

## Transportation - Railroads

# 4Q Review in Charts: Volume growth flips positive; Focus on UNP, CSX, and CPKC

Industry Overview

### Growth inflects positive; stay focused on UNP, CSX, CPKC

In 4Q23, Rail revenues declined 1% year-year, moderating from -10% in 3Q as volumes inflected up (+3% from -4% in 3Q23) and yield declines (average revenue/car) moderated to -2% from -5% in 3Q23. Peak season demand gains and easier comps supported the sequential improvement on a year-year basis. Operating Ratios improved 130 bps on avg from 3Q, vs normal seasonality of a 130 bps deterioration, on mild 4Q weather and positive earnings leverage. 3Q-4Q margin gains were led by CPKC (+300 bps), CNI (+260 bps), UNP (+240 bps), and NSC (+20 bps). Alternatively, BNSF and CSX declined 40 bps seq. as negative mix hit yields. We remain focused on Buy-rated UNP, CSX, and CP with service-related upside potential, which we expect will lead growth.

### Top pick UNP (w/ CEO Vena) widens margin gap to BNSF

At UNP, volumes were up 3% y-y, inflecting positive from -3% in 3Q23, yet below West Coast peer BNSF's +4% (from -5% in 3Q). BNSF was aided by a +7% y-y uptick in Consumer carloads (compared to UNP's 4% increase in Premium carloads). UNP's Revenue/Carload was down 3% y-y, moderating from -7% in 3Q23, outpacing BNSF's 7% decline, led by core pricing gains and positive mix. UNP has achieved significant margin and service gains after appointing Precision Scheduled Railroading expert Jim Vena as CEO in mid-August. Its freight car velocity has surged above 230 car miles/day in 4Q23, leading to margin gains. It posted a 60.9% Operating Ratio in 4Q23, 10 bps better year-year and a 710 bps positive gap to BNSF's 68.1% (widening from a 460 bps gap in 3Q23). We maintain our Buy on UNP as our top Rail pick, led by its idiosyncratic opportunity led by its network ops overhaul and service-led volume growth.

### CSX building momentum; sees service opportunities

At CSX, volumes were up 1% y-y (from -2% in 3Q) and yields were down 3% y-y (from -6% in 3Q) in 4Q23 given the negative impact of shorter haul mix. CSX expects low/mid-single digit carload/revenue growth in 2024 as momentum builds for Merchandise, Intermodal, and Coal carloads (we forecast +4% for both cars/revs) led by service-driven truck conversions and a new mine ramp up in West Virginia. We maintain our Buy on CSX as COO Mike Cory drives efficiency, which should support continued volume growth above peers and core pricing gains.

### CPKC gaining share; CNI negatively impacted by macro

At CPKC, carloads and yields were both up 2% y-y (from -5% and +2% in 3Q) as longer-haul traffic and share gain accelerated growth. It targets double digit 2024 EPS growth (we are +12%) on low single digit RTM gains (we forecast +2%). At CNI, carloads were down 1% y-y (from -10% in 3Q) and yields declined 1% y-y (from -3% in 3Q). CNI was the only Class 1 rail to post a volume decline in 4Q despite improved demand as lower Grain volumes offset a recovery in Intermodal. It targets 10% 2024 EPS growth (we forecast +10%) on mid-single digits RTM growth with a 2H ramp, which we note it has not achieved since 2018. We maintain our Buy on CPKC shares on its post-merger synergy gains yet stay Neutral on CNI's shares as we think macro pressures/grain crop may offset its service gains.

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#### Exhibit 1: Stocks mentioned

Shares mentioned include CNI, CP, CSX, UNP.

	RTNG	PRICE	PO	P/E	TGT P/E
CNI	N	\$131.21	\$131	22.2x	22.0x
CP	B	\$86.07	\$87	27.0x	27.0x
CSX	B	\$38.08	\$39	19.0x	19.5x
UNP	B	\$254.82	\$274	22.7x	24.5x

**Source:** BofA Global Research estimates and Bloomberg.  
N: Neutral, B: Buy.

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#### Abbreviations

BNSF: Burlington Northern Santa Fe

CNI: Canadian National Railway

CPKC: Canadian Pacific Kansas City

CSX: CSX Ltd.

NSC: Norfolk Southern Corp  
(Restricted)

UNP: Union Pacific

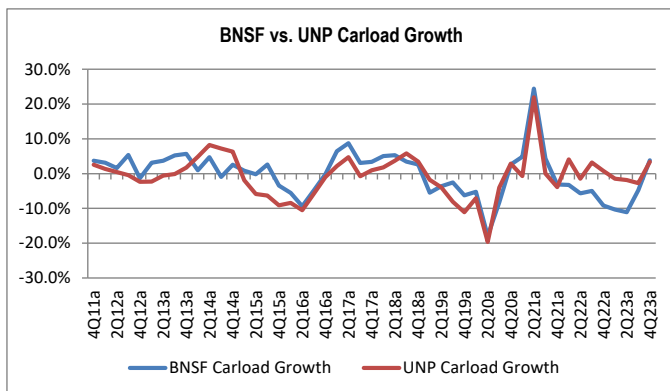
TE&amp;Y: Train, Engine &amp; Yard

PSR: Precision Scheduled Railroading

RTM: Revenue Ton Mile

**Exhibit 2: BNSF vs UNP Carload Growth**

BNSF carloads are up 4% year-year vs UNP up 3% year-year in 4Q23.

