

ASSOCIATION
OF AMERICAN
RAILROADS

John T. Gray
Senior Vice President - Policy & Economics

March 5, 2012

The Honorable Cynthia T. Brown
Chief, Section of Administration
Office of Proceedings
Surface Transportation Board
395 E Street, SW.
Washington, DC 20423-0001

Dear Ms. Brown:

This submission is the AAR forecast of the second quarter 2012 All-Inclusive Index and Rail Cost Adjustment Factor, filed in Ex Parte No. 290 (Sub-No. 5) (2012-2) *Quarterly Rail Cost Adjustment Factor*. The versions of RCAF-related indices covered in this filing are: the All-Inclusive Index (initiated in the second quarter of 1985), the Unadjusted RCAF (produced since October 1982), the Adjusted RCAF (first published in the second quarter of 1989), and the RCAF-5 (created by the STB in its Ex Parte No. 290 (Sub-No. 7) decision served October 3, 1996). The table below summarizes the second quarter 2012 results on the fourth quarter 2007 base, and shows the percentage changes from the previous quarter.

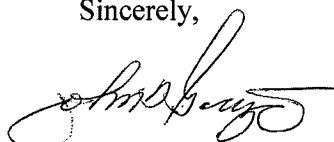
	<u>2012Q1</u>	<u>2012Q2</u>	<u>% Change</u>
All-Inclusive Index	117.6	120.7	2.6
Preliminary RCAF	1.176	1.207	2.6
Forecast Error Adjustment	-0.007	-0.022	
RCAF (Unadjusted)	1.169	1.185	1.4
Productivity Adjustment Factor	2.2724	2.2769	
RCAF (Adjusted)	0.514	0.520	1.2
PAF-5	2.3978	2.4062	
RCAF-5	0.488	0.492	0.8

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In its October 3, 1996 decision in Ex Parte No. 290 (Sub-No. 7), *Productivity Adjustment - Implementation*, the STB noted its intent to publish, in addition to the RCAF (Unadjusted) and RCAF (Adjusted), an RCAF-5 (i.e., a calculation of the productivity adjusted RCAF values as if the agency had always used a 5-year rolling average to calculate the productivity adjustment). In response to a request by STB staff, the AAR is including a calculation of the RCAF-5 in its quarterly RCAF filing. The AAR and its members, however, do not believe the publication of a third RCAF index is required or permitted by the applicable statute (49 U.S.C. § 10708) and do not endorse its publication.

We have notified Paul Aguiar, in the STB office handling this proceeding, of our plan to e-file the submission and hand-deliver workpapers. A copy of the quarterly non-proprietary workpapers underlying this submission will be hand-delivered and filed herewith, in accordance with the ICC's order in Ex Parte No. 290 (Sub-No. 2), *Railroad Cost Recovery Procedures*, served February 8, 1990. A second copy of the workpapers has been delivered to the STB office handling this proceeding. All workpapers are available for STB inspection. Questions should be directed to me or Clyde Crimmel (202 639-2309) of this office.

Sincerely,



John T. Gray

Attachments

**Second Quarter 2012
All-Inclusive Index**

Ex Parte No. 290 (Sub-No. 5) (2012-2)

**Quarterly Rail Cost Adjustment Factor
Surface Transportation Board**

**Policy and Economics Department
Association of American Railroads**

March 5, 2012

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Introduction

On January 2, 1985, the Interstate Commerce Commission (ICC) [now the Surface Transportation Board (STB)] adopted the All-Inclusive Index of Railroad Costs as the basis for the Rail Cost Adjustment Factor (RCAF). The quarterly projection of railroad costs, as documented herein, employ the All-Inclusive Index as required by the regulations. Also presented in this submission is the RCAF, both Adjusted and Unadjusted, as required by the ICC in its decision in Ex Parte No. 290 (Sub-No. 4), *Rail Cost Recovery Procedures - Productivity Adjustment*, served March 24, 1989. In addition, the AAR has included (but does not endorse) the RCAF-5, which was instituted by an STB decision served October 3, 1996 in Ex Parte No. 290 (Sub-No. 7), *Productivity Adjustment - Implementation*. This quarter's projection of railroad costs is for the second quarter 2012. The STB's February decision regarding the change in railroad productivity has been included where appropriate.

Index Weights

In the Ex Parte No. 290 (Sub-No. 2) final rules, issued in April 1981, the Interstate Commerce Commission mandated that the weights of each major cost component be updated annually. These "external" weights are calculated using data from Schedules 410 and 210 of the R-1 annual report filed with the Surface Transportation Board by the Class I railroads. The weights are typically updated with the fourth quarter projection.

