year of operations – win (customer switches)/*win* (Watco new business)/win for C1 partner CN (more cars for its long-haul business)
- All SLHCs have logistics/switching arms etc

## ***So why is the momentum of C1 strategy seemingly to buy or retake SLs***

- I support a “feed the beast” strategy (looking to extend a C1 market reach – ex CN 2018-21)
- Short lines being “taken back or in” – Pan Am, MRL etc
- However that should not preclude thoughtful C1-SL partnerships (that solve customer problems!) – ex RailPulse
- *Nonetheless, I see no evidence of C1 leadership taking these steps (yet?)*
- *There have been more C1 SL Meetings, discussions (ASLRRRA)*

# Short Lines – Dawn of the *Third Golden Age*?

- The 1<sup>st</sup> – Post-Staggers – CREATION
- The 2<sup>nd</sup> – ~2017?-present? Multiple explosion and the entry of the Infrastructure Funds (and with P&LE/Fortress – it doesn't appear over yet!)
- The Third Golden Age – short lines as key player in the railroad industry pivot to growth
  - One of three key components to C1 growth pivot (OW) along with Business Development and Intermodal
  - UP (!) in Eugene and KC
  - Big C1 teams roam ASLRRA Convention
  - New VPs of First Mile/Last Mile – first NS, then BNSF
  - Programs such as BNSF Select
  - New Partnerships initiated after CPKC
  - New Technologies employed – RailPulse, Intramotev, Parallel Systems
  - New DC initiatives (45-G+)
  - Intermodal outreach – PHL, Iowa Interstate, GWR
- But....will Class Ones be too distracted or demoralized to continue to pursue deals?

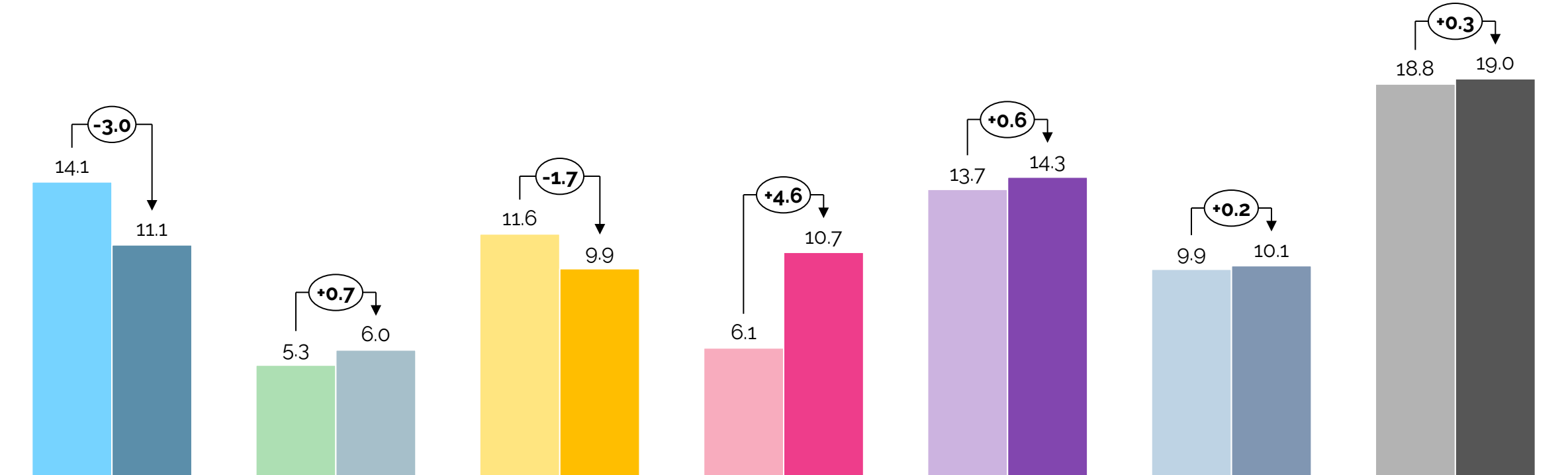


# The Industry is converging on a return on invested capital of 10%

UP and CN swapped places with UP having an industry leading 14.3% ROIC and CN coming in second at 11.1%

Return on invested capital (4-quarter rolling average based) compared to Q2 2024  
Percent

