

FINAL TRANSCRIPT

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NSC - Q1 2010 Norfolk Southern Corp Earnings Conference Call

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PRESENTATION

Operator

Greetings and welcome to the Norfolk Southern Corporation first quarter earnings conference call. At this time all participants are in a listen-only mode. A question-and-answer session will follow the formal presentation. (Operator Instructions) As a reminder this conference is being recorded. It is now my pleasure to introduce you're host, Leanne Marilley, Norfolk Southern Director of Investor Relations. Thank you, Ms. Marilley. You may begin.

Leanne Marilley - *Norfolk Southern Corporation - Director, IR*

Thank you and good afternoon. Before we begin today's call, I would like to mention a few items. First, we remind our listeners and internet participants that the slides of the presenters are available for your convenience on our website at nscorp.com in the investors section. Additionally, MP3 downloads of today's call will be available on our website for your convenience.

As usual, transcript of the call also will be posted on our website. At the end of the prepared portions of today's call will conduct a question-and-answer session. At that time, if you choose to ask a question, an operator will instruct you how to do so from your telephone keypad. Please be advised that any forward-looking statements made during the course of this presentation represent our best good-faith judgment as to what may occur in the future.

Statements that are forward-looking can be identified by use of the words such as believe, expect, anticipate, and project. Our actual results may differ materially from those projected and will be subject to a number of risks and uncertainties, some of which may be outside our control. Please refer to our annual and quarterly corporate reports filed with the SEC for a discussions of those risks and uncertainties we view as most important.

Additionally, keep in mind that all references to quarter results excluding certain adjustments such as non-GAAP numbers have been reconciled on our website at nscorp.com in the investor section. Now it is my pleasure to introduce Norfolk Southern Chairman, President and CEO, Wick Moorman.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

Thank you, Leanne and good afternoon everyone. It is my pleasure to welcome you to our first quarter 2010 earnings conference call. With me today are several members of our management team including Mark Manion, our Chief Operating Officer, and Don Seale, our Chief Marketing Officer. Jim Squires, our CFO, is in a middle of a session at Harvard, and therefore our Vice President and Controller Jake Allison is here to discuss the financials.

Norfolk Southern generated strong first-quarter results, demonstrating solid volume and revenue growth along with improved productivity and aggressive cost control. Which resulted in a 5.1 percentage point year-over-year improvement in the operating ratio, which declined to 75.2%. Income from railway operations was \$555 million, up 45% compared with the same period last year. Net income and earnings per share also were up 45%, as a 15% gain in revenues more than offset an 8% increase in operating expenses as well as increased income taxes, which included a \$27 million, or \$0.07 per share deferred tax charge due to the recently enacted healthcare legislation.

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Of particular significance, volumes continue to gain momentum, strengthening not only year-over-year, but also, and perhaps more significantly, on a sequential basis from the fourth quarter, which as you know, is almost unheard of in our industry. As Don will discuss in a moment, we posted a number of 52 week high's during the quarter. Operationally, we continue to improve productivity and saw significant operating leverage.

Against the 9% year-over-year volume increase, crew starts declined 1%, locomotive fuel consumption was up only 5%, and total headcount, as well as T&E headcount both declined 7%. On a sequential basis from the fourth quarter, volumes were up 1% while overall headcount and T&E headcount remained essentially flat. Mark will review these and other operating efficiencies, which we are confident well continue going forward.

Expenses were also reflective of this operating execution as we posted improvement in all expense categories except fuel and compensation. Those increases were driven by higher fuel prices, health care costs, and wage inflation, and improved financial performance measures rather than activity. And Jake will discuss the details later in the call.

Norfolk Southern's first quarter performance provides a strong platform from which to build momentum throughout the remainder of the year. And it reflects the strength of our high-value transportation product and operating efficiency. Against the backdrop of an improving economy and continuing operating leverage as volume growth, the stage is set for a favorable 2010.