The 2010 (current) and 2009 (previous) weights are shown below. The previous (2009) weights were used for the fourth quarter of 2010 through the third quarter of 2011. Beginning with the fourth quarter of 2011, the 2010 weights are used. The year 2010 was a recovery year from the reduced traffic levels of 2009, and operating expenses increased in every category. Fuel expenses increased by the highest percentage and amount, caused by increased traffic and higher fuel prices. Not surprisingly, Fuel's weight rebounded from 14.9 percent to 18.0 percent. This is the fourth highest weight ever for Fuel. The only other category to have its weight increase was Other, which had the second highest percentage increase in expenses. (Most of Other is purchased services, portions of general & administrative expenses, and property taxes.) Labor's weight decreased from 34.7 to 33.3 percent, despite increases in expenses. Weights for Depreciation and Equipment Rents decreased by 1.1 and 0.9 percentage points, respectively. Changes for the remaining categories were decreases of 0.1 percentage points.

RCAF Weights		
	Previous 2009	Current 2010
Labor	34.7 %	33.3 %
Fuel	14.9	18.0
Materials & Supplies	5.1	5.0
Equipment Rents	7.1	6.2
Depreciation	13.9	12.8
Interest	3.0	2.9
Other	21.3	21.8

Reweighting of the index is accomplished by calculating both the current quarter (normally the fourth) and prior (normally the third) quarter indexes with the new weights. The relative change between the two quarters is then multiplied times the prior quarter (usually the third) *linked* index. Use of this method ensures that the weight change, by itself, does not cause a change in the level of the All-Inclusive Index.

Internal weights in the labor and equipment rents components are updated at the same time as the external weights. When these weights are changed, they are also linked using the procedure described above in order to eliminate the effect of the change in weighting.

All-Inclusive Index Second Quarter 2012

The components and values of the current and previous All-Inclusive Indexes are shown below. Details of the construction of each component of the index are contained in the Appendices.

	2010 Weights	Forecast		Percent Change
		Previous 2012Q1	Current 2012Q2	
1. Labor	33.3%	379.4	385.8	1.7 %
2. Fuel	18.0%	387.7	409.4	5.6
3. M&S	5.0%	263.7	274.1	3.9
4. Equipment Rents	6.2%	203.4	204.8	0.7
5. Depreciation	12.8%	208.7	211.4	1.3
6. Interest	2.9%	90.6	90.6	0.0
7. Other	21.8%	215.6	218.8	1.5
8. Weighted Average				
a. 1980 = 100		298.3	306.0	
b. 1980 = 100 (linked)		289.2	296.7 ¹	
c. 4Q07 = 100		117.6	120.7 ²	2.6

¹ To calculate the 1980 = 100 Linked Index:

$$\begin{aligned} \text{Index}_{80} &= (\text{Current Index} / \text{Previous Index}) * \text{the Previous Quarter Linked Index} \\ &= (306.0 / 298.3) \times 289.2 \\ &= 296.7 \end{aligned}$$

² To calculate the 4Q07 = 100 index:

$$\begin{aligned} \text{Index}_{4Q07} &= (\text{Current Linked Index} / 4Q07 Linking Factor) * 100 \\ &= 296.7 \text{ divided by } 245.9 \text{ times } 100 \\ &= 120.7 \end{aligned}$$

Indexes based on other periods:

- 4Q02 based index = 296.7 / 192.1 x 100 = 154.5
- 4Q97 based index = 296.7 / 173.2 x 100 = 171.3
- 4Q92 based index = 296.7 / 156.9 x 100 = 189.1
- 4Q87 based index = 296.7 / 132.2 x 100 = 224.4

Forecast vs. Actual All-Inclusive Index Fourth Quarter 2011

Because of data availability, the forecast error adjustment has a two-quarter lag from each filing. As shown below, the fourth quarter actual index of 116.0 is 2.2 index points below the forecast value of 118.2. Therefore, the forecast error adjustment for second quarter 2012 is -2.2 index points.

	2010 Weights	Fourth Quarter 2011		Amt Difference
		Forecast	Actual	
1. Labor	33.3%	375.3	373.9 ¹	
2. Fuel	18.0%	396.9	375.4	
3. M&S	5.0%	265.7	265.7	
4. Equipment Rents ²	6.2%	205.9	204.2	
5. Depreciation	12.8%	208.4	208.4	
6. Interest	2.9%	90.6	90.6	
7. Other	21.8%	220.3	216.9	
8. Weighted Average				
a. 1980 = 100		299.8	294.6	
b. 1980 = 100 (linked) ³		290.6	285.3 ⁴	
c. 4Q07 = 100 ⁵		118.2	116.0	-2.2

Forecast error **→ -2.2 index points**

¹ One railroad revised its 2010 wage statistics in late October 2011, making it necessary to revise Q4. The forecast error calculation for 2012Q2, which is based on 2011Q4, will use the original number as "forecast" (375.3), and the corrected number as "actual" (373.9). See page 2 of STB Ex Parte No. 290 (Sub-No. 5)(2012-1), served December 20, 2011.