Q2 2024 Q2 2025

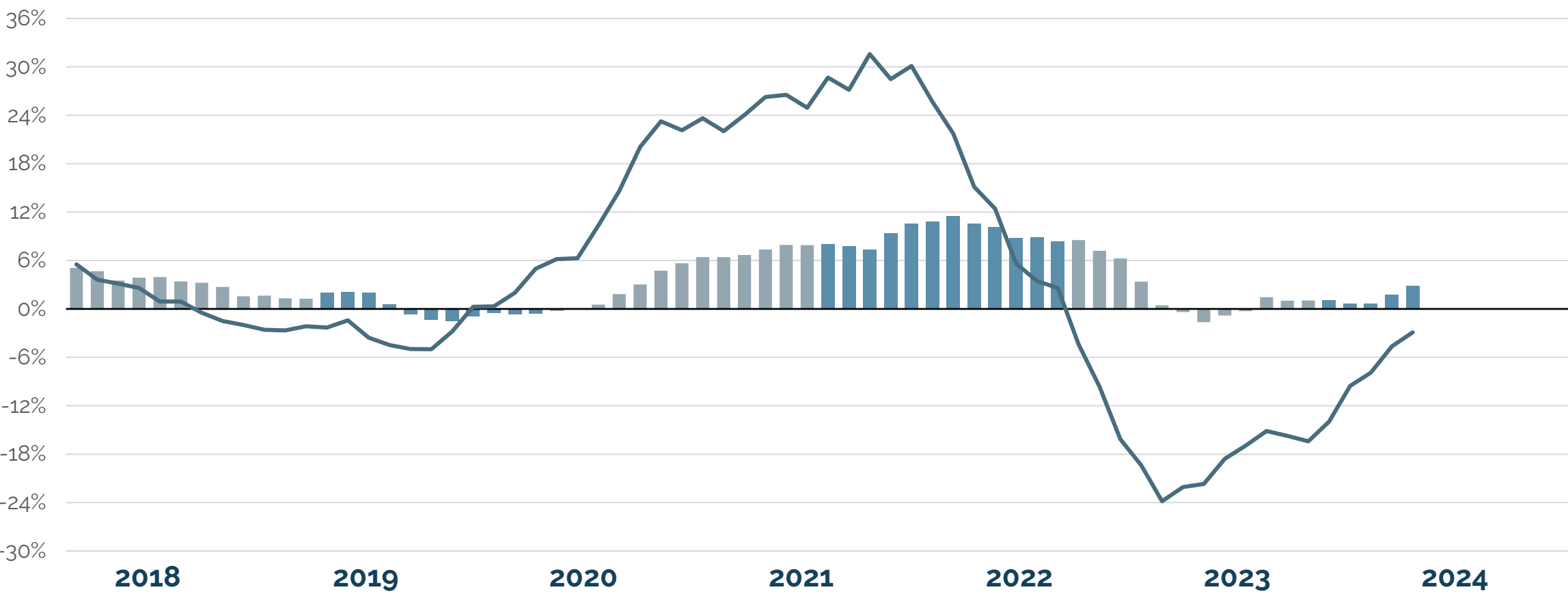


Notes: ROIC is calculated for all reported companies as (Net Income) / (Total Debt + Total Equity), based on 4-quarter rolling averages of reported values. Both UP and CN calculate their own Return on Invested Capital, but our methodologies are different, and therefore ROIC numbers may vary from reported results. CN reported ROIC for Q4 2023 and 2024 includes interest expense, net of taxes in their return calculation, and CN reduces invested capital by cash and cash equivalents. They reported 2023 and 2024 ROIC of 16.8% and 12.9%, respectively, a decline of 390 basis points. UP also adds interest expense, net of taxes in their return calculations, while adding operating lease liabilities as part of invested capital. They reported 2023 and 2024 ROIC of 15.5% and 15.8%, respectively. All financial information for CPKC reflects either combined CP and KCS results prior to the merger or the consolidated CPKC reporting post-merger. BNSF is BNSF Railway, not BNSF, LLC.

