Transit & Rail Advisory Committee

Funding Freight Rail

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Steamboat Springs, CO
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Today's Discussion Points

- Key freight rail characteristics
- Primary source of capital: earnings
- Capital intensity of freight railroads
- Future demand forecasts
- National Rail Capacity Study (2007)
- Public Private Partnership guidelines (BNSF)
- Federal Rail Funding Programs
  - Shortline Tax Credit
- States with railroad funding programs
- Example PPP projects

Key Freight Rail Characteristics

- Privately-owned network
- Same company usually owns, manages and maintains the track and operates trains over it
- No automatic access to another railroad's tracks
- Little government funding
- Regulation still substantial (FRA for safety; STB for rates, service, etc.)

Jim Young, Chairman & CEO

SECOND QUARTER EARNINGS RELEASE

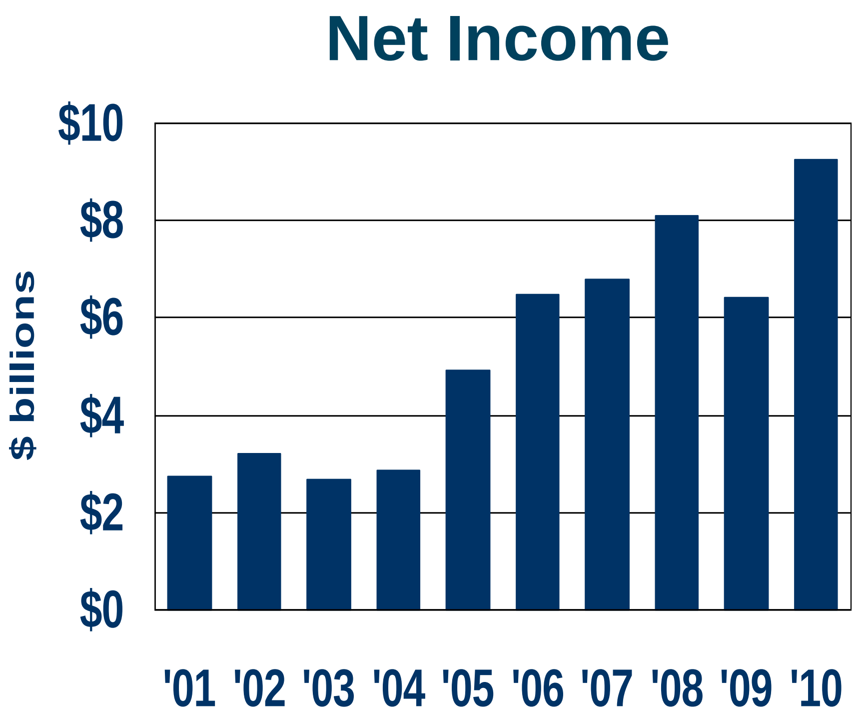
JULY 21, 2011

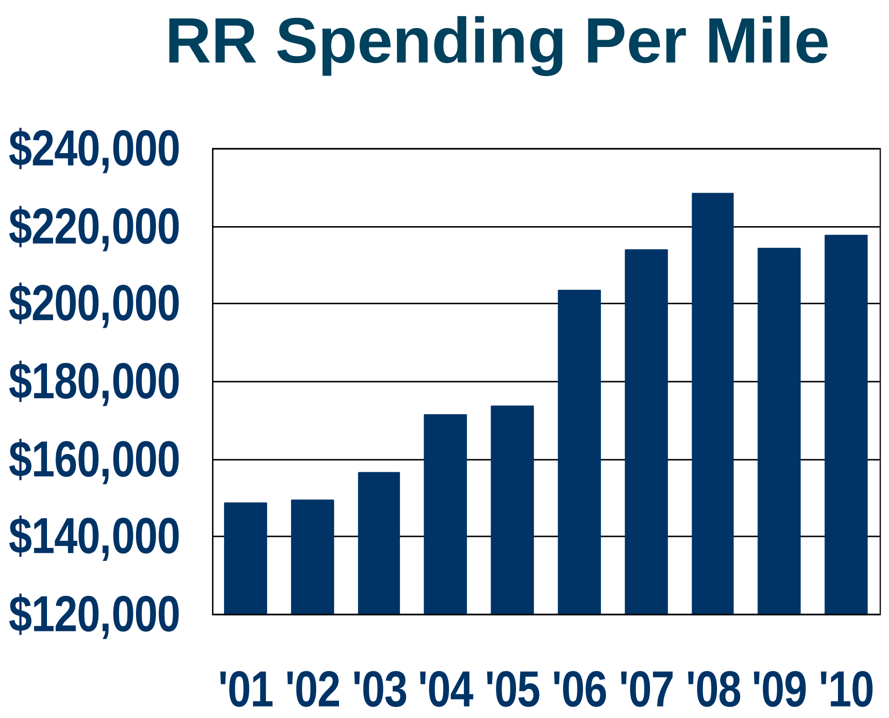
Second Quarter Earnings Summary

In Millions (except EPS)

	2011	2010	%
Operating Revenues	$ 4,858	$ 4,182	16
Operating Expenses	3,466	2,903	19
Operating Income	1,392	1,279	9
Other Income	26	19	37
Interest Expense	(148)	(152)	(3)
Income Taxes	(485)	(435)	11
Net Income	$ 785	$ 711	10
Weighted Average Diluted Shares	492.4	506.5	(3)
Diluted EPS	$ 1.59	$ 1.40	14

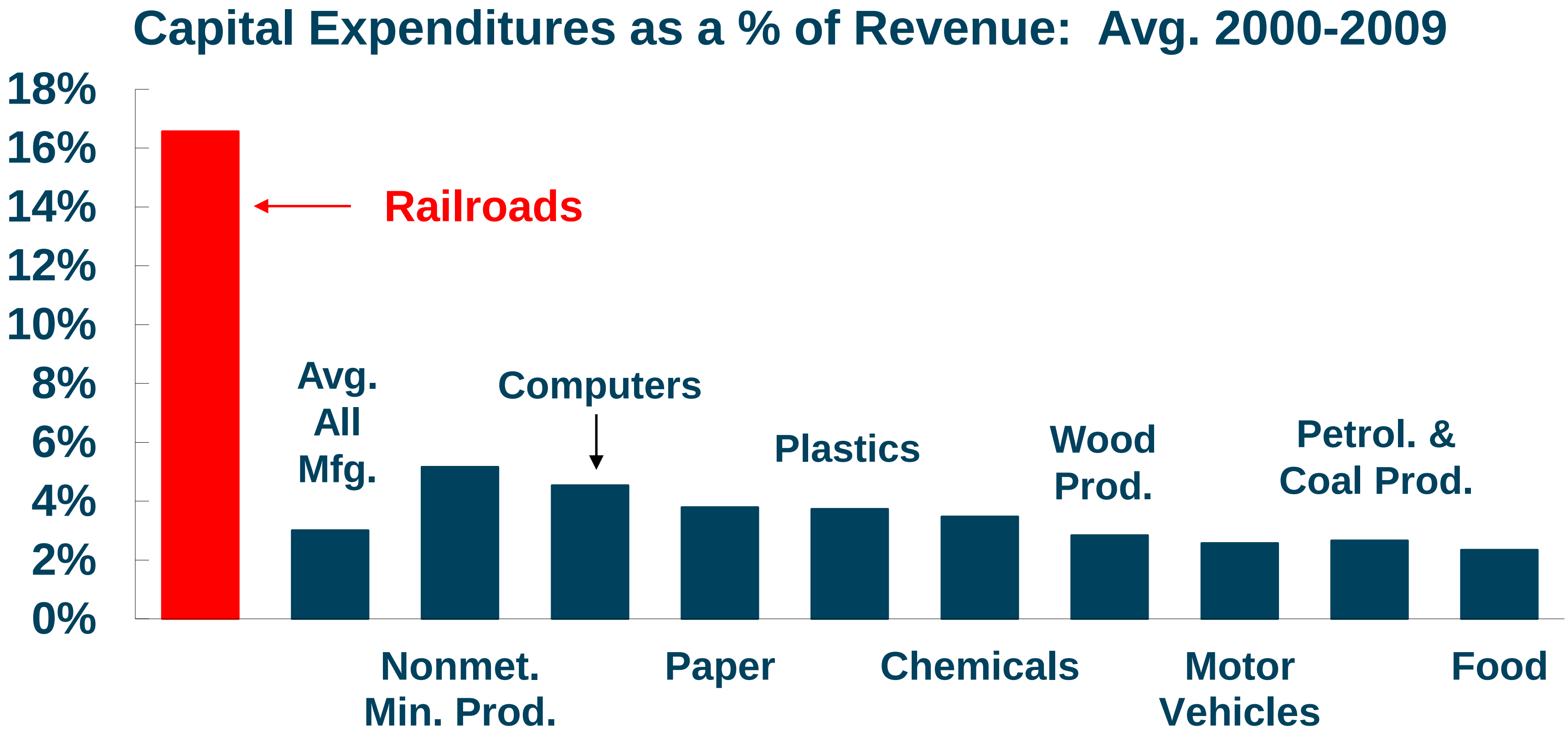
Today's Profits Pay For Tomorrow's Railroads