We remain bullish on the fundamentals of our business, and we continue to make strategic long-term investments in our company. I will now turn the program over to Don, who will be followed by Mark, and then Jake. I'll wrap up with some closing comments before we turn the program over to the operator for your questions. Don?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Thanks, Wick, and good afternoon, everyone. Starting with a recap of revenue, sequential volume improvement combined with the effect of higher fuel revenue and improved pricing, generated revenue of \$2.2 billion for the quarter, up \$295 million, or 15%. Approximately 58% of this increase was driven by higher volume, which represented \$170 million. Fuel related revenue was up \$65 million in the quarter, contributing 22% of the gain.

This included the effect of a \$7 million unfavorable lag in the quarter compared to a \$10 million positive effect in the first quarter of last year. And we continued to generate improved pricing along with \$4 million of positive mix effect, contributed \$60 million, or 20% of the first quarter revenue increased. Turning to yield, on slide three, revenue per unit of \$1,414 was up \$79, or 6%. Increased fuel revenue impacted RPU by \$41, while rate and mix contributed \$38 of the gain.

Record automotive RPU was driven by a successful major legacy contract negotiation and a change in our vehicle service network, which resulted in an extended length of haul. Intermodal and paper revenue per unit was impacted by strong motor carrier competition and increased volumes of the shorter haul -- shorter haul business.

And agriculture saw an increase in shorter haul phosphate rock and grain traffic. Finally, pricing improvement of 3% was recorded during the quarter, as strong competition from rail, barge, and trucking along with the impact of a modest 1.6% gain in the RCAFU moderated yield growth.

Over the past four rolling quarters, we have now realized an average of 5% in price increases. And we believe that tightening transportation capacity in the truckload market in particular bodes well for continued price improvement in the months ahead. Now turning to volume, on slide four, total shipments of nearly \$1.6 billion were up 9% over first quarter last year, driven by gradual economic recovery and project growth.



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Volume gains were slightly offset by the severe winter weather throughout our service territory, which mainly impacted utility coal shipments to Southern utility plants that are generally not equipped with thaw sheds to quickly unload frozen coal. During the quarter, we saw each of our business groups week of 52 week high loadings except automotive. Total volume gains for the month of March accelerated, up 19% over last year.

As shown on slide five, merchandise volume increased by 16% in the quarter. Of that total, agricultural volume up 21% was our second highest quarter ever, and was led by increased shipments of ethanol, up 23%, export grain up 5,200 carloads or nearly 450%, and fertilizers up 128%.

Metals in construction traffic was up 14% in the quarter, as steel traffic grew by 64%, bolstered by higher production and new business. And chemicals volume increased by 20%, as all four of our major chemicals markets expanded year-over-year from improved market demand and the stronger project growth.

Now turning to slide six, paper and forest products volume grew by 5% as inbound woodchips and export wood pulp drove volumes higher. And finally, automotive volume increased by 14% from higher auto production, coupled with new business into the Northeast. This increase was partially offset by the redesign of the Ford vehicle network. This redesign on an annual basis will eliminate some 33,000 carloads, moving in and out of the service centers, which previously were billed as separate shipments.

Also this new design removes the overhead handling of some 11,000 carloads per year as well. In summary, as shown on the next slide, we are seeing a pronounced sequential improvement in merchandise volume from the depth of the recession in the first half of last year. Now transitioning to intermodal on slide eight, total volume was up 11% in the quarter, led by domestic traffic, which was up 23% over the first quarter last year.

Higher volume came primarily from continued success in truckload conversions and our local Eastern network. Currently, truckload capacity is showing signs of tightening. Diesel fuel prices are rising, and pricing in the truckload market has begun to firm, all of which make intermodal a more attractive option for shippers. International intermodal volume was up 3% in the quarter. Higher export shipments which were up 14%, drove this increase as the weaker dollar and increased global demand converged.

Also we saw greater activity with repositioning of empty containers for loads during the quarter, along with modest improvement in import related retail sales. Now turning to our coal business, total coal volume fell 4%, below first quarter 2009, as shown on slide nine our export in domestic metallurgical coal markets benefited from the global resurgence of the steel industry. In that regard, our domestic met business was up 61% versus last year, as 13 blast furnaces that we serve resumed operations. Export coal volume was up 39% over the first quarter 2009, as global steel production grew 30% in the first quarter.