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

# Truck Rates Are Down....

Year-Over-Year Change in the Producer Price Index

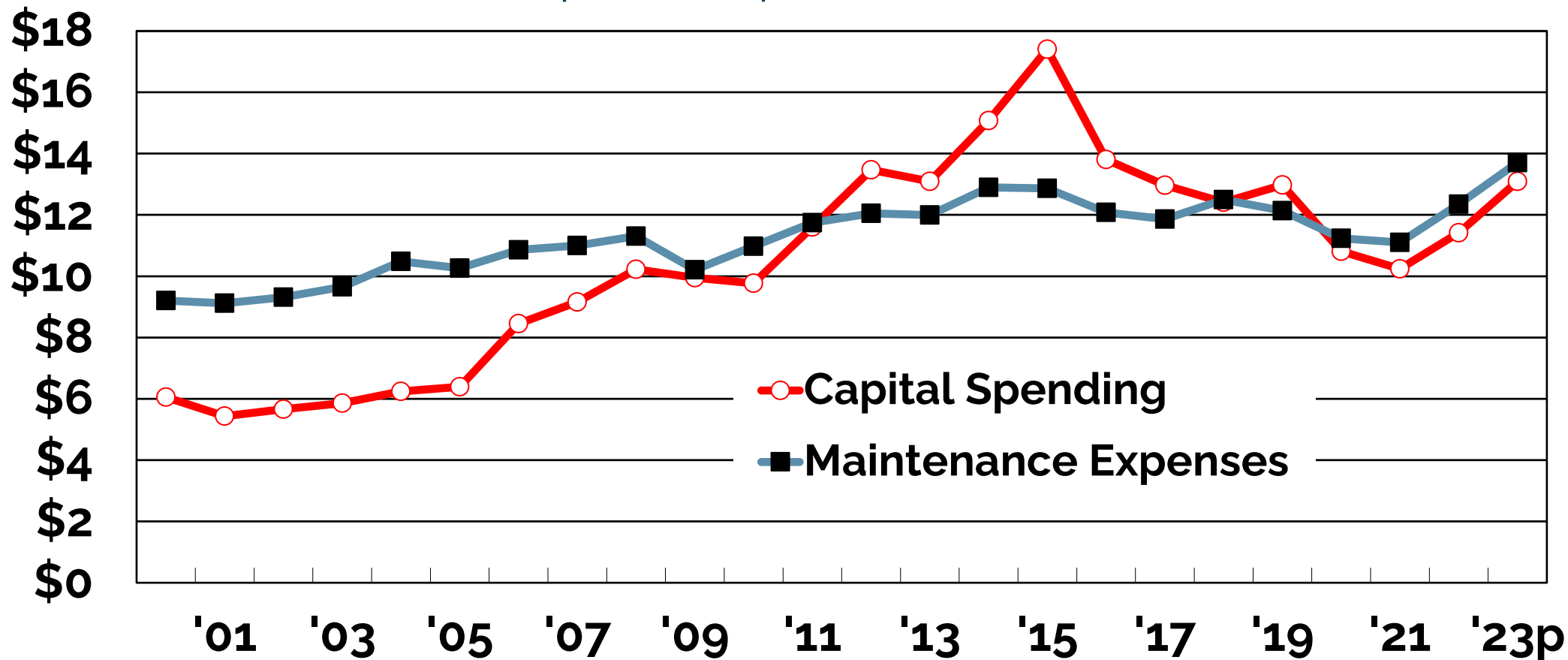


Source: Bureau of Labor Statistics

# Mexico's Moment?

- For rails, since NAFTA it has *always* been momentous (yet – it's 2-3% NA IM total units!)
- Near-Shoring is (was?) the headline grabber – if for real? FDI into Mexico reached an 11-year low in '24
- X-Border IM (US-Mexico) declined in 2024!
- 1) Reasons for concern/South of the border:
  - Pemex support (impact on cost, emissions)
  - KKR example in refined products – Constellation Brands, etc
  - Passenger traffic forced on the freights?
  - Border shutdowns
  - Election landslide, repercussions (COFECE)
  - 25% of Latam GDP; 17% FDI – Near-shoring always was more hype than reality (Tesla!)
- But – Huge Rail/Intermodal efforts: CPKC; Meridian, Falcon, especially now BNSF/JBHunt
- 2) Reasons for concern/NORTH of the border: Tariffs!! Immigration!! And USMCA “review” in 2026
- Canadian election, response; Elbows Up!
- Modelo Especial! AMTI

(\$ billions, current dollars)