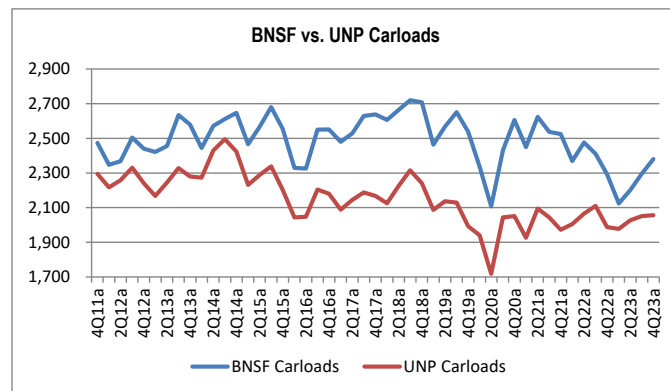


Source: Company reports

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**Exhibit 3: BNSF vs UNP Rail Carloads**

BNSF 4Q carloads were 2.4 mil vs UNP at 2.1 mil, 325k higher (vs 244k 3Q)

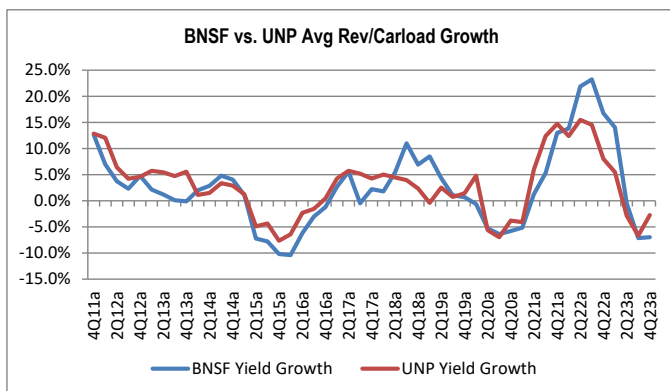


Source: Company reports

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**Exhibit 4: BNSF vs UNP Revenue/Carload Growth**

BNSF 4Q23 rev/carload are down -7% y-y, worse than UNP's -3% y-y.

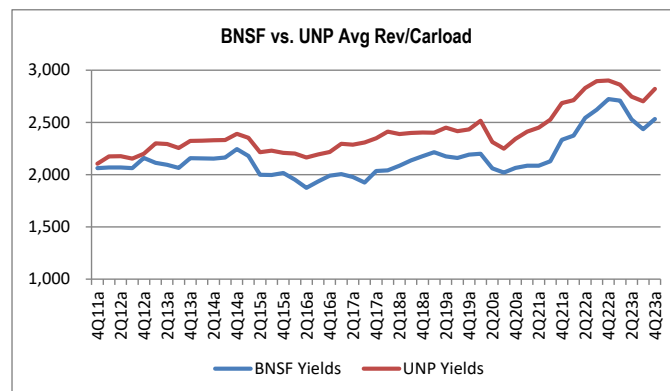


Source: Company reports

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**Exhibit 5: BNSF vs UNP Revenue per Carload**

BNSF 3Q23 revenue/carload was \$2,534/car vs UNP at \$2,821/car

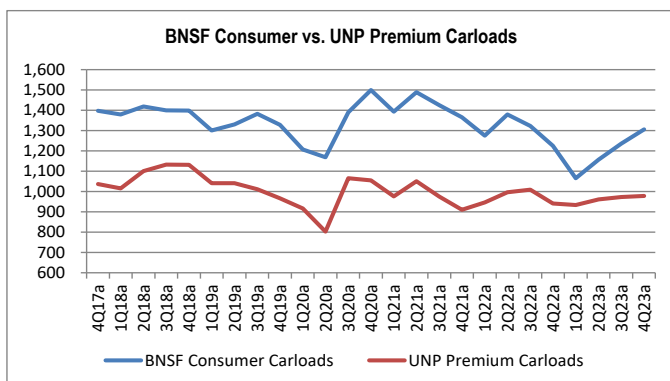


Source: Company reports

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**Exhibit 6: BNSF Consumer vs UNP Premium Carloads**

BNSF Consumer carloads +7% y-y, above UNP's +4% Premium growth

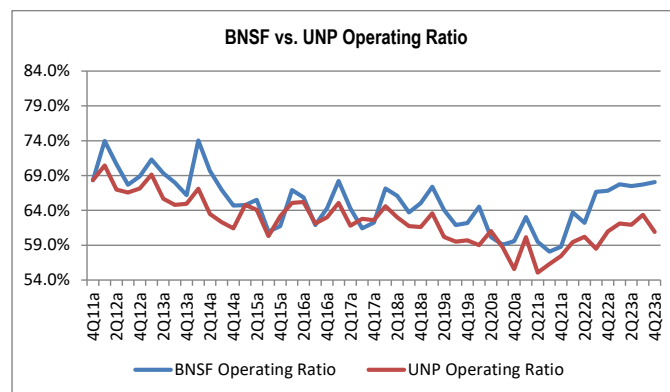


Source: Company reports

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**Exhibit 7: BNSF vs UNP Operating Ratio**

BNSF operating ratio deteriorated 130 bps y-y vs UNP 10 bps improvement.

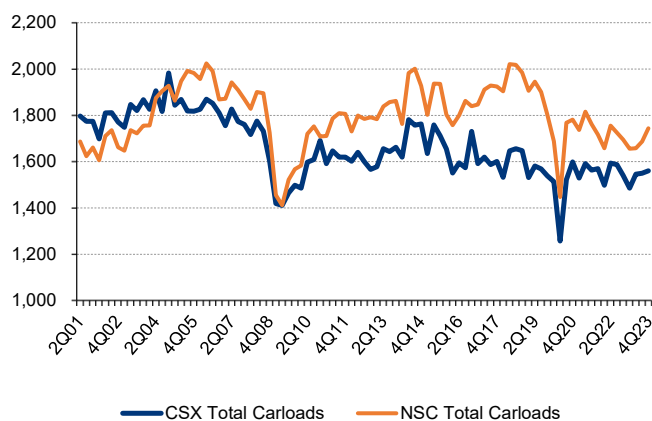


Source: Company reports

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**Exhibit 8: CSX vs NSC Carloads**

NSC Carloads were 1.7 mil in 4Q23, 180,00 carloads above CSX's 1.5 mil.