Coal through our Lambert's Point facility was up 25%, while the Baltimore volume was up 125% in the quarter. Volume growth was driven by continued port congestion in Australia, strong Asian demand, and China's exit from the export Coke market, which continued to create opportunities for Coke producers in other countries. Concluding with utility coal on slide 10, volume was down 17% in utility for the first quarter, driven by high stock piles of most utility plants in our service territory.

Also, severe winter weather conditions affected both production and deliveries as coal receipts at utilities were at their lowest level in the last 11 years. Impacting our volume in the quarter by nearly 14,000 carloads. But on a positive note, these severe weather conditions and the improving industrial economy, profit higher electricity generation in our network, which reduced stockpiles by 25%, or 24 million tons.

Some utilities are now within eight to 10 days of target inventory. This conversion trend is approaching the point where coal replenishment will be required for summer and fall generation. Looking ahead, as shown in the next slide, we expect further sequential improvement in our volume as the global economy continues its gradual recovery and as we ramp up new business activity.



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Our industrial products markets will be driven by ongoing manufacturing recovery and specific project growth, which includes a strong expansion in our ethanol network as new terminals are added in our service territory. Current dynamics in the trucking industry including higher fuel and labor costs and tighter truckload capacity, will benefit not only our domestic intermodal conversion strategy, but our business in general.

And increased auto and appliance production along with new business will generate increased volumes of steel as well as higher shipments of domestic and metallurgical coal ahead. Turning to our remaining markets on the next slide, automotive volume comparisons are projected to be flat to slightly positive due to the previously mentioned changes in the Ford vehicle network. And the outlook for forest products will remain challenging for the remainder of 2010 due to the uncertainty of the housing sector, while paper volumes are showing some modest improvement at this point.

In summary, our first quarter volume growth of 9% was encouraging, particularly in view of the accelerating trend realized in the month of March, which was up 19% or 93,000 loads and represented 73% of our first quarter increase. Sequentially, first quarter volume was 16,000 loads of 1% higher than fourth quarter volume.

As we move through the second quarter and the year, we fully expect strong project growth combined with a gradually recovering economy, will sustain higher volumes and revenues. Our higher carloadings in April reflect this upward trend.

In tandem with these positive factors, we expect tighter transportation capacity ahead across all modes, which will support improved pricing as the year progresses. And finally, as always, we will continue to strive to provide efficient and high-quality rail services to all of our customers, never forgetting that they hold the key to our future success. Thanks for your attention, and I will now turn the mike over to Mark for our operating report. Mark?

Mark Manion - Norfolk Southern Corporation - COO

Thank you, Don. Starting with safety, preliminary analysis shows NS with an injury ratio of 1.07 for the first quarter of 2010, while our performance is not where it needs to be, we continue to place a priority on the fundamentals, including rule compliance and employee engagement in the safety process.

Turning to operating performance, at this point you're probably familiar with this graph. It illustrates our focus in maintaining a balanced operating plan.

The green line indicates training starts, while the other lines represent car days, car handling, and car miles. During the first quarter of 2010, we saw a 1% reduction in train starts in the face of a 9% increase in car loadings. This is especially rewarding in light of the challenges of the first quarter of 2010.

As you are aware, this first quarter started with some particularly brutal weather in January and February. When the weather -- then when the weather moderated, we experienced a very pronounced rise in car loadings. These two events back-to-back presented us one of the most challenging operating environments in several years. With regard to assets, during the last quarter, we decreased the number of freight cars in storage to approximately 10,500, and locomotives in storage to approximately 100.

Turning to the next slide, with regard to fuel, consumption was up only 5% while gross ton miles were up 9%. On the next slide, train and engine service employees were reduced 7% versus last year, as we size our workforce to the operating plan and take advantage of labor productivity initiatives such as remote-control locomotives. Approximately 300 T&E employees remain furloughed in areas where business volumes have not returned. All furloughed T&E employees have been offered transfers to areas where business volumes are stronger. However, in addition to the transfers, we have initiated some hiring in these areas as well.