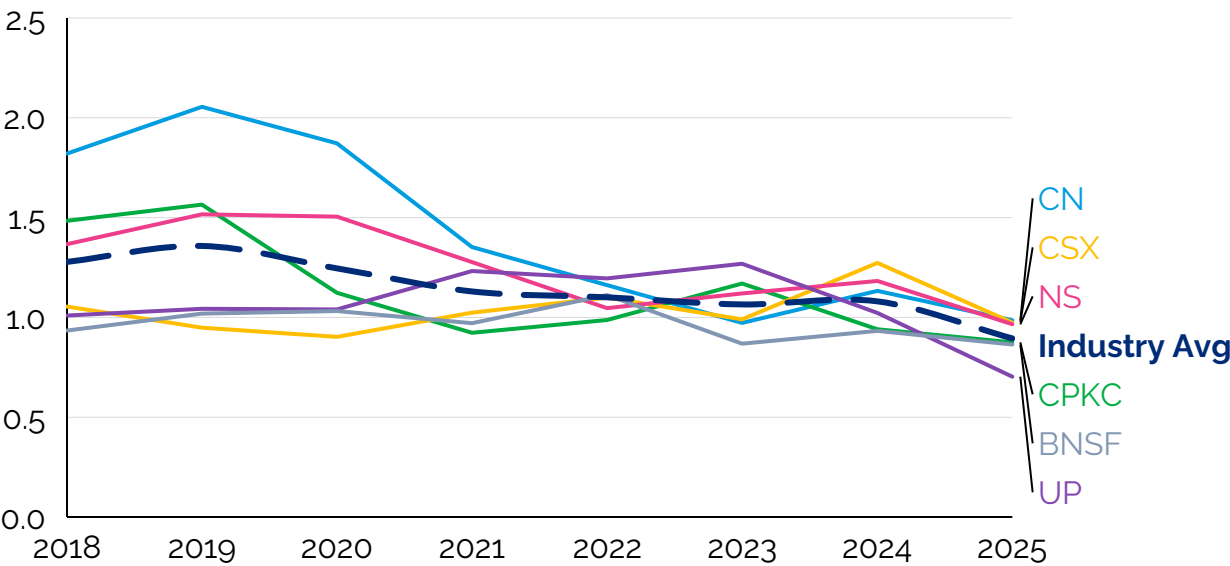
P – preliminary Data are for Class I railroads. Source: AAR

# The Industry continues to improve its safety record post-covid

CN and NS have consistently improved their injury rate the most, while UP has improved their equipment incident rates the most