Source: AAR

Railroading Can't Be Done on the Cheap



Sources: U.S. Census Bureau, AAR

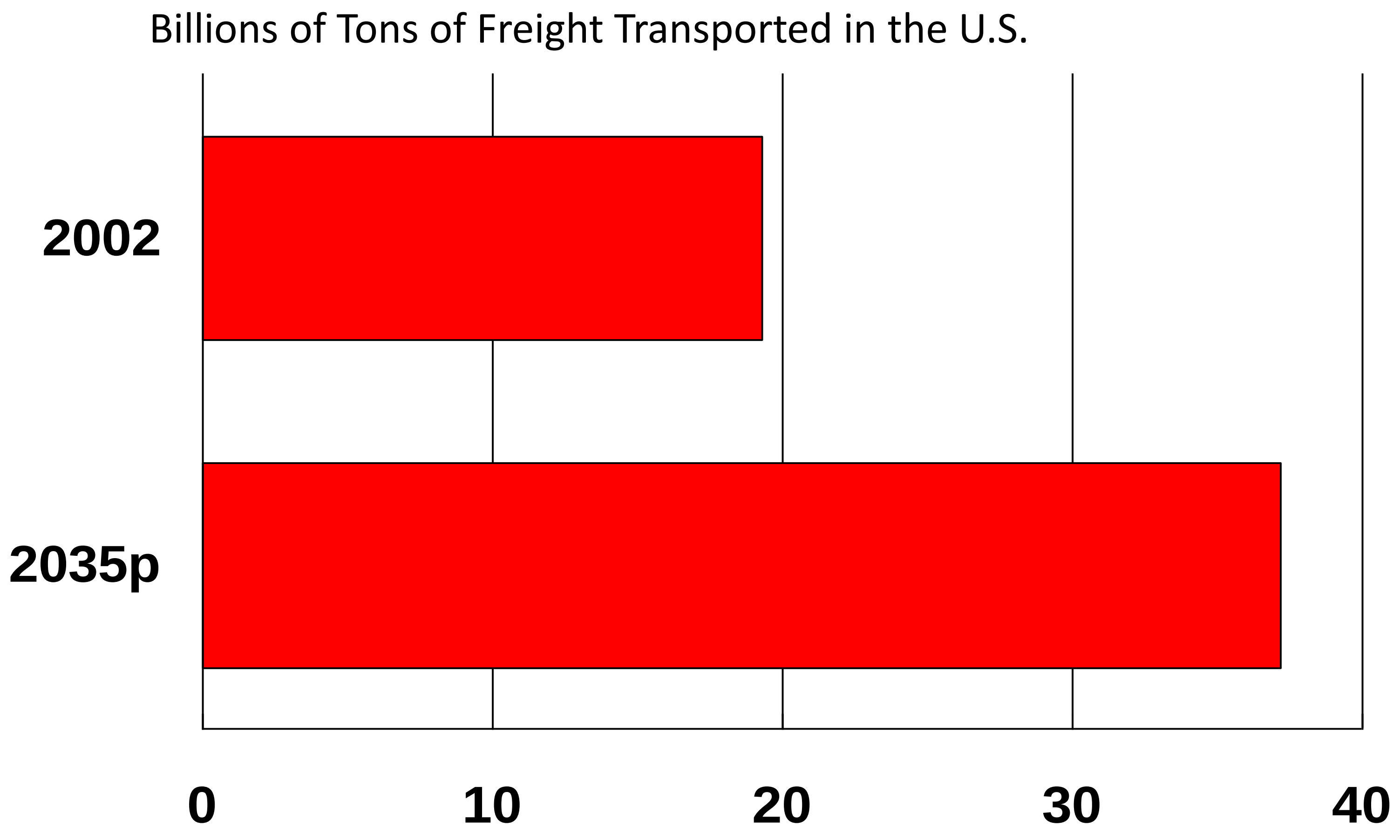
Railroads Spend More Than Most State Highway Agencies!

RR Spending on Way & Structures vs. State Highway Agency Spending - 2008 ($ billions)

		Total
1.	Texas	$8.40
2.	Florida	$6.24
3.	California	$5.65
	Union Pacific	**$4.91**
	BNSF	**$4.02**
4.	New York	$3.82
5.	Pennsylvania	$3.77
6.	Illinois	$3.50
7.	Georgia	$2.84
8.	North Carolina	$2.71
	CSX	**$2.70**
9.	Michigan	$2.52
	Norfolk Southern	**$2.48**
10.	Virginia	$2.39

Data include capital outlays and maintenance expenses. Sources: FHWA, AAR

Future Demand for Freight Transportation Will Grow



2006 U.S. DOT projection

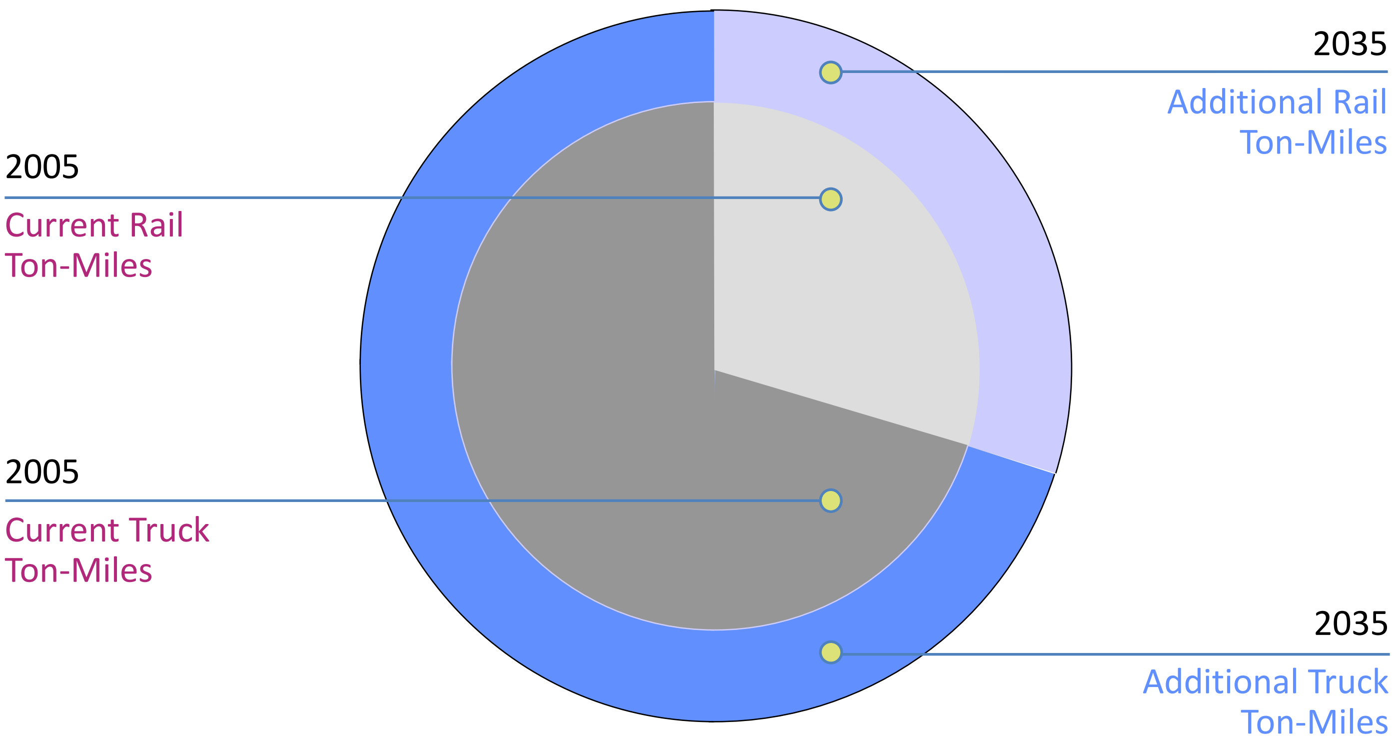
Freight growth is forecasted to continue in all major surface transportation sectors