	2010 Weights	Fourth Quarter 2011	
		Forecast	Actual
Car-Hire	45.8%	175.2	175.5
Lease Rentals	54.2%	220.3	216.9
Weighted Average		199.6	197.9
Weighted Average (linked)		205.9	204.2

³ The standard linking procedure has been used to eliminate any changes to indexes that would be caused by updating weights. The Q3 unlinked weighted averages for the All-Inclusive Indexes (forecast and actual) and for Equipment Rents (forecast and actual) were recalculated using the new (2010) weights.

⁴ Linked actual index = (actual index / previous actual index) x previous linked actual index.

$$285.3 = 294.6 / 299.2 \times 289.8$$

⁵ The 4Q07 based indexes are 1980 based indexes divided by the 4Q07 linking factor (245.9/100). Other linking factors are: 4Q02 = 192.1; 4Q97 = 173.2; 4Q92 = 156.9; and 4Q87 = 132.2.

Productivity

On February 6, 2012, the Surface Transportation Board (STB) served a decision in Ex Parte 290 (Sub-No. 4) which added the year 2010 to the Productivity Adjustment Factor (PAF) and removed the year 2005. This creates a geometric average annual productivity change, for the five-year period 2006 through 2010, of 0.8 percent per year. The components of this average annual value are shown on the following table in ratio format – therefore, 1.008 is the same as an increase of 0.8 percent.

Productivity changes are calculated by multiplying each of the five productivity changes together and taking the result to the one-fifth power. The quarter productivity adjustment factors (PAF) are calculated by increasing the previous quarter's PAF by quarterly versions of the annual rate, which are the fourth root of the geometric average annual growth rate. The difference between the PAF and the PAF-5 is the timing of the five-year productivity trend.

Comparison of Output, Input, & Productivity			
2006 - 2010			
Year	Output Index (1)	Input Index (2)	Productivity ¹ Changes (3)
2006	1.018	1.024	0.994
2007	1.000	0.996	1.004
2008	0.990	0.970	1.021
2009	0.847	0.861	0.984
2010	1.109	1.070	1.036
Average			1.008
Previous Average (2005-2009)			1.014

¹ The values shown in Column 3 are based on full float calculations and may not exactly match numbers calculated using the rounded numbers displayed in Columns 1 and 2.

Calculation of PAF and PAF-5

For 2006-2010, use fourth root of avg. productivity change = 1.0020

For 2005-2009, use fourth root of avg. productivity change = 1.0035

Quarter	Year	PAF	PAF-5
Q1	2012	2.2724	2.3978
Q2	2012	2.2769	2.4062
Q3	2012	2.2815	2.4146
Q4	2012	2.2861	2.4231
Q1	2013	2.2907	2.4279

2005-2009

2006-2010

Rail Cost Adjustment Factor Second Quarter 2012

Four RCAF values are presented in this filing. Two are not modified for productivity (Preliminary RCAF and RCAF Unadjusted), and two incorporate a productivity calculation (RCAF Adjusted and RCAF-5). The All-Inclusive Index and all four RCAF values, plus the percent change for each, are shown below. Note that the All-Inclusive Index is on a 2007Q4=100 basis.

	Previous 2012Q1	Current 2012Q2	Percent Change
All-Inclusive Index ¹	117.6	120.7	2.6
Preliminary RCAF ²	1.176	1.207	2.6
Forecast Error Adjustment ³	<u>-0.007</u>	<u>-0.022</u>	
RCAF (Unadjusted) ⁴	1.169	1.185	1.4
Productivity Adjustment Factor ⁵	<u>2.2724</u>	<u>2.2769</u>	
RCAF (Adjusted) ⁶	0.514	0.520	1.2
PAF-5 ⁷	2.3978	2.4062	
RCAF-5 ⁸	0.488	0.492	0.8

¹ See All-Inclusive Index on page 3.

² All-Inclusive Index divided by the All-Inclusive Index in the base period (100.0).

³ The current figure is from Forecast vs. Actual All-Inclusive Index in this filing (page 4). The previous quarter figure is shown in a similar section of the previous quarter's filing.

⁴ Preliminary RCAF plus the forecast error adjustment.

⁵ See Productivity on page 5.

⁶ RCAF (Unadjusted) divided by the Productivity Adjustment Factor (PAF).

⁷ See Productivity on page 5.

⁸ RCAF (Unadjusted) divided by the PAF-5.

Appendixes

Labor

Second Quarter 2012

The second quarter 2012 Labor Index is forecast to rise 1.7 percent from the previous quarter. New national labor agreements were added to the index, causing the increase.

New National Agreements: Ten new national labor agreements were added to the labor index. Counting the two national agreements added in 2012Q1, all possible new labor agreements for the national unions except the BMWED have been included in the index. (See Appendix H for union and railroad abbreviations.) The ten unions added to the index for this quarter are listed below.