## Employee injuries

Quarterly values per 200,000 employee-hours

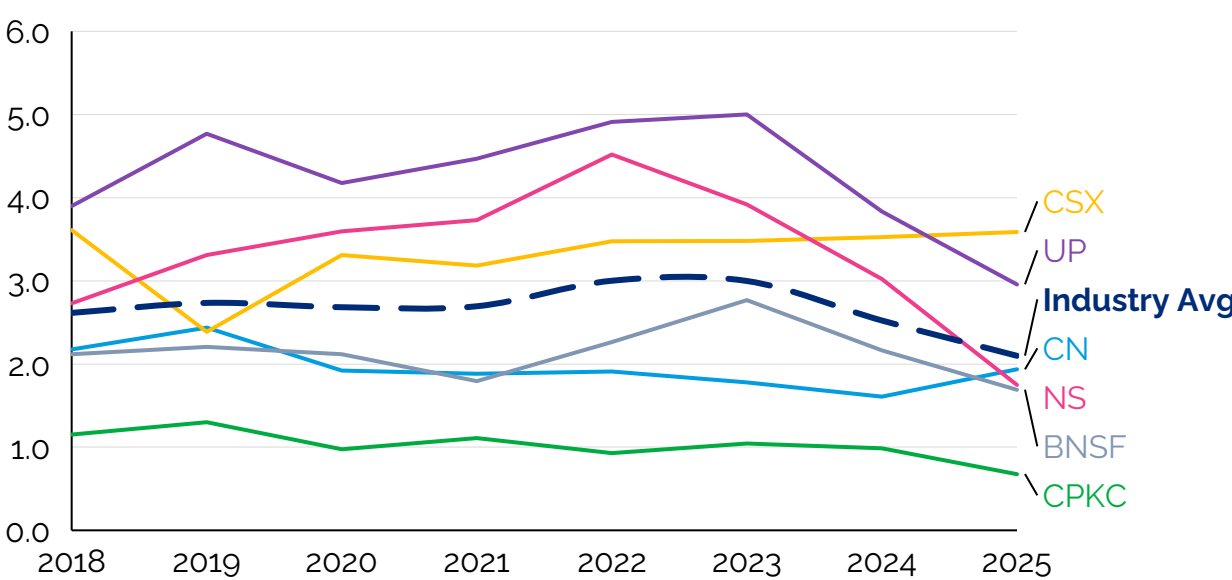


**3-year trend:** Q2 2022 to Q2 2025  
**Long-term trend:** Q1 2018 to Q2 2025

	CN	CPKC	CSX	NS	UP	BNSF	Industry Avg
3-year:	-12.6%	-2.2%	4.3%	-4.8%	-7.6%	-4.9%	-4.6%
Long-term:	-17.7%	-9.1%	2.6%	-7.0%	0.0%	-1.5%	-5.5%

## Equipment incidents

Quarterly values per 1 million train-miles

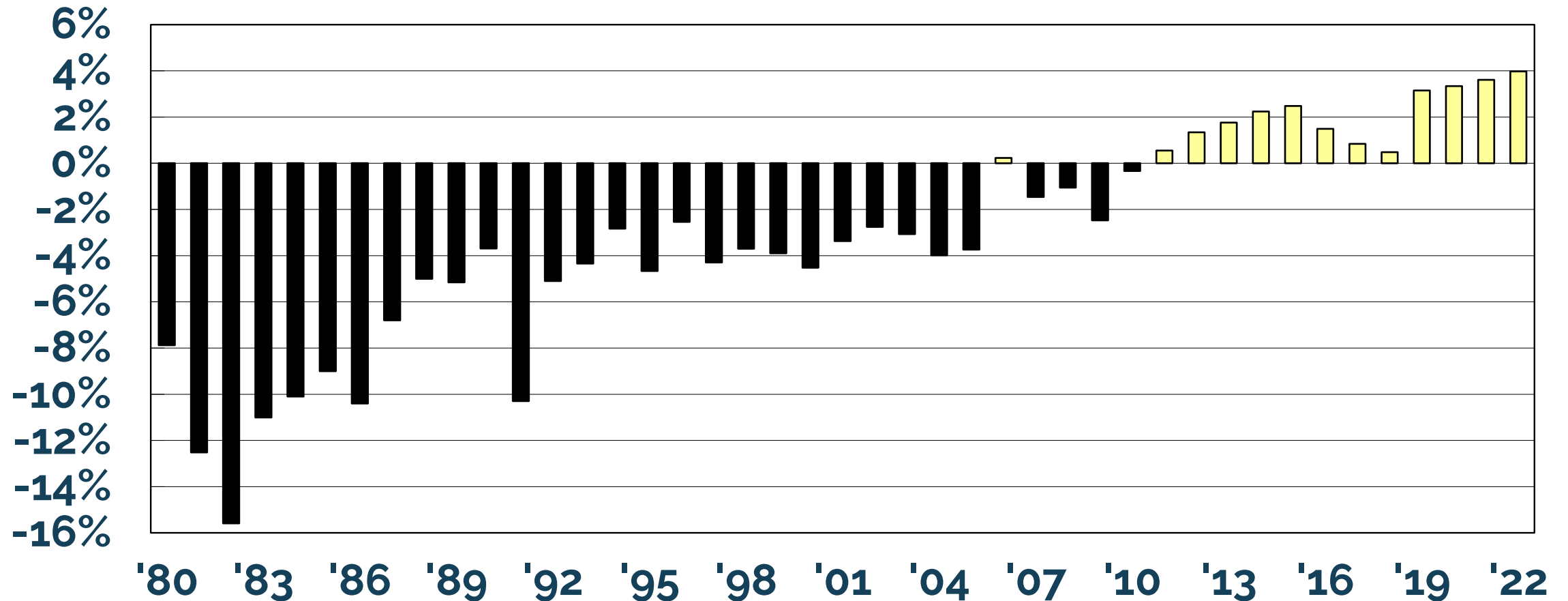


**3-year trend:** Q2 2022 to Q2 2025  
**Long-term trend:** Q1 2018 to Q2 2025

	CN	CPKC	CSX	NS	UP	BNSF	Industry Avg
3-year:	-4.3%	-4.2%	2.0%	-40.3%	-21.6%	3.4%	-10.8%
Long-term:	-9.4%	-5.1%	9.4%	-3.4%	-6.6%	0.9%	-2.4%