AASHTO forecasts U.S. domestic freight ton-mileage to grow at 2.05% compound annual growth rate from 2005-2020

- Truck 2.32% CAGR = 60% increase in 2020
- Rail 1.94% CAGR = 55% increase in 2020
- Water .68% CAGR = 30% increase in 2020

Truck and Rail Market Shares in Ton-Miles - 2005 and 2035

Will the highway and rail freight systems have the capacity to accommodate future demand even if current modal shares remain the same? What will it cost?



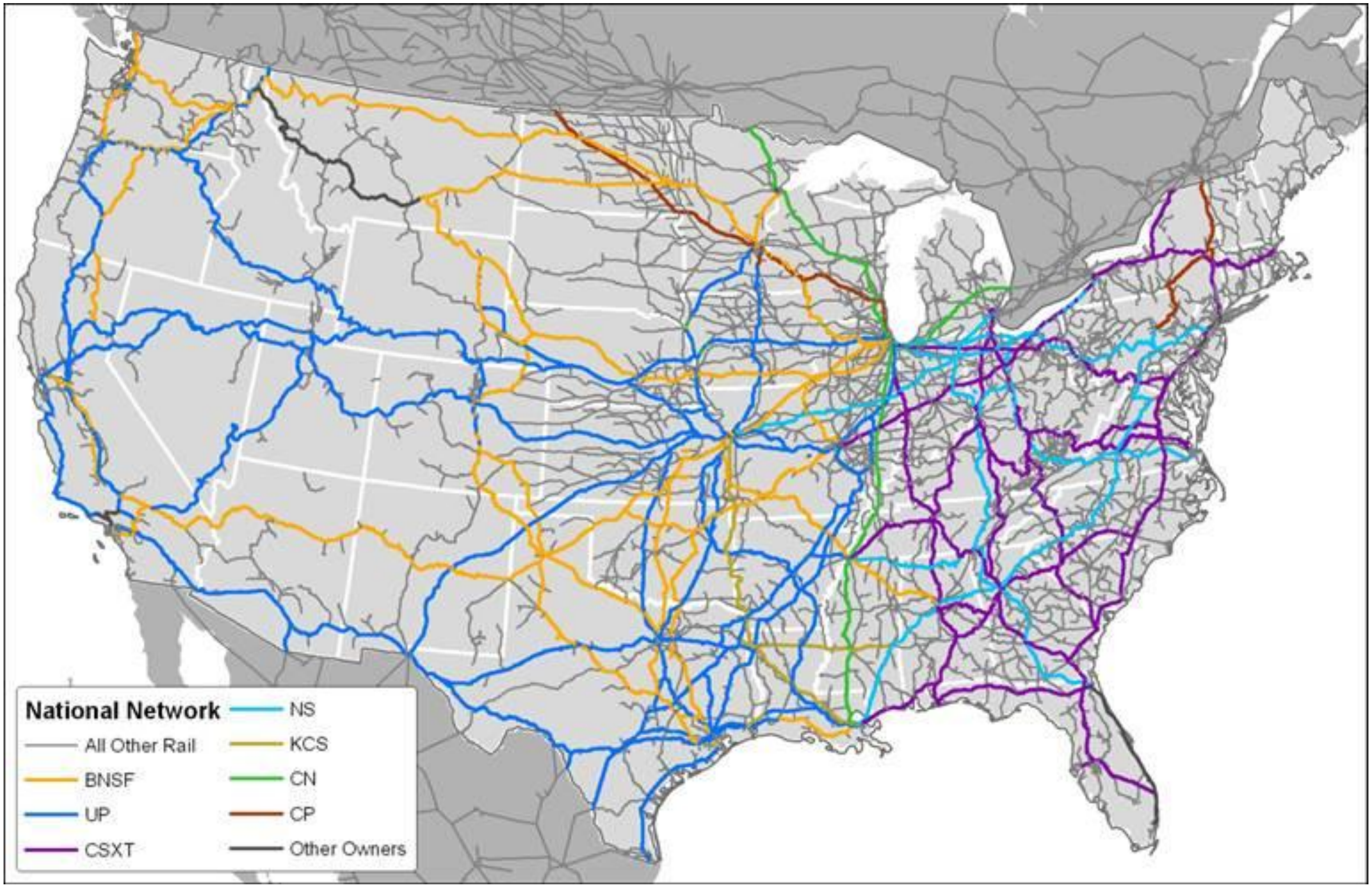
National Rail Capacity Study (2007)

- Requested by the National Surface Transportation Policy and Revenue Study Commission
- Commissioned by the Association of American Railroads
- Prepared by Cambridge Systematics, Inc.
- Study participants:
  - BNSF Railway
  - CSX
  - Norfolk Southern
  - Union Pacific
  - Association of American Railroads
  - American Shortline & Regional Railroad Association
- The full report can be accessed by going to the Association of American Railroads’ website at www.aar.org