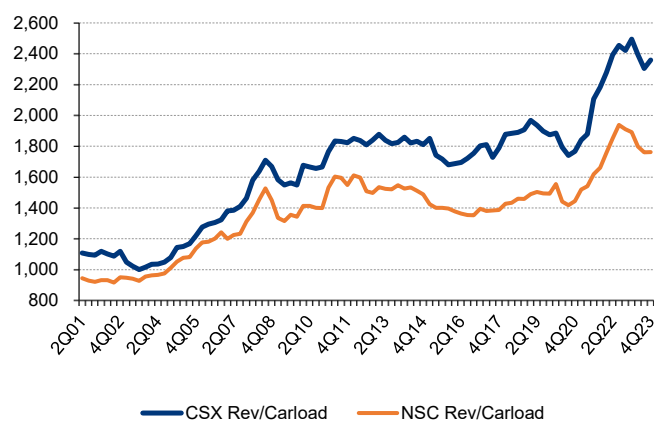


Source: Company reports

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**Exhibit 9: CSX vs NSC Average Revenue/Carload**

NSC Revenue/Carload was \$1,762 in 4Q23, below CSX's \$2,359.

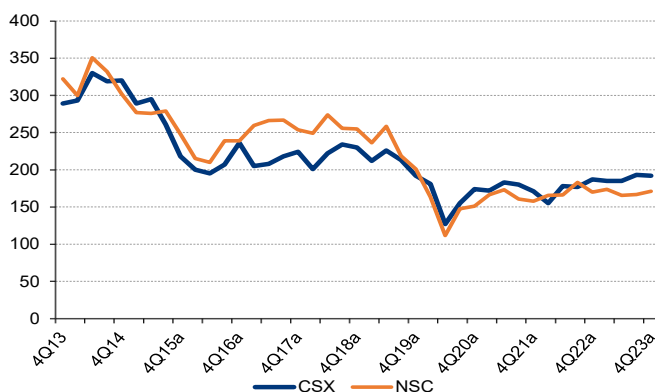


Source: Company reports

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**Exhibit 10: CSX vs NSC Coal Carloads**

NSC moved 171k Coal carloads in 4Q23, below CSX's 192k moved.

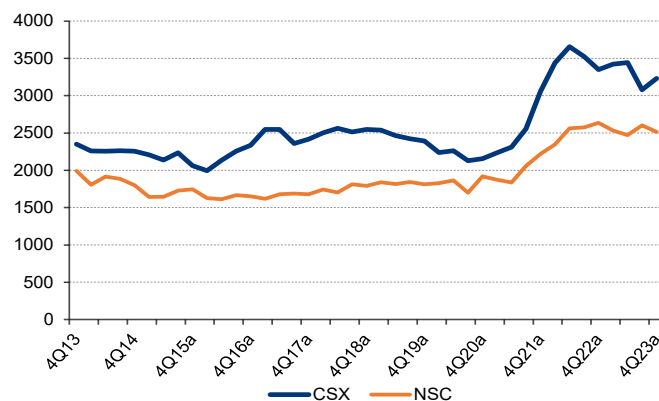


Source: Company reports

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**Exhibit 11: CSX vs NSC Revenue per Coal Carload**

NSC average Revenue/Coal Carload is \$2,515 in 4Q23, below CSX's \$3,229.

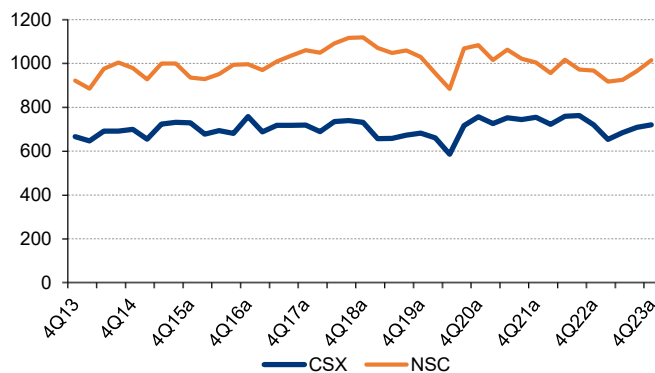


Source: Company reports

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**Exhibit 12: CSX vs NSC Intermodal Carloads**

NSC moved 1,015k Intermodal carloads in 4Q23, above CSX's 720k.

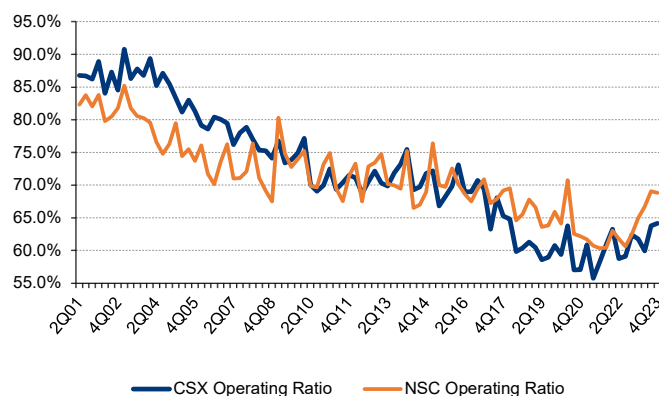


Source: Company reports

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**Exhibit 13: CSX vs NSC Operating Ratio**

NSC's Op Ratio was 68.8% in 4Q23, 470 bps above than CSX's 64.1%.