- American Train Dispatchers Association (ATDA)
- Brotherhood of Locomotive Engineers and Trainmen (BLET)
- Brotherhood of Railroad Signalmen (BRS)
- International Association of Machinists and Aerospace Workers (IAM)
- International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths.... (IBBM)
- International Brotherhood of Electrical Workers (IBEW)
- National Conference of Firemen and Oilers (NCFO)
- Sheet Metal Workers' International Association (SMW)
- Transportation Communication International Union (TCU)
- Brotherhood of Railway Carmen Division of the TCU (TCU-Carmen)

The new labor agreements typically feature two retroactive wage increases of 2.0 and 2.5 percent (which cause back pay) and a lump sum payment. Because of the complexity of the lump sum calculations for members of the BLET, lump sum payments for that union will not be added to the index until 2012Q3.

Wage Rate Index

The Wage Rate Index portion of the Labor Index increased 2.4 percent from the previous quarter. Much of this increase was caused by new labor agreements.

Wage Increases: Ten new national labor agreements (discussed above) were added to the index. These contracts had retroactive wage increases of 2 and 2.5 percent, plus bonuses. One of the unions (IAM) kept one of two cost-of-living adjustments. Increases in the national agreement for the BLET were "diluted" because many of the railroads have independent agreements with their locomotive engineers for wage purposes.

Lump Sums: The second quarter lump sum rate increased 18.8 cents (or \$0.188). The increase was caused by national and independent labor agreements. The UTU and UTU-Yardmaster Rate Progression Bonus was not added to the Q1 index because of lack of information. This bonus has been added to the 2012Q2 index. Lump sum payments for 9 of the 10 newest labor agreements were also added to the index. The lump sum payments for the 10th union, BLET, are more difficult to determine, so they will not be added to the index until 2012Q3. Two railroads independently make annual performance bonus payments to their locomotive engineers. The net result of the removal of the 2011 performance bonus payments (which were completely amortized), and the addition of new payments for 2012, was an increase.

Labor

Second Quarter 2012

Back Pay: The second quarter back pay rate more than doubled because of the retroactive wage increases for employees participating in the 10 new national agreements. As always, index procedure dictates that back pay amounts are amortized over 4 quarters instead of applied entirely in one quarter.

Other: In wages, "Other" contains the amortization of incentive compensation payments that a large railroad makes each year to its dispatchers, yardmasters, and engineers. This rate is unchanged. This quarter is the fourth quarter for amortization of the 2011 payment. For 2012Q3, the 2011 payment will be removed from the index and replaced by the 2012 payment.

Supplements Index

The impact of higher taxable earnings on Railroad Retirement costs caused the 0.8 percent increase in the Supplements Index.

Health & Welfare: Normally, new health & welfare premiums become effective on January 1. Because of labor agreement negotiations, the premiums in effect for 2011 will continue into the first and second quarters, but will be updated sometime this year (possibly causing back pay if employee cost sharing is affected). The Health & Welfare rate is unchanged from the first quarter.

Railroad Retirement: The Railroad Retirement & Medicare rate increased 1.9 percent because of higher taxable earnings.

Unemployment Insurance: The Unemployment Insurance rate is unchanged despite higher taxable earnings because of relatively low maximum taxable earnings.

Other: The "Other" category is a reflection of all other fringe benefits, and currently contain known employer contributions to employee 401(k) accounts and employer contributions to employee stock plans that are recorded as fringe benefits. The hourly rate is similar to the previous quarter, decreasing only 0.1 cents.

Labor Index Calculation

As shown in Table A-1 on the next page, the 2.4 percent increase in the Wage Index and the 0.8 percent increase in the Supplements Index had a combined effect of a 1.7 percent increase in the Labor Index. The linked second quarter 2012 index is 385.8.

Labor
Second Quarter 2012

Table A-1 Labor Index

	2012Q1	2012Q2	Change	
			Percent	Amount
<u>Base Wage</u> – Straight Time & Pay For Time Not Worked	\$35.633	\$35.956	0.9%	\$0.323
Adjustments:				
Lump Sum	0.226	0.414	83.2%	0.188
Back Pay	0.347	0.707	103.7%	0.360
Other	0.195	0.195	0.0%	0.000
Total Wages	<u>36.401</u>	<u>37.272</u>	2.4%	0.871
Health & Welfare Benefits	8.554	8.554	0.0%	0.000
RR Retirement & Medicare	7.228	7.363	1.9%	0.135
Unemployment Insurance	0.433	0.433	0.0%	0.000
Other	0.134	0.133	-0.7%	-0.001
Total Supplements	<u>\$16.349</u>	<u>\$16.483</u>	0.8%	0.134
Total Labor	\$52.750	\$53.755		
Wage Index¹	311.5	319.0	2.4%	
Supplements Index²	604.2	609.1	0.8%	
Total labor Index, 2010 Weights ³	399.9	406.6		
Labor Index (linked)⁴	379.4	385.8	1.7%	