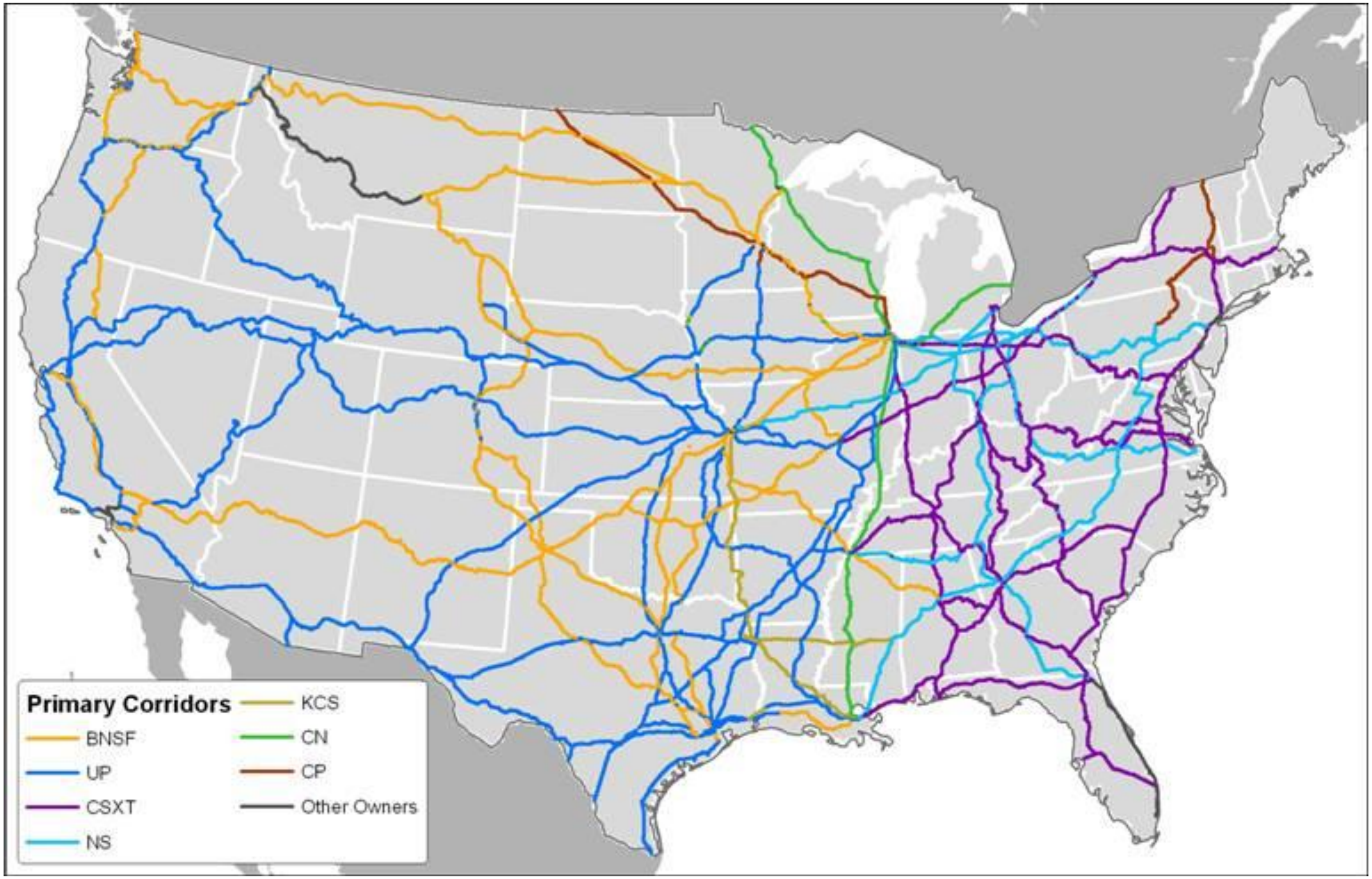
Purpose

- Estimate the rail freight infrastructure improvements and investments needed to meet the U.S. Department of Transportation's projected demand for rail freight transportation in 2035
  - The U.S. DOT estimated demand for rail freight transportation – measured in tonnage – will increase 88 percent by 2035