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Turning to our composite service performance, based on the operating challenges previously discussed, our service in the first quarter declined, primarily driven by train performance in connection performance. We dropped to 7.9% in our composite service measure. However, since mid-March, we have managed through many of our service issues and we are closing the gap.

And finally, on the last page, this scorecard summarizes some of our achievements in a recovering economy. Car loadings increased 9% while crew starts were reduced 1%, and total railroad employment was reduced 7%. Our efficiency metrics of gross ton miles per employee, gallons of diesel fuel and train hours, all showed improvements in the quarter. Car hire days per carload increased 5% as networks slowed. However as I stated on the previous slide, our service issues are being addressed and we are seeing benefits of a more fluid network. Thank you, and now I will turn the program over to Jake Allison.

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

Thank you, Mark. I will now review our financial results for the first quarter. Let's start with our operating results. As Don described, railway operating revenues for the quarter totaled \$2.2 billion, up \$295 million, or 15% compared to the first quarter of last year. Slide three shows our total operating expenses. Which increased by \$123 million, or 8% for the quarter. Income from railway operations grew 45% to \$555 million.

A substantial increase in revenues, driven by higher volumes, fuel revenue, and pricing, was partly offset by increased operating expenses. The resulting 75.2% operating ratio is a first quarter, post Conrail transaction record. Turning to our expenses, here are the major components of the \$123 million net increase. Fuel expense accounted for over three fourths of the variance.

As shown on slide five, higher prices drove practically all of the \$95 million of additional costs. Our average price per gallon of diesel fuel was \$2.13, a 54% increase compared with the first quarter of 2009. As you may recall, fuel prices bottomed out in the first quarter last year. As Mark mentioned, although consumption grew by 6%, it compares favorably to our 9% increase in gross ton miles.

Next, compensation and benefits increased by \$60 million, or 9%. Slide seven shows the major components. First, stock-based and incentive compensation increased \$34 million, due primarily to changes in stock price and improved financial results. While our stock and financial measures declined in the first quarter of 2009, they increased in the first quarter of 2010. Second, higher agreement wage rates effective primarily in July 2009, added \$18 million. Third, medical benefits increased \$10 million. Largely related to higher agreement employee health and welfare premiums, coupled with increased retiree medical costs, both of which were partly offset by lower employment levels. Fourth, pension costs increased \$8 million. Lastly the \$10 million decrease in the other category is principally due to reduced employment levels.

As highlighted on slide eight, materials and other expenses decreased \$9 million, or 5%, primarily reflecting lower locomotives and freight materials costs. Depreciation expense decreased as well by \$3 million, or 1%, reflecting the results of a recently completed equipment depreciation study that more than offset the effects increase capital.

This reduction is expected to continue for the remainder of the year. Purchased, services and rents declined \$20 million, or 6%, which reflects a favorable settlement with the freight car supplier, and lower equipment rents. Other miscellaneous favorable items were mostly offset by higher expenses for increased hauling services.

Turning to our non-operating items on slide 10, the majority of the net increase is due to improved returns on corporate owned life insurance, which was up \$6 million. The remaining variance reflects the variety of smaller items, including decreased equity and earnings of Conrail. As illustrated on slide 11, income before income taxes increased \$173 million, or 61%, principally due to higher operating income.



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Income taxes totaled \$199 million and the effective tax rate was 43.6%. Income taxes last year were \$106 million, with an effective rate of 37.5%. The increase in the effective rate for 2010 was almost entirely due to a \$27 million deferred tax charge, resulting from the enactment of the recent healthcare legislation.

Turning to slide 13, first quarter net income was \$257 million, an increase of \$80 million compared to last year. And diluted earnings per share were \$0.68, a \$0.21 per share increase. Both results reflect 45% year-over-year improvements.