¹ 1980 wage rate \$11.685

² 1980 supplements rate \$2.706

³ 2010 weights: wages, supplements 69.8% 30.2%

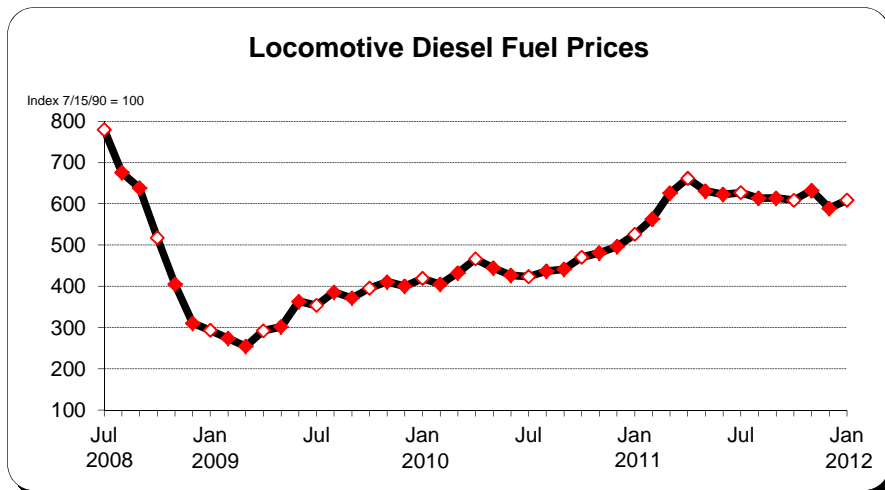
⁴ 2012Q2 linked Index = 2012Q1 linked x (2012Q2 / 2012Q1)
= 379.4 x 406.6 / 399.9

Fuel Second Quarter 2012

The forecast for fuel is based on: (1) a survey of railroad fuel purchasing officers concerning current price and volume levels, (2) expectations of railroad purchasing officers based on their own forecast models and discussions with their major suppliers, and (3) a consensus of petroleum industry experts and general business publications.

Locomotive diesel fuel prices for 2011 reached a peak in April, continuing a trend upward that began after March 2009 (with a few "dips"). The latest locomotive diesel fuel prices available are for January, and its average continues a "leveling off" trend with a small increase. While average prices for locomotive diesel fuel are not currently available for February, the Energy Information Administration has posted averages for heating oil for the first four weeks of the month, and they are higher than their January average.* Crude oil spot prices for West Texas Intermediate were also higher in February than January.** The current political situation in Iran has caused concerns about oil supply, and positive economic numbers from China and the United States indicate stronger demand. On-highway diesel fuel prices have also been rising in recent weeks.

Railroads believe locomotive diesel fuel prices for April 2012 (Q2) will be 9.0 percent higher than the first quarter prices actually paid in January (which represents Q1). However, because the first quarter forecast (made in early December) was too high, the second quarter 2012 forecast is only 5.6 percent higher than the previous quarter.



Forecast Fuel Index	409.4
Change from previous quarter forecast	5.6%
Change from previous quarter actual	9.0%

* Heating oil and locomotive diesel fuel are part of a group of closely related products, commonly labeled as distillates, that differ mostly by their sulfur content. Because of these similarities, these fuels are produced together and have similar pricing trends.

** Diesel fuel used by locomotives is made from refined crude oil, and therefore usually has some price correlation with crude oil.

Materials & Supplies

Second Quarter 2012

The second quarter 2012 Materials & Supplies Index increased 3.9 percent from its first quarter value. The increase was caused by higher prices paid in the Miscellaneous Products category, which contains items such as ballast, creosote, lube oil, and others. The net result of changes in prices for the Forest Products and Metal Products categories was almost no change.

2012Q2 Materials & Supplies Index = 274.1

2012Q1 Materials & Supplies Index = 263.7

Difference	10.4 basis points
	or
	3.9 %

Equipment Rents Second Quarter 2012

The Equipment Rents Index consists of two components – car hire and lease rentals. The methodology used to create these two components and the final Equipment Rents Index are explained below.

Car Hire

The car hire component is indexed using data from the Car Hire Accounting Rate Master (CHARM) file. Car hire rates for the forecast quarter are estimated based on data for active freight cars using the most recent month available. For the first quarter, December 1 of the previous year is used. For the second, third and fourth quarters; March 1, June 1, and September 1 are used, respectively. Using data retrieved from the latest CHARM file, an average rate per car is developed. Next, those average rates are grouped into car type categories to create an overall summary of car hire rates. The summary rates are then compared from quarter to quarter to determine the Car Hire Index.