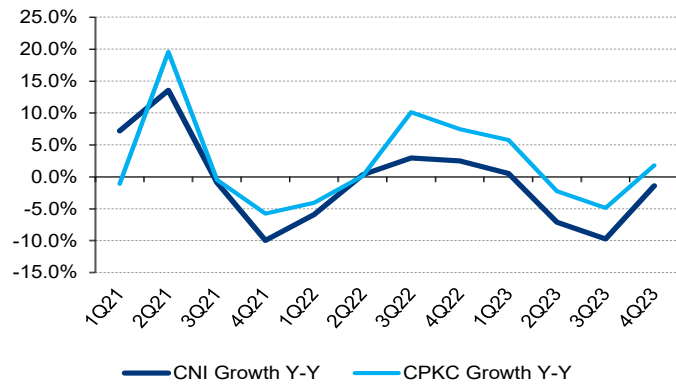


Source: Company reports

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**Exhibit 14: CNI vs CP Carload Growth**

CPKC carloads increased 1.8% year-year in 4Q23, above CNI's -1.4%.

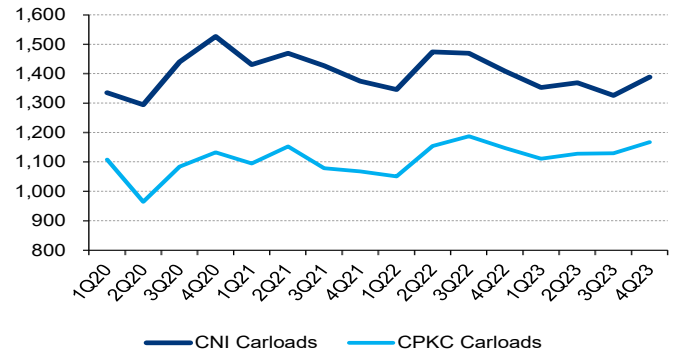


Source: Company reports

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**Exhibit 15: CNI vs CP Rail Carloads**

CPKC's 1.2 million carloads compares to CNI's 1.4 million in 4Q23.

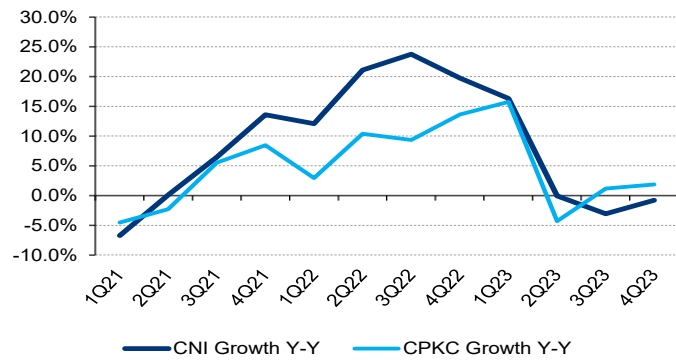


Source: Company reports

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**Exhibit 16: CNI vs CP Revenue/Carload Growth**

CPKC's Revs/Carload increased 1.9% year-year in 4Q23, above CNI's -0.8%.

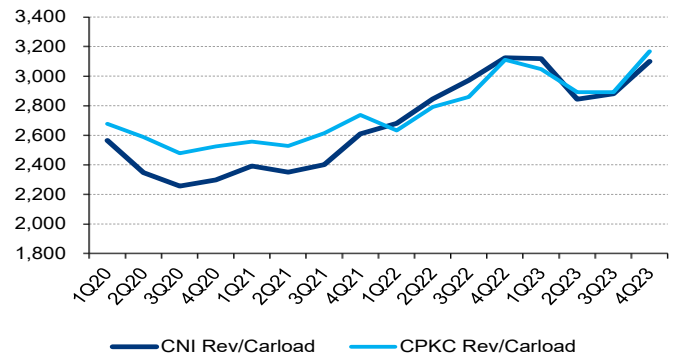


Source: Company reports

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**Exhibit 17: CNI vs CP Revenue per Carload**

CPKC's revenue/carload of C\$3,168, above CNI's C\$3,100 in 4Q23.

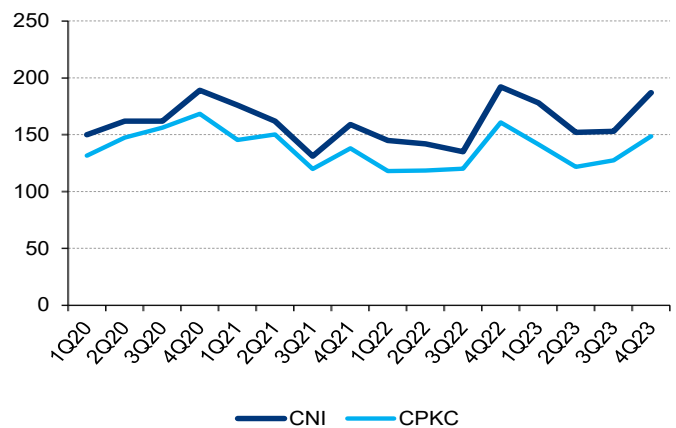


Source: Company reports

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**Exhibit 18: CNI vs CP Grain Carloads**

CPKC's 149k Grain carloads compares to CNI's 187k in 4Q23.