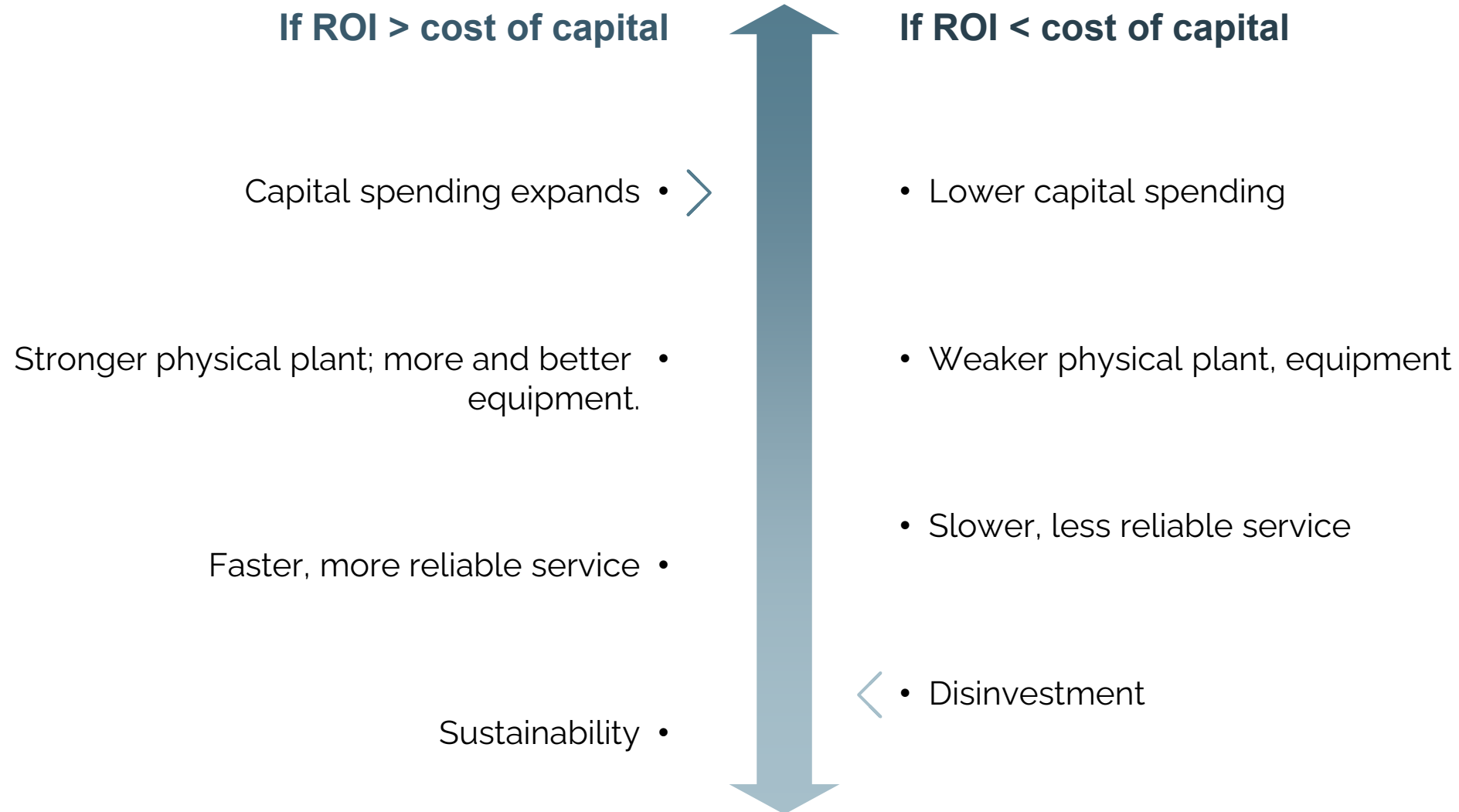
Note: Percentages may not add due to rounding. CN and CPKC figures originate from their respective financial statements, all other figures originate from the FRA. BNSF is BNSF Railway, not BNSF, LLC. Industry average evaluated as average across reported railroads, not weighted average  
Sources: Federal Railroad Administration; corporate financial reports; Oliver Wyman analysis