National Rail Freight Network and Primary Rail Freight Corridors

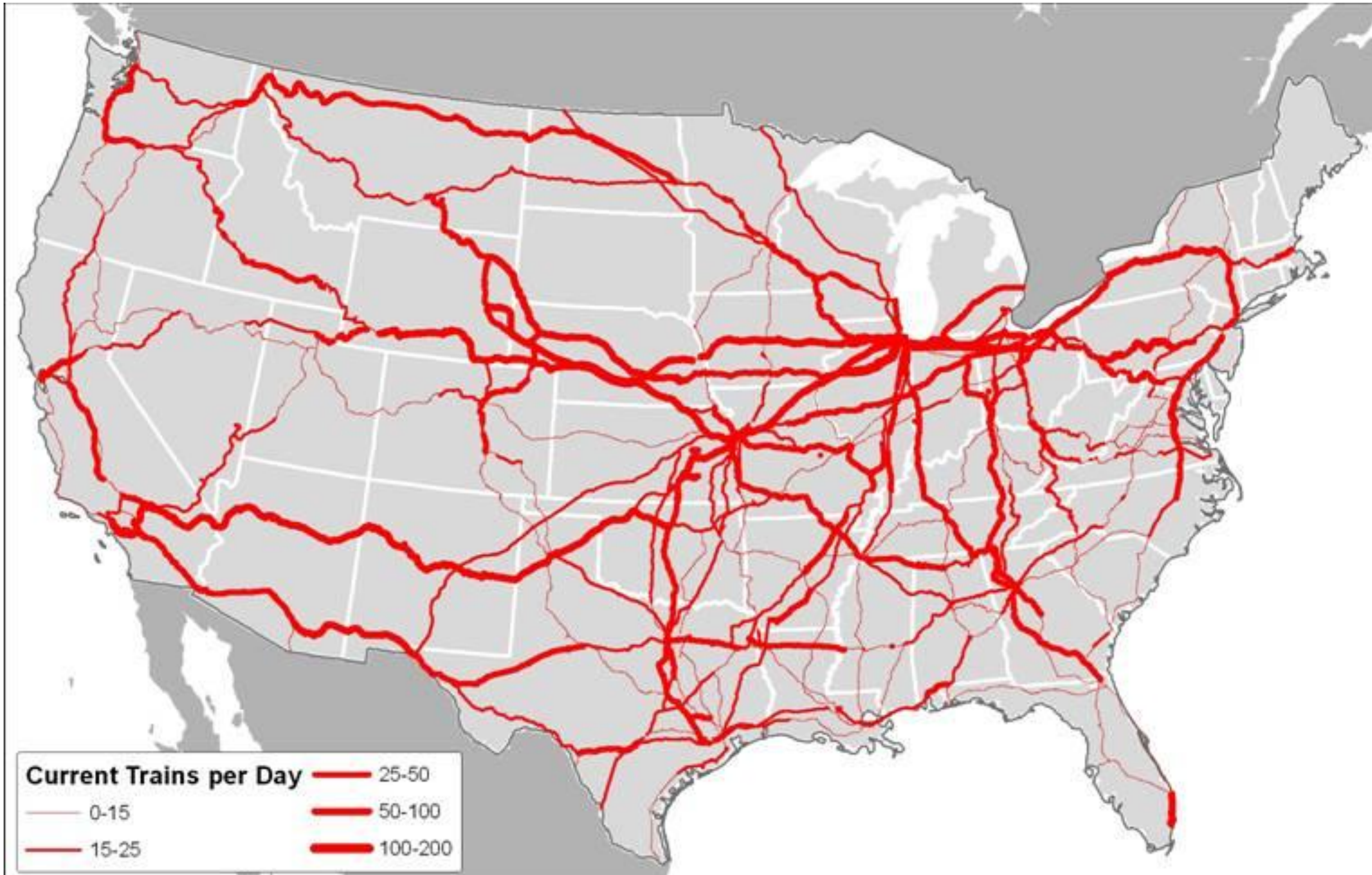


Primary Rail Freight Corridors



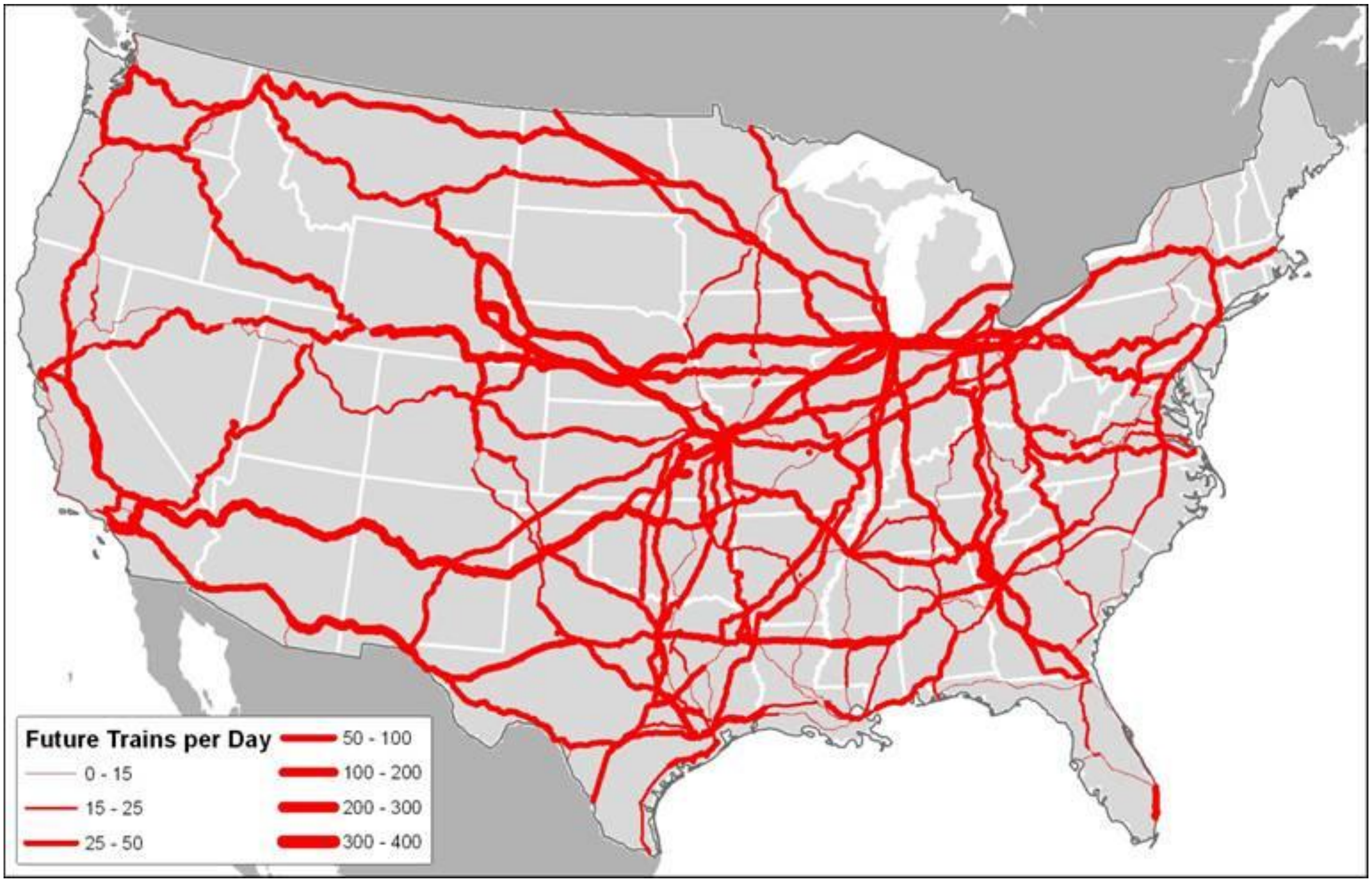
Current Primary Corridor Volumes

2005 Freight Trains and 2007 Passenger Trains per Day



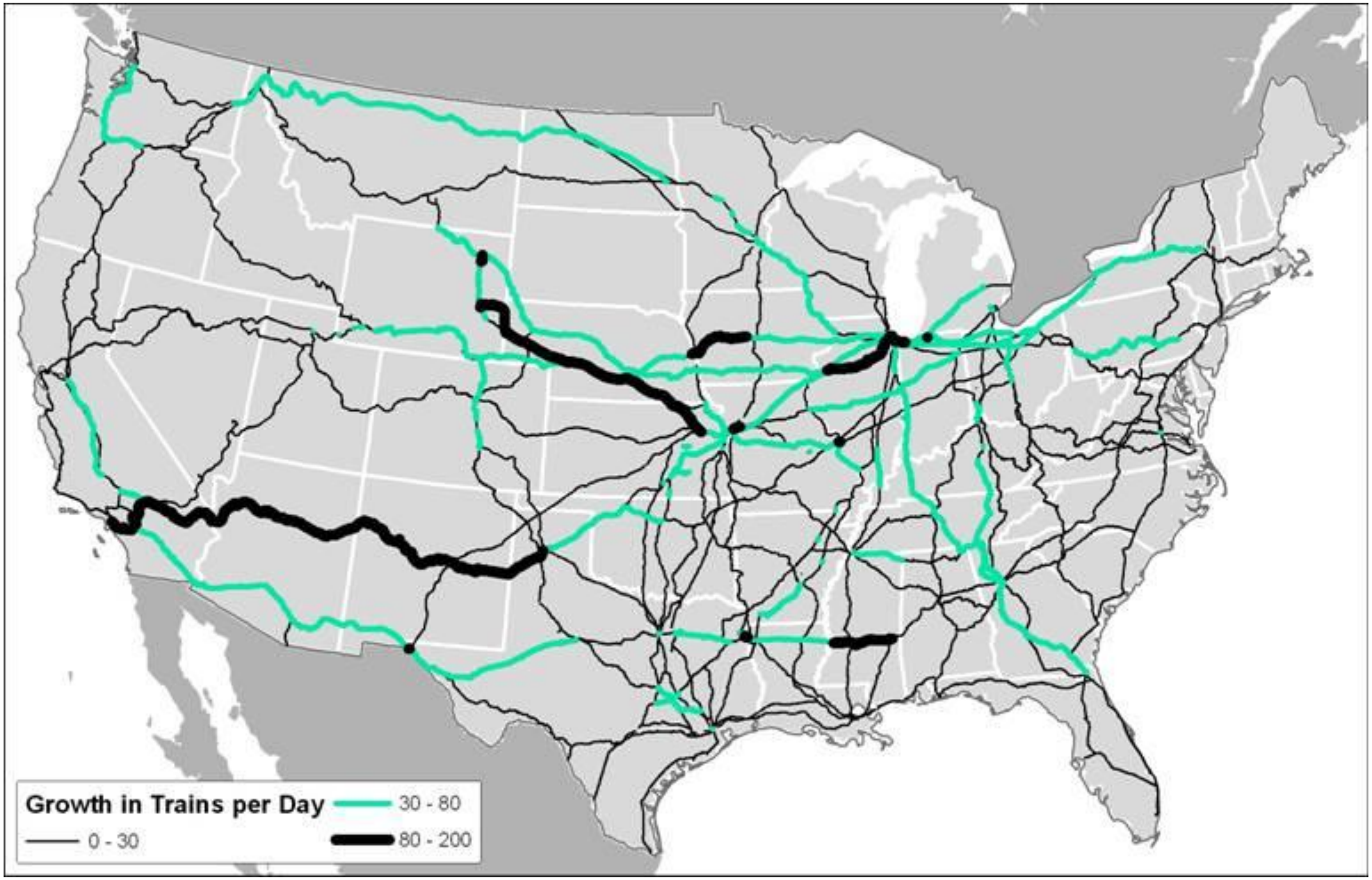
Future Corridor Volumes

2035 Freight Trains and 2007 Passenger Trains per Day



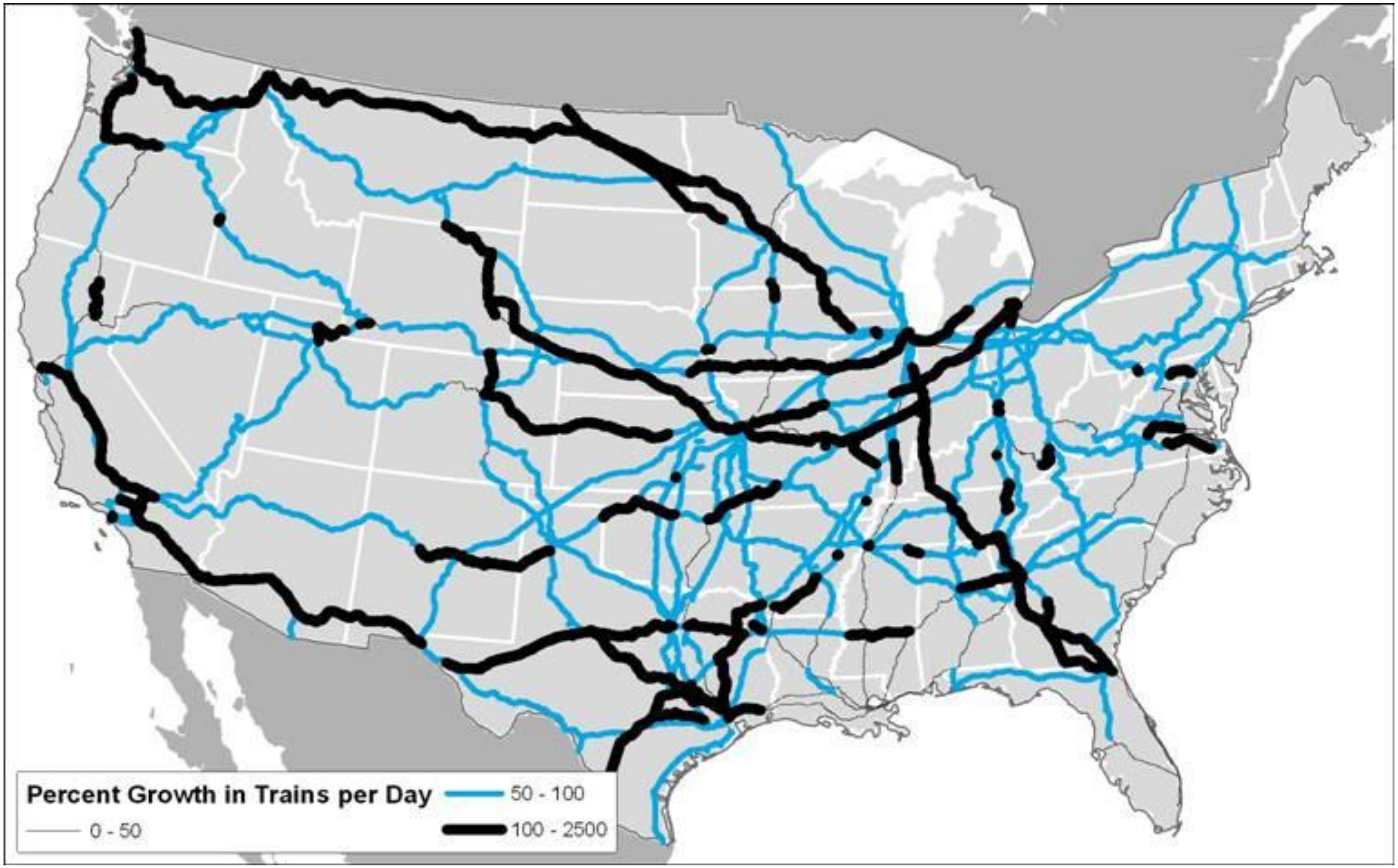