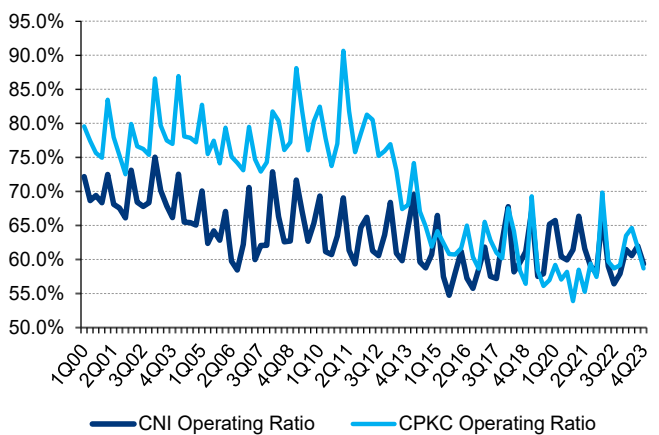


Source: Company reports

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**Exhibit 19: CNI vs CP Operating Ratio**

CPKC's 58.7% adj Operating Ratio compares to CNI's 59.3% in 4Q23.



Source: Company reports

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**Exhibit 20: Class I Rail Carrier Carload Growth**

Carloads were up 2% year-year in 4Q23, inflecting from -4% in 3Q23.

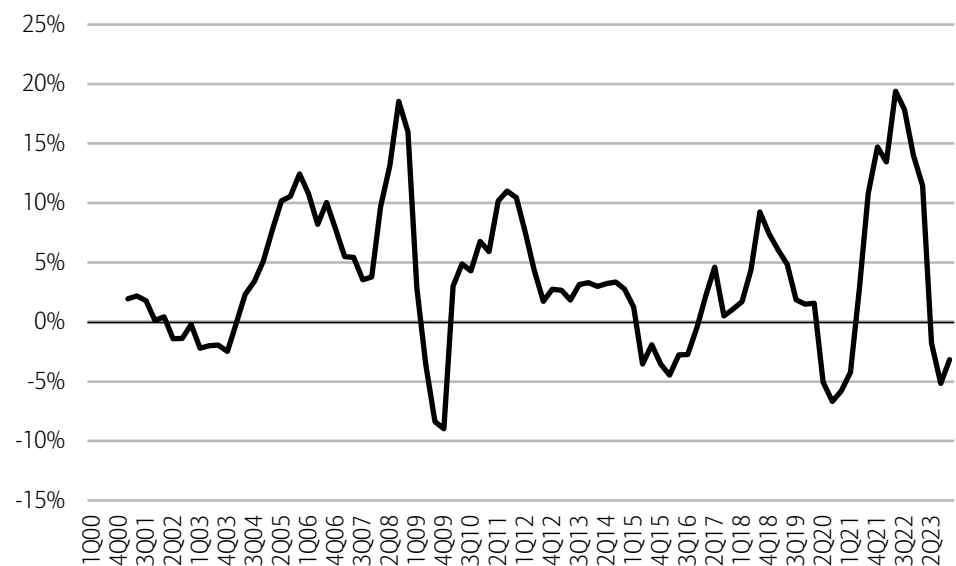


Source: Company reports

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**Exhibit 21: Class I Rail Average Revenue per Carload**

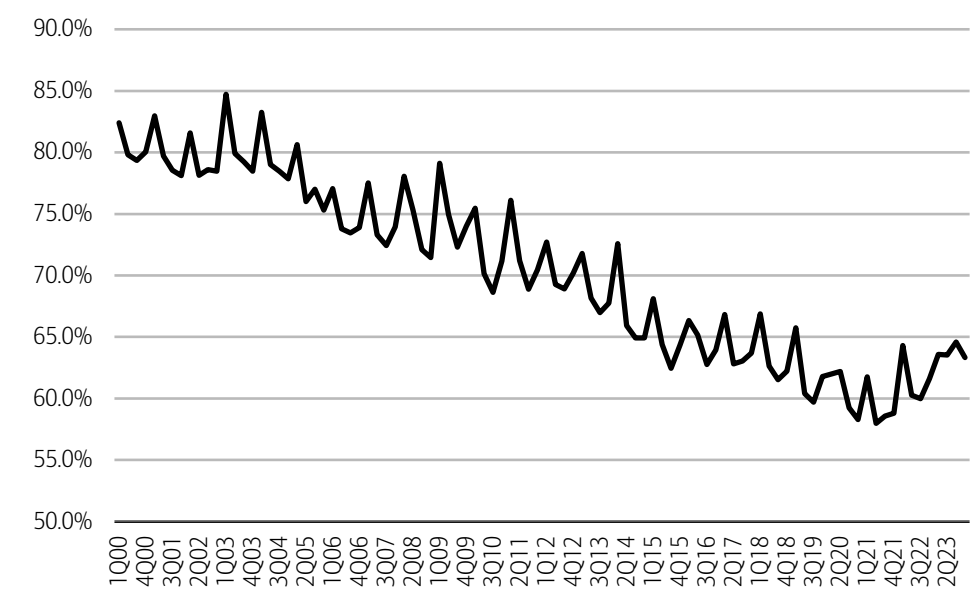
Revenues per rail carload are down 3% in 4Q23, moderating from -5% in 3Q23.



Source: Company reports

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**Exhibit 22: Class I Rail Operating Ratio**  
Operating ratios deteriorated 170 bps year-year yet improved 130 bps sequentially on average.



Source: Company reports

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**Table 1: Stocks mentioned**

Prices and ratings for stocks mentioned in this report

BofA Ticker	Bloomberg ticker	Company name	Price	Rating
CNI	CNI US	Canadian Natl	US\$ 131.21	B-2-7
CP	CP US	Canadian Pacific	US\$ 86.07	B-1-7
CSX	CSX US	CSX Corporation	US\$ 38.08	B-1-7
UNP	UNP US	Union Pacific	US\$ 254.82	B-1-7

Source: BofA Global Research

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## Price objective basis & risk

### Canadian National (CNI)

Our US\$131 price objective is based on a 22x multiple on our 2024 US\$ EPS estimate, above the midpoint its 5-year 18x-23x one standard deviation trading range (above the top of its 13.5x-20x 20-year historical trading range), a premium to peer average given its service yet near market value of shares.