# The Spread: Between WACC & ROIC/STB (USA only)



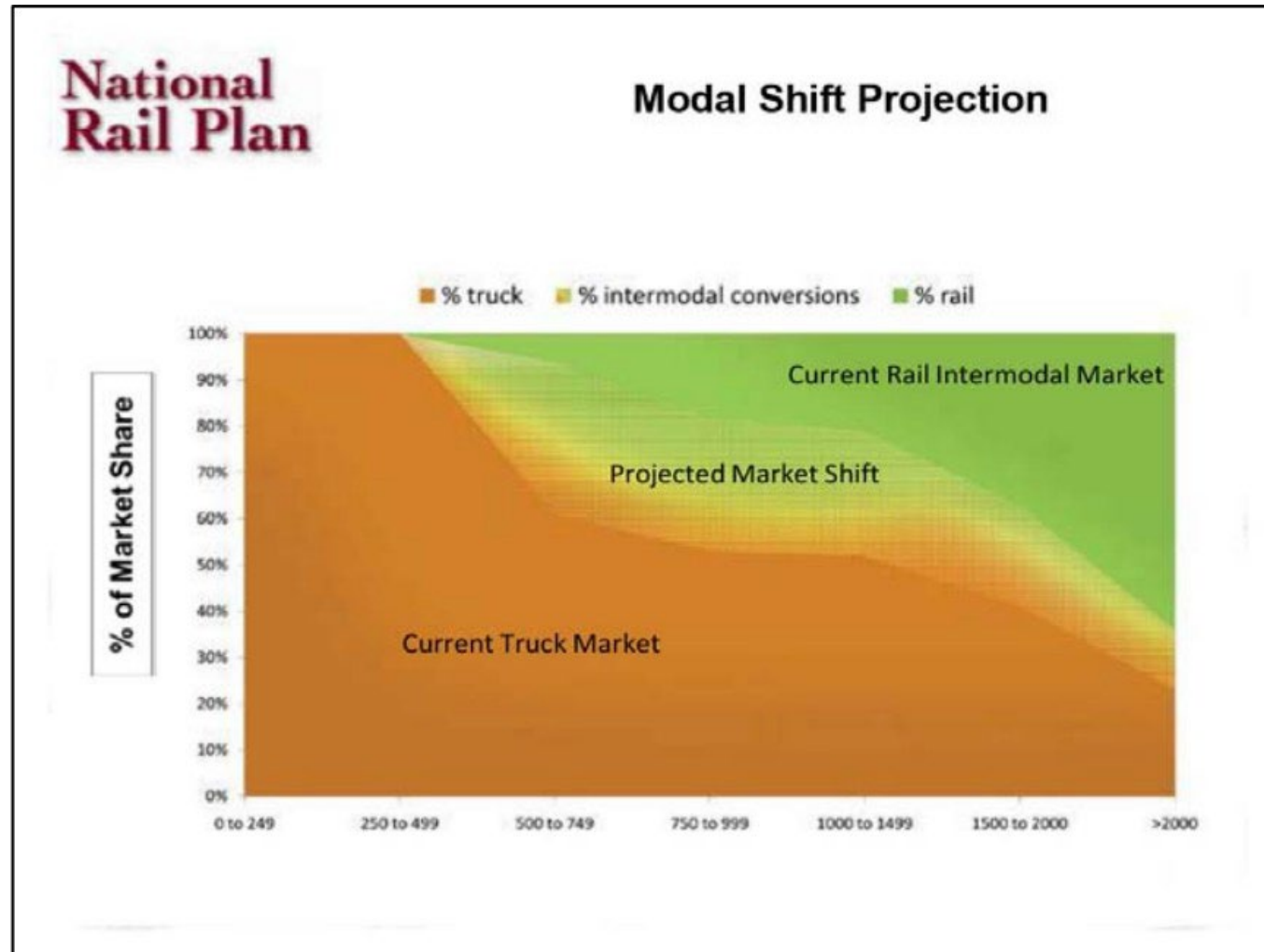
\*In 2006, the Surface Transportation Board significantly changed the method by which it calculates the rail industry cost of capital. Source: STB

# Return on Investment is Crucial





# Market Share is Still Out There



# Problem: These Are Coming



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STORMS"**

Preceded by a brief sneak preview of  
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(PBS) and wttw.com in April 2026.

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