Growth in Number of Trains per Day

2005 to 2035

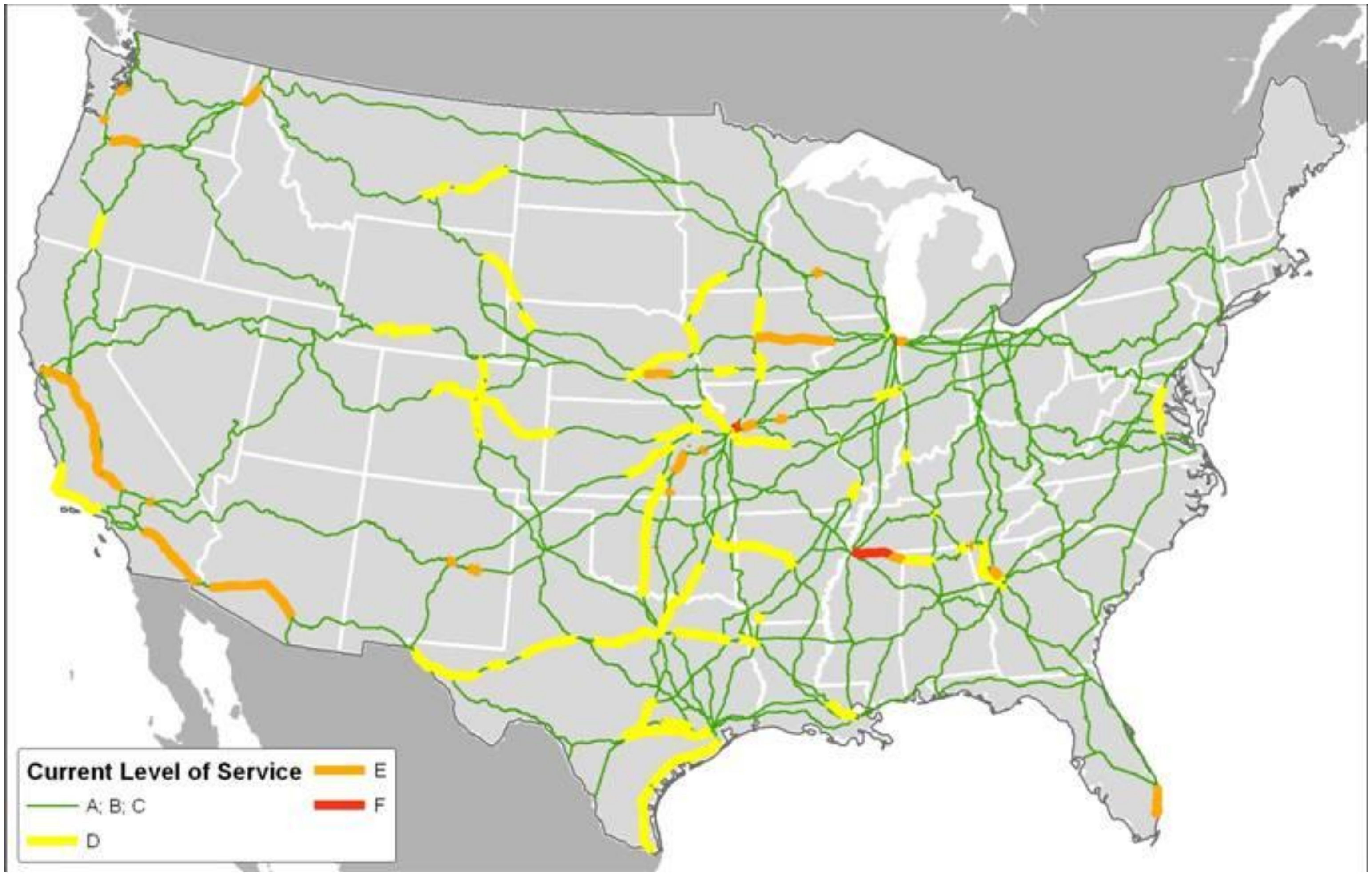


Percentage Growth in Trains per Day

2005 to 2035

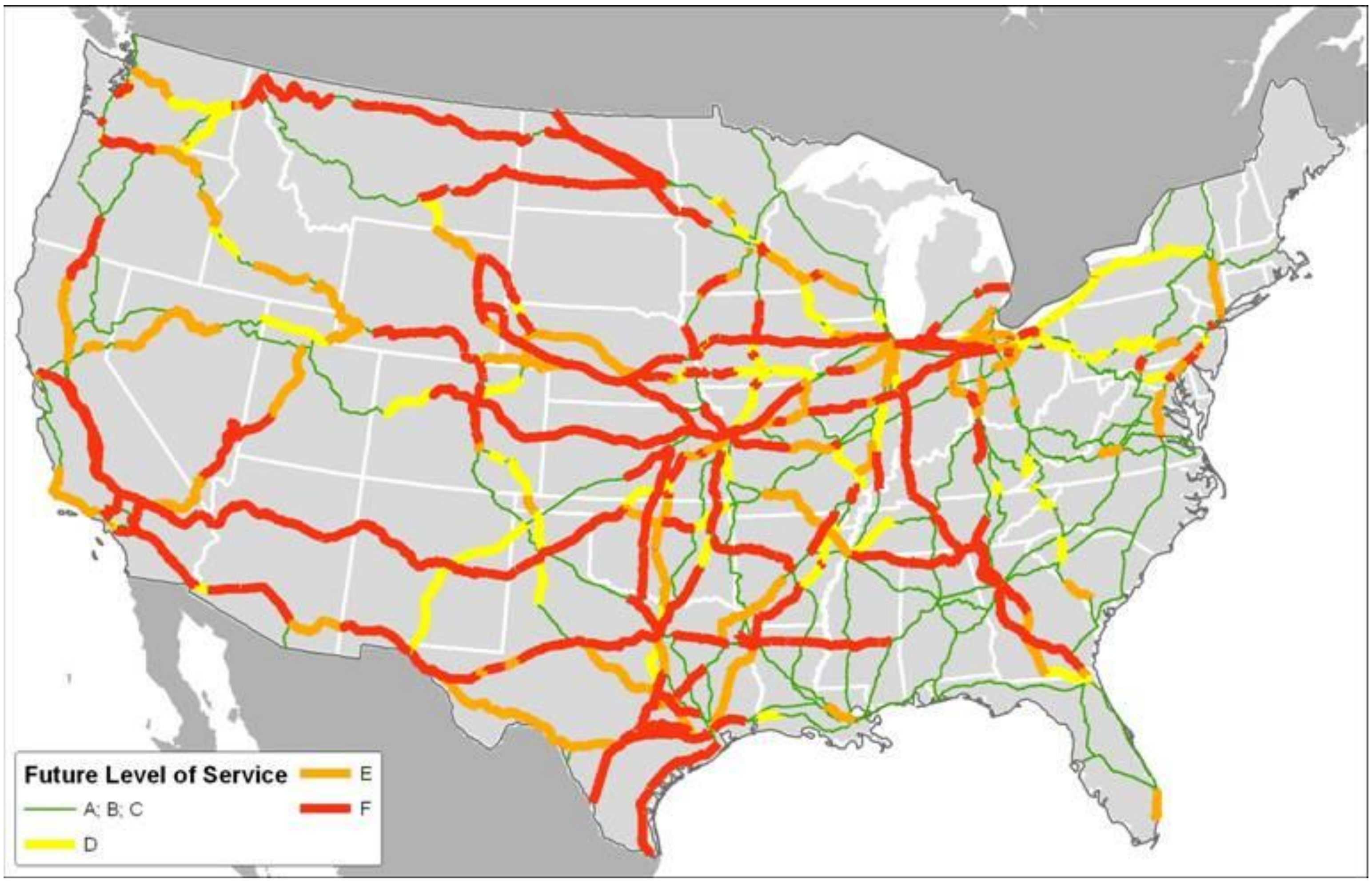


Current Train Volumes Compared to Current Train Capacity



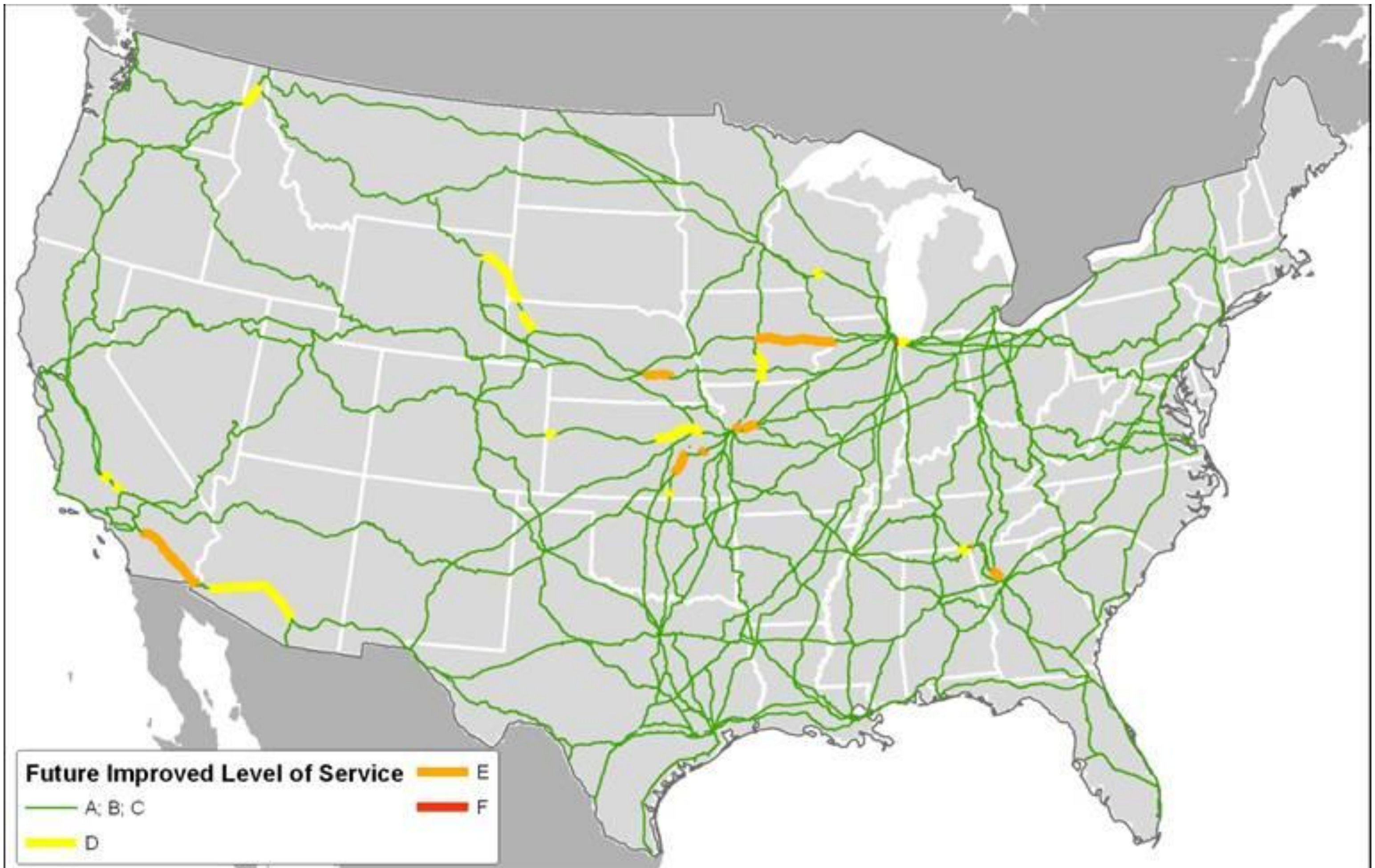
Future Corridor Volumes Compared to Current Corridor Capacity

2035 Without Improvements



Future Train Volumes Compared to Future Train Capacity

2035 With Improvements



Investment Needed

Infrastructure Improvement	Class I Freight Railroads	Short Line and Regional Freight Railroads	Totals
Line Haul Expansion	$94,750	$320	$95,070
Major Bridges, Tunnels, and Clearance Projects	$19,400	$5,000	$24,400
Branch Line Upgrades	$2,390	$7,230	$9,620
Intermodal Terminal Expansion	$9,320		$9,320
Carload Terminal Expansion	$6,620		$6,620
Service Facilities	$2,550		$2,550
Totals	$135,030	$12,550	$147,580