Lease Rentals

The lease rentals portion of the Equipment Rents Index uses the Producer Price Index for Industrial Commodities less Fuel and Related Products and Power (PPI-LF). The Commission adopted this surrogate in its decision served March 13, 1987. The AAR uses six years of historical data to derive its forecast for the PPI-LF. The forecast is used not only for lease rentals, but also for the "Other" component of the All-Inclusive Index. Appendix G discusses the forecast in more detail.

Equipment Rents Index Calculation

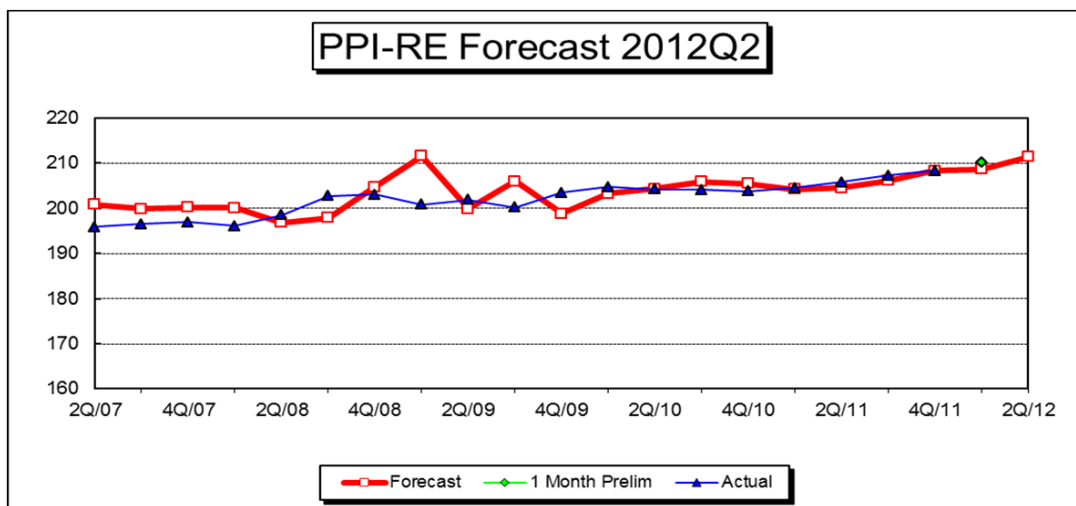
The table below calculates the Equipment Rent Index, which increased 0.7 percent. The second quarter Car Hire portion of the Index decreased 0.4 percent because of lower rates for railroad-owned cars and autoracks. A 1.5 percent increase for the PPI-LF (See Appendix G) used as a proxy for Lease Rentals, combined with the 0.4 percent decrease for Car Hire, caused the Equipment Rent Index to increase 0.7 percent.

	2010			Percent
	Weight	2012Q1	2012Q2	Change
Car Hire	45.8%	175.5	174.8	-0.4 %
Lease Rentals	54.2%	215.6	218.8	1.5
Weighted Average		197.2	198.6	0.7
Weighted Average (Linked)		203.4	204.8	0.7

Depreciation Second Quarter 2012

The Producer Price Index for Railroad Equipment (PPI-RE) is used to index depreciation expense. The PPI-RE is forecast using an ARIMA (Auto-Regressive Integrated Moving Average) process where a statistical package picks the model that best fits the historical data set (see next page), and that model is then used for the forecast. The historical data set contains 6 years of monthly data (a sample size of 72), where the most recent available data point is the first month of the quarter prior to the forecast quarter. For a first quarter forecast, the most recent month of data available would be for October of the prior year. For a second quarter forecast, January would normally be the most recent period available. April and July would be the most recent months available for third and fourth quarter forecasts, respectively. The output from the forecast model is shown on page 2 of this appendix on a 1982=100 basis. The figure forecast by the model reflects monthly PPI-RE figures that, with one exception, have had only small increases during recent months. The increase in the forecast may be amplified by a previous quarter forecast that may have been too low.

Forecast of Depreciation Index (1982=100)	191.1
Forecast of Depreciation Index (1980=100)	211.4
Change from previous quarter forecast	1.3%
Change from actual first month of previous quarter	0.6%
Change from same quarter of prior year (actual)	2.7%



Depreciation Second Quarter 2012

PPI RAILROAD EQUIPMENT

Recommended model: Exponential Smoothing
 Forecast Model for PPIRE
 Holt exponential smoothing: Linear trend, No seasonality

Component	Smoothing Weight	Final Value
Level	0.83173	189.90
Trend	0.01861	0.29950

Within-Sample Statistics

Sample size 72	Number of parameters 2
Mean 180.2	Standard deviation 5.828
R-square 0.9678	Adjusted R-square 0.9674
Durbin-Watson 2.037	Ljung-Box(18)=22.2 P=0.7766
Forecast error 1.053	BIC 1.102
MAPE 0.004121	RMSE 1.038
MAD 0.7369	