Lastly, slide 14 reflects first quarter cash flow highlights. Cash provided by operations more than doubled, easily covering capital expenditures and dividends, and establishing an even more secure liquidity position. Free cash flow for the first quarter jumped over 350%. Thank you for your attention, and now I'll turn the program back to Wick.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

Thank you, Jake. Well, as you seen our strong first quarter results demonstrated the fundamental strengths of our franchise. While our service was impacted by the region's extraordinary weather in January and February, we continue to provide a superior service product, and our customers responded by shipping more on Norfolk Southern as their business levels improved.

The resulting 9% increase in carloads was then combined with continuing operating efficiencies to produce our best the first quarter ratio since the Conrail transaction. Looking ahead, we are increasingly convinced that the domestic economic recovery is well underway, although the rate of growth is still somewhat unclear.

As Don told you earlier, we saw a big upsurge in business in March. And while some of that was clearly catch up from a snowbound February, we are very encouraged that our April volumes have continued to be strong.

If the recovery continues on pace, we are confident that we can continue to sustain our productivity gains and improved our operating ratio and earnings as the year progresses. In addition, as Jake outlined, the substantial improvement in operating results has also strengthened in our cash position. Consistent with past practice, we are taking a balanced approach with respect to our capital structure and distributions. We are making strategic investments in the franchise, as evidenced by our robust capital program this year. We also are continuing our long tradition of delivering value to our owners in the form of dividends as we maintain the highest dividend yield in the industry.

During 2010, we will focus on returning cash to our shareholders, as we continue to look at the dividends and also resume our share repurchase program on an opportunistic basis as market conditions warrant. Going forward, I'm confident that Norfolk Southern will continue to successfully strengthen our economic performance by improving service, launching new product offerings, and building on our operating leverage reaffirming our position as the thoroughbred of transportation. Thanks for your attention, and I will now turn it over to the operator for your questions.

QUESTIONS AND ANSWERS

Operator

Thank you. Ladies and gentlemen, at this time will be conducting a question and answer session. (Operator Instructions) Our first question comes from the line of Jason Seidl with Dahlman Rose. Please proceed with your question.

Jason Seidl - *Dahlman Rose & Co. - Analyst*

Good afternoon, everyone. I guess my first question is going to be for Don. Don, you walk through pricing in the quarter up 3%, but you mentioned that was including RCap. Could you tell us what it was excluding that RCap number of 1.6%?



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Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Good afternoon, Jason. RCap was negligible. As I mentioned, it was only up 1.6% in the quarter, so it had a negligible impact on the 3%.

Jason Seidl - Dahlman Rose & Co. - Analyst

Okay.

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

It is of no consequence.

Jason Seidl - Dahlman Rose & Co. - Analyst

Okay, fair enough. As we look at Q1, it's kind of feeling like a might signal sort of the bottom of the rail pricing network, and I think Wick, you mentioned it yourself, things feel like there tightening up across all modes of transportation. Should investors look at sort of 3% as the bottom and as long as the recovery continues, it will probably build a little bit from there?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Well, Jason, I'll let Don answer that. I will begin by saying that obviously we try not to forecast too far ahead, but as Don mentioned, we do see the transportation market tightening up. We did -- we have averaged about 5% over the past four quarters. Don, what color would you want to get there?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I think that's a good summary. We see transportation demand increasing and transportation capacity declining. Both in the drive then trucking segment as well as the flatbed trucking segment, which I think bodes well for volume and price implications for our steel traffic, Intermodal traffic, as well as some of our carload business.

Jason Seidl - Dahlman Rose & Co. - Analyst

My follow-up question is regards to the Intermodal section. You know, we've had a couple of changes here with CSX and UNP, and now we're hearing UNP is going to be directly marketing its own products. How is that going to change the competitive landscape at least?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

The competitive landscape continues to evolve, Jason. And it continued to do that over time. Were very comfortable that we're positioned properly in the marketplace with good strong Intermodal partners, and as you know, we are making very prudent investments in terms of expanding our Intermodal network and capabilities for the future. So, we feel like we are very well positioned. We are committed to that market, and we feel that it's going to be a growth engine ahead.