Key Findings

- $148 billion investment (in 2007 dollars) for infrastructure expansion over the next 28 years is required to keep pace with economic growth and meet the U.S. DOT's forecasted demand
  - Class I freight railroads' share is projected to be $135 billion
  - Short line and regional freight railroads' share is projected to be $13 billion
- Without this investment, 30 percent of the rail miles in the primary corridors will be operating above capacity by 2035, causing severe congestion that will affect every region of the country and potentially shift freight to an already heavily congested highway system

Key Findings (continued)

- The Class I railroads anticipate that they will be able to generate approximately $96 billion of their $135 billion share through increased earnings from revenue growth, higher volumes, and productivity improvements, while continuing to renew existing infrastructure and equipment
  - Requirement: Current regulatory policy remains in place
- This leaves a balance for the Class I freight railroads of $39 billion or about $1.4 billion per year to be funded from railroad investment tax incentives, public-private partnerships, or other sources
  - Example: Investment Tax Credit for new capacity

Closing Observations

- This is the first study of its kind to put a "price tag" on a 30 year look into the future for freight rail infrastructure needs
- Study needs updating based on changes since 2007
  - Recession and commodity shifts slowed growth . . .
  - Which has now resumed for the freight railroads
- The study demonstrates that public-private partnerships will be necessary in order for the public to realize the full benefits of freight rail
- The study underscores the impact of re-regulation in potentially restricting the railroads' ability to expand capacity at a time when it's most needed
- Any public policy which consumes present or future freight rail capacity or deters private investment from adding freight rail capacity should not be considered

BNSF Public Private Partnerships

- Projects combine BNSF business interests with diverse local, state and Federal goals
- Public sector/BNSF cooperation may allow both to achieve their respective goals better, faster, and at lower costs
- BNSF will consider PPPs that protect or enhance the ability of BNSF to provide safe, efficient freight transportation services while offering the public –
  - Improved livability
  - Economic development
  - Public affordability

BNSF Public Private Partnerships

- Factors BNSF considers in entering a PPP:
  - Understand project’s scope, goals, and possible effects on BNSF infrastructure, operations
    - No harm to present, future operations
  - Public funding sources, probability and timing of funding must be compatible with project’s goals
  - Public benefit reflected in public investment level
  - BNSF dependent on system capital demands, projects returns justifying investment

Federal Funding Programs

- Railroad Rehabilitation & Improvement Financing (RRIF)
- Congestion Mitigation & Air Quality Improvement Program (CMAQ)
- Surface Transportation Program (STP)
- Rail Line Relocation Grant Program
- Transportation Infrastructure Finance & Innovation Act (TIFIA)
- Private Activity Bonds
- Transportation Investment Generating Economic Recovery (Tiger) III:
  - $2.6 billion already provided in Tiger I, Tiger II
  - Additional $527 million announced July 5, 2011

Shortline Tax Credit

- On December 17, 2010, President Obama signed the Middle Class Tax Relief Act of 2010, extending short lines' Section 45G tax credit for tax years 2010 and 2011.
  - Originally enacted in 2004.
  - Tax credit had expired on December 31, 2009.
- Section 45G enables regionals and short lines to claim a tax credit of 50 cents for every dollar spent on infrastructure improvements, up to an annual cap of $3,500/mile of owned or leased track.
  - Efforts to extend into 2012 now underway.

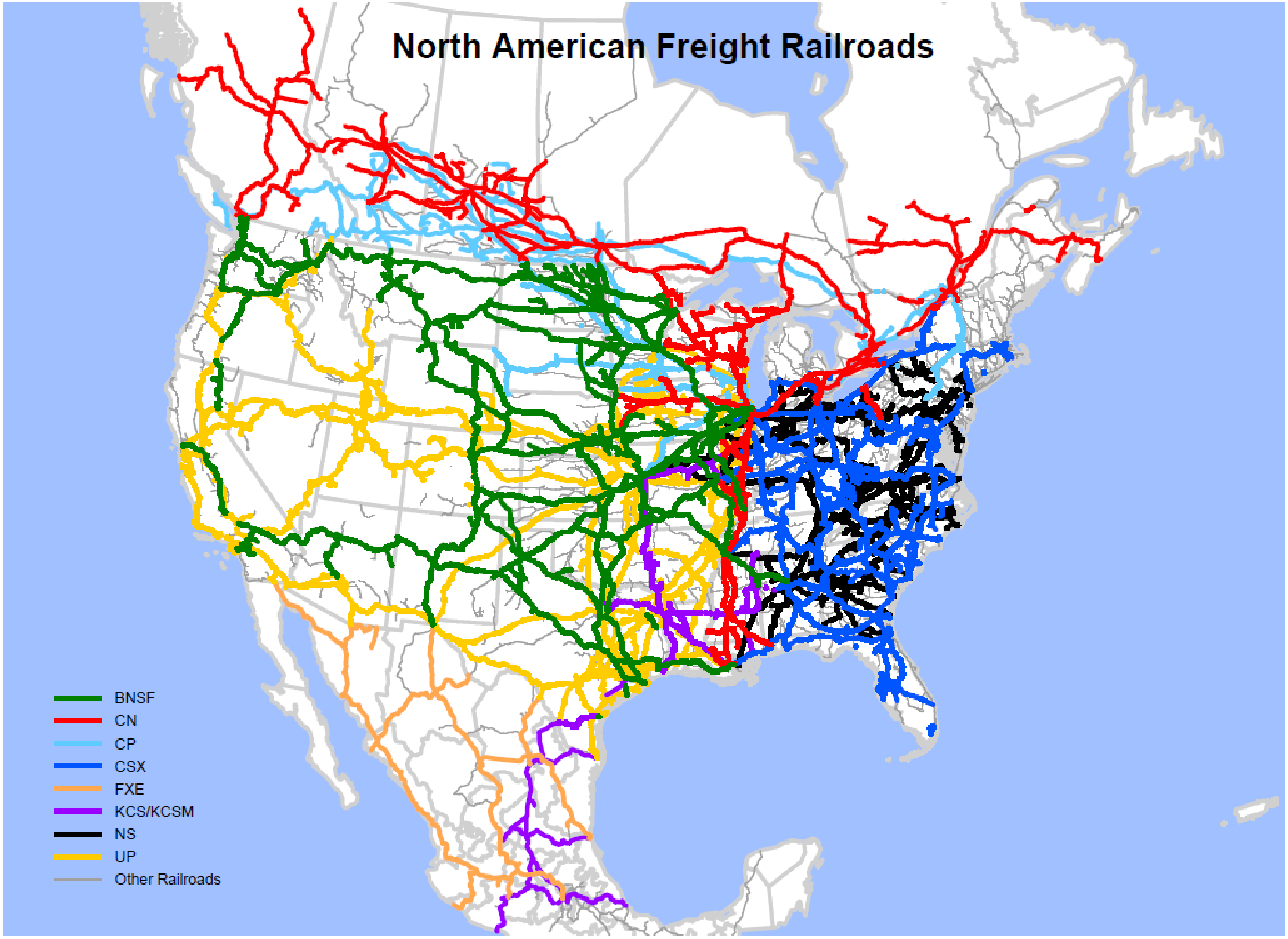
State Railroad Funding Programs

- Current programs
  - Florida
  - Idaho
  - Illinois
  - Iowa
  - Kansas
  - Maryland
  - Minnesota
  - New Jersey
  - New York
  - Ohio
  - Pennsylvania (?)
- Future anticipated programs: DE, KY, MS, MT, TN

Example Freight Rail PPPs

- Alameda Corridor (CA)
- Chicago Regional Environmental & Transportation Efficiency Program (CREATE)
- Tower 55 (TX)
- Heartland Corridor (NS, Hampton Roads, VA – Columbus, OH)
- Crescent Corridor (NS, Harrisburg, PA-Memphis, TN)
- National Corridor (CSX, Baltimore, MD-Chicago, IL)

Questions?


North American Freight Railroads
BNSF
CN
CP
CSX
FXE
KCS/KCSM
NS
UP
Other Railroads