Actual Values for the Most Recent 6 Periods:

Date	Actual
2011-08	187.400
2011-09	187.500
2011-10	187.500
2011-11	187.700
2011-12	189.900
2012-01	189.900

Forecasted Values

Date	2.5 Lower	Forecast	97.5 Upper
2012-02	188.037	190.196	192.355
2012-03	187.665	190.495	193.325
2012-04	187.425	190.795	194.164
2012-05	187.260	191.094	194.928
2012-06	187.146	191.394	195.642
QTR AVG	187.277	191.094	194.911

Interest Second Quarter 2012

The Interstate Commerce Commission, in its decision served February 28, 1989, revised the All-Inclusive Index methodology to include a specific interest component, which is to track changes in the average interest rate from year to year. The interest rate is essentially the embedded cost of debt, i.e., total interest expense divided by average total long term debt. The interest rate is calculated for the most recent year and used until the next year's figures are available. Typically in the fourth quarter filing, the interest rate is updated to the new level. The source for interest expense is Schedule 210, column b, from the R-1 annual report. The lines used from current R-1 annual reports are listed below. The source for average total debt is Schedule 200 from the R-1 annual report. The sums of data from columns b and c (ending and beginning balances) are combined and divided by 2 to compute an average balance. The line numbers are listed below. Beginning with fourth quarter 2011, the Interest Index is based on data for 2010.

The interest index is the latest year's interest rate divided by 7.85 percent, which was the interest rate in the 1980 base period.

Interest Expense (Schedule 210)

Line	
42	Total Fixed Charges
44	Contingent Interest
less	
22	Release of Premium on Funded Debt

Average Total Debt (Schedule 200)

Line	
30	Current Loans and Notes Payable
39	Equipment Obligations and Other Long Term Debt Due Within One Year
41	Funded Debt Unmatured - Non-Current
42	Equipment Obligations - Non-Current
43	Capitalized Lease Obligatons - Non-Current
44	Debt in Default - Non-Current
45	Accounts Payable: Affiliated Companies - Non-Current
46	Unamortized Debt Premium - Non-Current

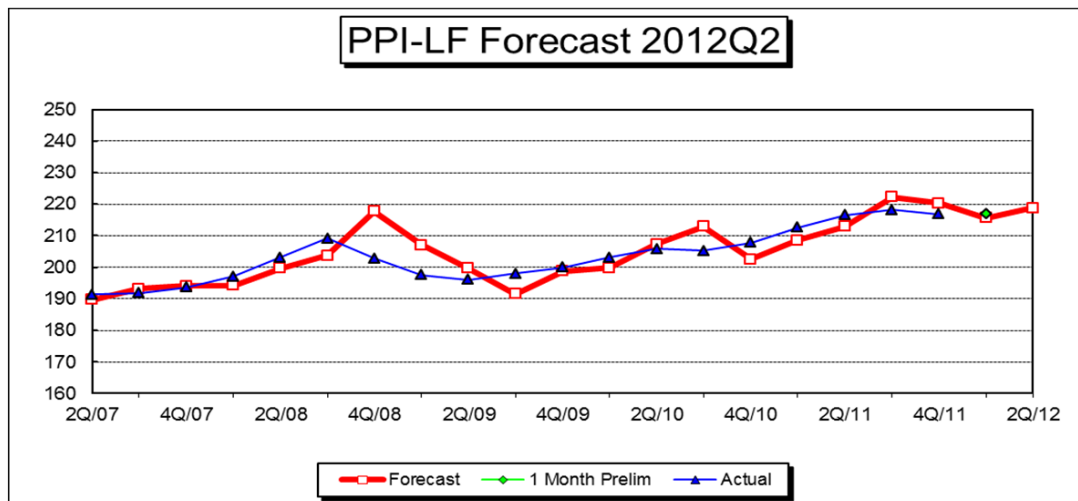
2010	Interest Rate	7.11%
1980	Interest Rate	7.85%
2012Q2	Interest Index	90.6
2012Q1	Interest Index	90.6
	Percent Change	0.0%

Other Expenses Second Quarter 2012

The Producer Price Index for Industrial Commodities less Fuels and Related Products and Power (PPI-LF) is used to index purchased services, casualties and insurance, loss and damage, taxes (other than income and payroll), general and administrative expenses, and lease rentals. These expenses, when grouped together, are usually called "Other" expenses.

Like the PPI-RE, the PPI-LF is forecast using an ARIMA process on 6 years of monthly data (a sample size of 72) with the most recent available monthly data being the first month of the quarter prior to the forecast quarter. For a first quarter forecast, the most recent month of data available would be for October of the prior year. For a second quarter forecast, January would normally be the most recent month available. April and July would be the most recent months available for third and fourth quarter forecasts respectively. The output from the forecast model is shown on page 2 of this appendix for 1982=100. The figure forecast by the model for the second quarter reflects recent monthly PPI-LF figures that were decreasing until the latest month, which increased by the largest percentage since July 2011.