Downside risks to our price objective and estimates are slower-than-expected economic growth, higher-than-historical-average costs (including fuel) and those costs outpacing surcharges, potential disruptions from a highly unionized (79%) labor force, volume or pricing softness, regulatory changes, a surge in the Canadian dollar relative to the U.S. dollar, and external factors (such as weather) impacting operations. Disruptive rail re-regulation that limits the company's ability to earn proper returns on its investments would also be a downside risk. Additionally, CP continues to improve ops which could cause an increase in price competition.

Upside risk to our price objective would be stronger than expected acceleration in carload volumes, a larger than expected Canadian grain harvest season, an uptick in macro demand, and greater than anticipated cost reductions through CN's service gains.

### Canadian Pacific Kansas City Ltd (CP)

Our US\$87 objective is based on a 27x target multiple on our US\$ 2024 EPS estimate (which includes synergies from its KCS acquisition), above its 13x-20x historical band. Our '24 estimate remains somewhat depressed, as it works to rebound with initial synergies post KCS acquisition, as well as benefit from a rebounding economy. Our target PE is above the rail average, reflecting the strength of CP's management and its network, as well as potential upside from its KCS acquisition.

CP consistently demonstrates its ability to manage costs in a rapidly declining & rising volume environment, highlighting its operating model and one of the best management teams in the industry, led by CEO Keith Creel. We see upside to estimates from synergies with its KCS acquisition.

Risks to our PO are slower-than-expected economic growth, higher-than-expected pension expense/cash contribution requirements, high fuel costs (CP's exposure to crack spreads), potential disruptions from a highly unionized (79%) labor force, volume or pricing softness, regulatory changes (such as retroactive grain rate changes), change in the Canadian dollar beyond targets, external factors (such as weather) impacting operations, as well as Mexico concession network ownership/renewal risk. Disruptive rail re-regulation that limits the company's ability to earn proper returns on its investments, and inability to fully merge with KCS.

### CSX Corporation (CSX)

Our \$39 price objective is based on a 19.5x target multiple on our 2024 EPS estimate, just above the top of the company's 12x-18x historical range, given its move above



trough earnings and potential for rebounding ops and top line growth. CEO Joe Hinrichs, previously head of Ford's global auto business, aims to balance improving service with top line growth, as part of ONE CSX. It continues to absorb impacts from its acquisition of Pan Am Rail, Quality Distribution, and declining fuel surcharges. It has topped its target to hire Train & Engine employees as it restores its service levels.

Risks to our price objective are operational issues, a return to significant pricing competition among the rails, slower-than-expected economic growth, a deterioration in service metrics, any work stoppages or impacts from its unionized employee base, inability to exercise pricing power due to regulatory changes or legal challenges from customers, external factors (such as weather) impacting operations, additional regulations for the rails, or ones that impact customers, such as expediting shutdown of coal generating facilities, and low nat gas prices that push continued coal to Nat Gas switching.

### **Union Pacific (UNP)**

Our \$274 price objective is based on a 24.5x multiple on our 2024 EPS estimate, as we are above the top of its 14x-20x historical range given the rapidly improving service gains under new CEO Jim Vena. We believe 2024 earnings will rebound from 2023's trough, particularly aided by the operational and cultural turnaround launched by Mr. Vena. The company should significantly improve its earnings outlook, drive improved cash flow, and return to buybacks in 2024. We target leverage to remain between 2.8x-3.0x, and look for it to re-engage in top-line growth, drive improved returns and cash flow.

Risks to our price objective are a more muted economic recovery, accelerating coal volume declines, muted winter weather leading utilities to build coal inventories, increased pricing competition neutralizing the benefits from the pricing currently enjoyed by the rail industry, higher than expected fuel prices, employee/union strikes, inability to exercise pricing power due to regulatory changes or legal challenges from customers, disruptive rail re-regulation that limits the company's ability to earn proper returns on its investments or mandates open access with unfavorable terms, risk from the Canadian Pacific (CP)-Kansas City Southern (KSU) merger absorbing Mexico vols, or harsh weather that disrupts operations beyond normal. Additionally, aggressive moves by in-region peer BNSF to take share, or if UNP's service metrics cannot improve, it could see sustained higher costs.

## **Analyst Certification**

I, Ken Hoexter, hereby certify that the views expressed in this research report accurately reflect my personal views about the subject securities and issuers. I also certify that no part of my compensation was, is, or will be, directly or indirectly, related to the specific recommendations or view expressed in this research report.

## **Special Disclosures**

BofA Securities is currently acting as Financial Advisor on potential Activism Defense assignment to Norfolk Southern Corp (NSC).