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Jason Seidl - *Dahlman Rose & Co. - Analyst*

Okay, fair enough. I appreciate you're time as always, guys.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

Thank you, Jason.

Operator

Our next question comes from the line of Chris Ceraso with Credit Suisse. Please proceed with your question.

Chris Ceraso - *Credit Suisse - Analyst*

Thanks. Good afternoon. I got a couple of questions related to wages and expenses in that vein. First, any remind us what you're expecting for the full year in terms of comp inflation and then how much of that do you think you can offset with productivity and then following that, maybe if you can just give us a rundown on what some of the areas are where you think you still have room to pick up productivity improvement to help offset the comp inflation?

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

Hey, Chris, this is Jake Allison. I will take the comp side of that. Or the initial half of that question. The guidance we gave you at the end of the fourth quarter as it related to increased wages is still accurate. Wages and healthcare for agreement employees, we're expecting about \$150 million over the year. So that's about \$37 million a quarter you can anticipate there.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

As far as the productivity and what we expect, as you know, we have a lot productivity initiatives underway. We are aggressively looking at all of the places that we can do things with technology, including remote control. We are certainly focused on crew size, across the railroad, and we are in the middle of rolling out our leader technology across the northern region. And as the year goes on, we do expect to see further fuel savings as a result.

If you look at our first quarter, we clearly also had some expenses in there that were due to the inclement weather that impacted our train operations. We had a lot of people out on the railroad. We had a lot of overtime. We had a lot of the reworks. The weather has moderated and we are certainly are focused on controlling both expenses as well. We don't forecast how much of the increased labor rates we might be able to make up with productivity, but we are very focused on productivity improvements, and we think we have some good initiatives underway.

Chris Ceraso - *Credit Suisse - Analyst*

Okay, just one follow-up. You mentioned the weather. Is that the primary reason that operating profit declined from Q4 to Q1 even though revenue was up slightly?

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

Jake, I'll turn it to you. Clearly, Q1 has some weather impact. It also always has some comp and benefit impacts that we don't have in the fourth quarter. It's the quarter that our grants are made. It also has some other issues in terms of stock -based

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compensation, incentive -based compensation. I think there were a number of reasons you can walk through. Jake, can you give any more color on that?

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

You've touched on the high points. There were incremental increases over 2009 for pension and post retirement benefits, but Wick mentioned the major drivers.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

Pension and post retirement as well. And historically, if you look at the past few years, our first quarter operating ratio has always been the highest operating ratio of the year.

Chris Ceraso - *Credit Suisse - Analyst*

Okay, thank you very much.

Operator

Our next question comes from the line of Bill Greene with Morgan Stanley. Please proceed with your question.

Bill Greene - *Morgan Stanley - Analyst*

Hi. Don, I'm curious, if I can come back to the pricing question, I know the point of tightening supply certainly makes sense that you would see an improvement in pricing. But I'm also curious if you reset you're export coal prices in the first quarter, or if that's a second quarter even for you that would explain some of the reasons why it doesn't feel like you got quite the kick on pricing that I would expect given how strong export coal was.

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Bill, our export coal repricing is done on April 1. So it's a second quarter event.

Bill Greene - *Morgan Stanley - Analyst*

Okay, that makes sense. Thanks, than. And then Wick, did I understand it to say in effect that you are going to start doing any buyback or is that still yet to come?

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

No, it will be opportunistic. But we are going to reinstate our share purchase program.

Bill Greene - *Morgan Stanley - Analyst*

Okay. Thank you very much.

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Operator

Our next question comes from the line of Tom Wadewitz from JPMorgan. Please proceed with your question.

Tom Wadewitz - JPMorgan - Analyst

Yeah, good afternoon.

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Hi, Tom.