Forecast of Other Expense Index (1982=100)	195.2
Forecast of Other Expense Index (1980=100)	218.8
Change from previous quarter forecast	1.5%
Change from actual first month of previous quarter	0.9%
Change from same quarter of prior year (actual)	1.0%



Other Expenses Second Quarter 2012

PPI INDUSTRIAL COMMODITIES LESS FUELS AND RELATED PRODUCTS AND POWER

Recommended model: Exponential Smoothing
Forecast Model for PPILF
Holt exponential smoothing: Linear trend, No seasonality

Component	Smoothing Weight	Final Value
Level	1.00000	193.50
Trend	0.03165	0.41556

Within-Sample Statistics

Sample size 72	Number of parameters 2
Mean 178.9	Standard deviation 9.004
R-square 0.9863	Adjusted R-square 0.9861
Durbin-Watson 0.5422	**Ljung-Box(18)=104.1 P=1
Forecast error 1.062	BIC 1.111
MAPE 0.004016	RMSE 1.047
MAD 0.7251	

Actual Values for the Most Recent 6 Periods:

Date	Actual
2011-08	194.500
2011-09	194.600
2011-10	194.200
2011-11	193.400
2011-12	193.000
2012-01	193.500

Forecasted Values

Date	2.5 Lower	Forecast	97.5 Upper
2012-02	191.738	193.916	196.093
2012-03	191.203	194.331	197.459
2012-04	190.896	194.747	198.597
2012-05	190.704	195.162	199.620
2012-06	190.586	195.578	200.570
QTR AVG	190.729	195.162	199.596

Railroad and Union Abbreviations

Second Quarter 2012

Railroads

BLE	Bessemer & Lake Erie Railroad (Part of CN's Grand Trunk Corp.)
BNSF	BNSF Railway Company
CC	Chicago, Central & Pacific (Part of CN's Grand Trunk Corp. Sometimes noted as CC&P.)
CN	Canadian National Railway (Commonly known as CN, owns Grand Trunk Corporation.)
CNGT	AAR's abbreviation for Grand Trunk Corporation (Almost all of CN's U.S. operations.)
CP	Canadian Pacific (Also noted as CPR. Owns the U.S. Class I railroad Soo Line.)
CSX	CSX Transportation
D&H	Delaware & Hudson (Canadian Pacific's U.S. operations, to be included beginning 2011Q4.)
DME	Dakota, Minnesota & Eastern (Canadian Pacific's U.S. operations, to be included beginning 2011Q4.)
DMIR	Duluth, Missabe & Iron Range Company (Part of CN's Grand Trunk Corp.)
DWP	Duluth, Winnipeg & Pacific Railway (Part of CN's Grand Trunk Corp.)
EJE	Elgin, Joliet & Eastern Railway (Part of CN's Grand Trunk Corp.)
GTW	Grand Trunk Western Railroad (Part of CN's Grand Trunk Corp.)
IC	Illinois Central Railroad (Part of CN's Grand Trunk Corp.)
KCS	Kansas City Southern Railway
NS	Norfolk Southern Combined Railroad Subsidiaries (a.k.a. Norfolk Southern Railway or NS Rail)
SOO	Soo Line Railroad (the largest of Canadian Pacific's U.S. operations.)
UP	Union Pacific Railroad
WC	Wisconsin Central and subsidiaries (Part of CN's Grand Trunk Corp.)

Major Unions Involved with Railroads

ATDA	American Train Dispatchers Association
BLET	Brotherhood of Locomotive Engineers and Trainmen Div. of the International Brotherhood of Teamsters
BMWED	Brotherhood of Maintenance of Way Employees Division of the International Brotherhood of Teamsters
BRS	Brotherhood of Railroad Signalmen
IAM	International Association of Machinists and Aerospace Workers
IBBM	International Brotherhood of Boilermakers, Iron Ship Builders, Blacksmiths, Forgers & Helpers
IBEW	International Brotherhood of Electrical Workers
NCFO	National Conference of Firemen and Oilers
SMW	Sheet Metal Workers' International Association
TCU	Transportation Communication International Union
TCU-Carmen	Brotherhood of Railway Carmen Division of the Transportation Communications International Union
UTU	United Transportation Union
UTU-Yard	United Transportation Union Yardmaster Department (also noted as UTU-YMD)

Predecessor Unions (Some AAR databases use these old abbreviations.)

BLE	Brotherhood of Locomotive Engineers (predecessor to BLET)
BMWE	Brotherhood of Maintenance of Way Employees (predecessor to BMWED)
BRC	Brotherhood of Railway Carmen (predecessor to TCU-Carmen)
IBFO	International Brotherhood of Firemen and Oilers (predecessor to NCFO)