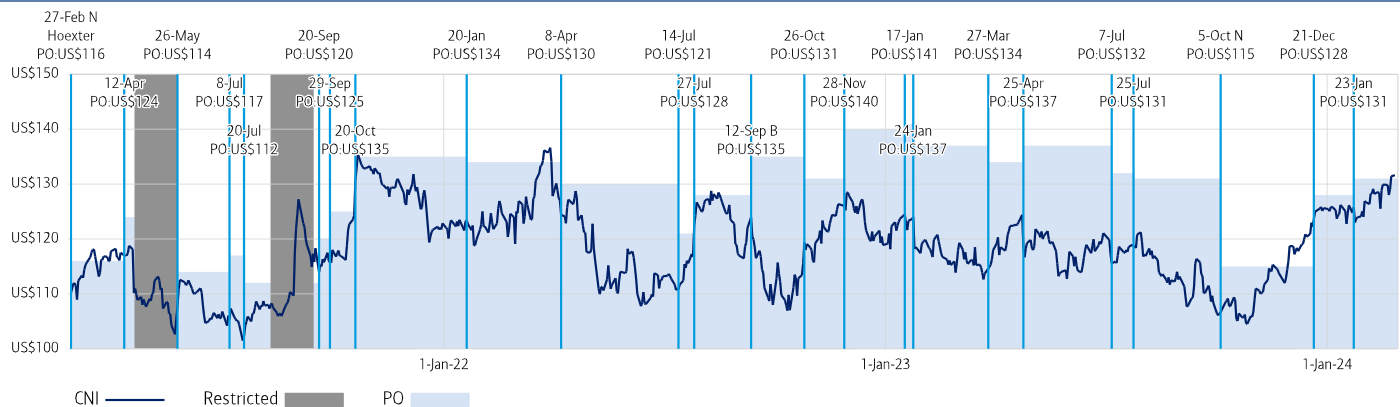
## US - Transportation Coverage Cluster

Investment rating	Company	BofA Ticker	Bloomberg symbol	Analyst
<b>BUY</b>				
	Canadian Pacific Kansas City Ltd	CP	CP US	Ken Hoexter
	CSX Corporation	CSX	CSX US	Ken Hoexter
	FedEx Corp.	FDX	FDX US	Ken Hoexter
	J.B. Hunt Transport Services	JBHT	JBHT US	Ken Hoexter
	Kirby Corp	KEX	KEX US	Ken Hoexter
	Knight-Swift Transportation Holdings Inc	KNX	KNX US	Ken Hoexter
	Old Dominion Freight Line	ODFL	ODFL US	Ken Hoexter
	Saia Inc.	SAIA	SAIA US	Ken Hoexter
	Teekay Tankers Limited	TNK	TNK US	Ken Hoexter
	Union Pacific	UNP	UNP US	Ken Hoexter
	Wabtec Corp.	WAB	WAB US	Ken Hoexter
	XPO, Inc.	XPO	XPO US	Ken Hoexter
<b>NEUTRAL</b>				
	Canadian National	CNI	CNI US	Ken Hoexter
	RXO, Inc.	RXO	RXO US	Ken Hoexter
	Schneider National	SNDR	SNDR US	Ken Hoexter
	Scorpio Tankers Inc.	STNG	STNG US	Ken Hoexter
	TFI International	TFII	TFII US	Ken Hoexter
	TFI International	YTFII	TFII CN	Ken Hoexter
	UPS	UPS	UPS US	Ken Hoexter
<b>UNDERPERFORM</b>				
	ArcBest Corporation	ARCB	ARCB US	Ken Hoexter
	C.H. Robinson	CHRW	CHRW US	Ken Hoexter
	The Greenbrier Companies	GBX	GBX US	Ken Hoexter
	Werner Enterprises	WERN	WERN US	Ken Hoexter
	World Kinect	WKC	WKC US	Ken Hoexter
<b>RSTR</b>				
	Norfolk Southern	NSC	NSC US	Ken Hoexter

## Disclosures

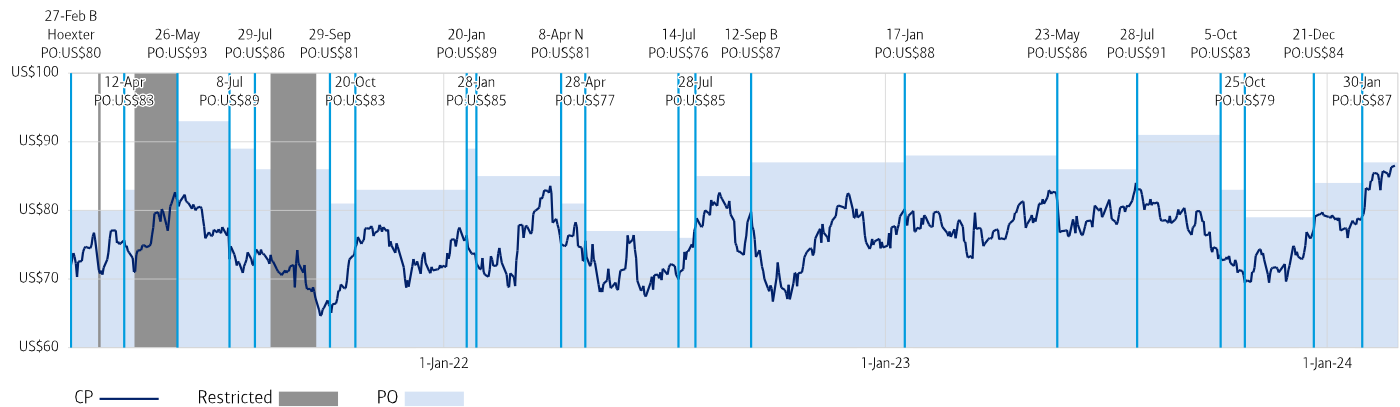
## Important Disclosures

## Canadian Natl (CNI) Price Chart



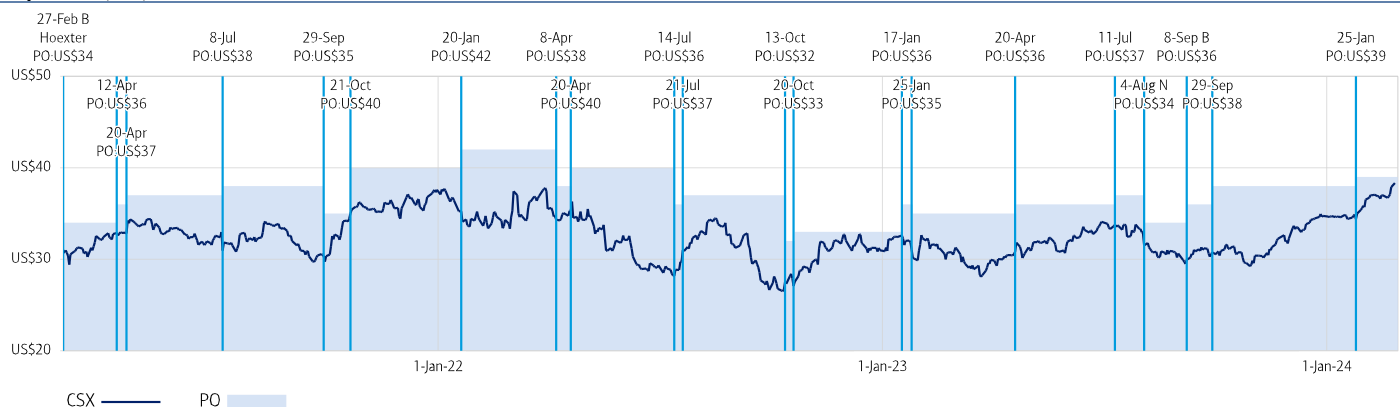
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

**Canadian Pacific (CP) Price Chart**

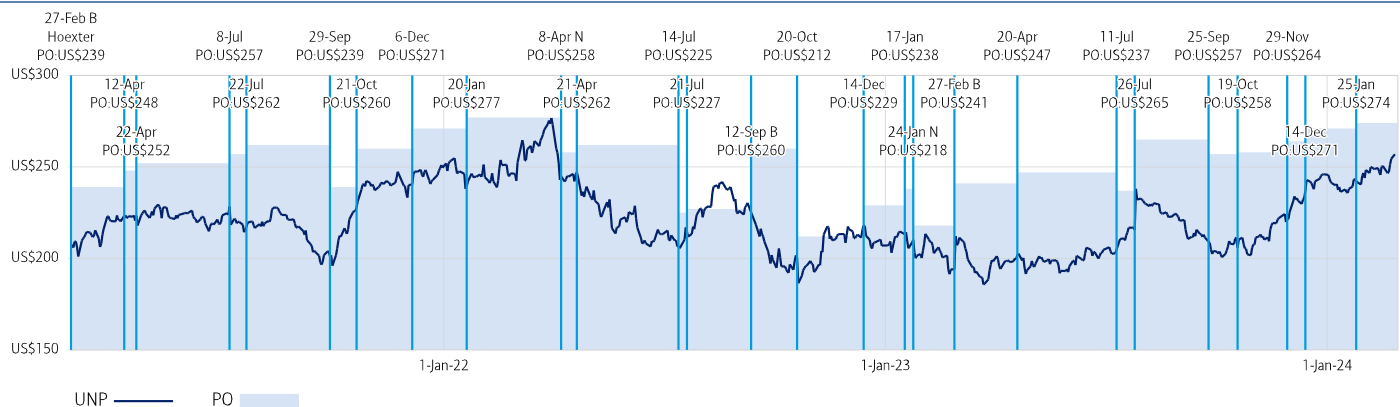
B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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**CSX Corporation (CSX) Price Chart**

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

**Union Pacific (UNP) Price Chart**

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

The Investment Opinion System is contained at the end of the report under the heading "Fundamental Equity Opinion Key". Dark grey shading indicates the security is restricted with the opinion suspended. Medium grey shading indicates the security is under review with the opinion withdrawn. Light grey shading indicates the security is not covered. Chart is current as of a date no more than one trading day prior to the date of the report.

**Equity Investment Rating Distribution: Transport/Infrastructure Group (as of 31 Dec 2023)**

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	67	50.38%	Buy	44	65.67%
Hold	31	23.31%	Hold	13	41.94%
Sell	35	26.32%	Sell	17	48.57%

**Equity Investment Rating Distribution: Global Group (as of 31 Dec 2023)**

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

<sup>R1</sup> Issuers that were investment banking clients of BofA Securities or one of its affiliates within the past 12 months. For purposes of this Investment Rating Distribution, the coverage universe includes only stocks. A stock rated Neutral is included as a Hold, and a stock rated Underperform is included as a Sell.

**FUNDAMENTAL EQUITY OPINION KEY:** Opinions include a Volatility Risk Rating, an Investment Rating and an Income Rating. **VOLATILITY RISK RATINGS**, indicators of potential price fluctuation, are: A - Low, B - Medium and C - High. **INVESTMENT RATINGS** reflect the analyst's assessment of both a stock's absolute total return potential as well as its attractiveness for investment relative to other stocks within its Coverage Cluster (defined below). Our investment ratings are: 1 - Buy stocks are expected to have a total return of at least 10% and are the most attractive stocks in the coverage cluster; 2 - Neutral stocks are expected to remain flat or increase in value and are less attractive than Buy rated stocks and 3 - Underperform stocks are the least attractive stocks in a coverage cluster. An investment rating of 6 (No Rating) indicates that a stock is no longer trading on the basis of fundamentals. Analysts assign investment ratings considering, among other things, the 0-12 month total return expectation for a stock and the firm's guidelines for ratings dispersions (shown in the table below). The current price objective for a stock should be referenced to better understand the total return expectation at any given time. The price objective reflects the analyst's view of the potential price appreciation (depreciation).

Investment rating	Total return expectation (within 12-month period of date of initial rating)	Ratings dispersion guidelines for coverage cluster <sup>R2</sup>
Buy	≥ 10%	≤ 70%
Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

<sup>R2</sup> Ratings dispersions may vary from time to time where BofA Global Research believes it better reflects the investment prospects of stocks in a Coverage Cluster.

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