Tom Wadewitz - JPMorgan - Analyst

Wanted to ask you is about your capacity in the network. It seems like you did a real nice job with headcount and train starts, holding that down versus the increase in volume. And to try to get a sense of how much there is left to go, can you give a sense of maybe average train length in your carload network and Intermodal network and how you would view available capacity within those two networks, assuming the same train schedule?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I think I can help you with that, John. If we look at our general merchandise network, where currently averaging 73 cars. That's up 8% quarter over quarter. And similarly, Intermodal is up about 11%. So if you look at that, the average number of cars per train, there is still a lot of there's still a lot of room to grow there. And of course, we try to keep our operating plan sized to the volume, so as we need, we can certainly grow that plan. But will fill out our trains first, and you can see we have a long way to go to fill them out.

Tom Wadewitz - JPMorgan - Analyst

In terms of containers, what would the average length have been for the Intermodal?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Average train length -- average train length in our Intermodal is, it's up about 550 feet. Don --

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

This is Don. For the first quarter, we average about 120 boxes per train in our Intermodal network, and we looked at -- if we look at 160 boxes being about a standard 8,800-foot train, we've got another 25% to 30% capacity in the existing train network as it sits right now and the Intermodal network.

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

We, in general, feel, and you can kind of look at where we've been in the past, but we have a fair amount of capacity in the network. There are places, because business does not come back uniformly across the network, as Mark mentioned, where we're going to be doing some hiring, we're going to be doing some reasonable amount of hiring this year just because we



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always have attrition going on. So we've got to make sure we have people trained and ready to move into places as folks a tread out. But we're confident of our capacity.

Tom Wadewitz - JPMorgan - Analyst

What about in the carload trains? Is said it's 23 cars on average. You said that 73 cars is inkmark on average. What's the potential that that can be at reasonably? Can it get to 90 or 85?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Up in the neighborhood of 90 cars.

Tom Wadewitz - JPMorgan - Analyst

90 cars. Okay. And then a quick one on pricing. I know you aren't big into giving point forecasts or necessarily ranges, but how much impact do you think there is to your franchise if the market, the truckload market really tightens up through -- through the year? Can you see a couple points added onto that 3% basis price that you have been first quarter, or would you be a lot more measured that and get to 5%, 6% later in the year?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Well Tom, we'll kind of restate what we've said previously, that we're watching the rate of inflation, rail inflation, and we're very comfortable and confident that our pricing will exceed our rate of rail inflation going forward.

Tom Wadewitz - JPMorgan - Analyst

Okay, great. Well, thank you for the time. Nice results.

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Thank you.

Operator

Our next question comes from the line of Ed Wolfe with Wolfe Trahan & Company. Please proceed with the question.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Thanks. Good afternoon. Just to start with on the coal side, Don, is that export coal repricing is effective April 1st. Can you give a sense of how that went in the magnitude of what that looks like?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, you know, the export market is strong. It's very robust, both in Asia and in Western Europe. And China being one of the drivers, but recovering global steel production and steel demand is a close second driver to that. So our negotiations went well, and we're very pleased with the result.

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Ed Wolfe - Wolfe Trahan & Company - Analyst

And should we see that full impact in the second quarter, or is there some part -- what percentage of the business repriced on April 1st, in other words?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

We repriced just about all that on April 1.

Ed Wolfe - Wolfe Trahan & Company - Analyst

And is that all matter or is that utility expert that repriced, too?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Predominately metallurgical coal. Some utility in it, but there's a small percentage.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay. Why did the net coal exports weaken from the fourth quarter to first quarter?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Traditionally, the first quarter is weaker because some of the receivers hold back on deliveries as they negotiate new supply contracts in anticipation of new contract year, starting April 1. The second thing is we're doing some maintenance at our facility in Norfolk, and while that's going well, and we've got about 14 more days of that ahead in terms of until we finish that maintenance project, that tempered some of the volume we handled in the month of March as well.

Ed Wolfe - Wolfe Trahan & Company - Analyst

So for those two reasons we should see that pickup in the second quarter as well throughout the quarter?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Yes. That's a fair estimate.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay. Is there any potential impact, positive or negative, from the Massy mine issues? In other words can you guys -- the mines that you serve pick up some of the slack?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, we certainly have a good relationship with Massy, have a good portfolio of mining operations, and I'm sure that the Massy folks are looking at all their options at this point.

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Ed Wolfe - Wolfe Trahan & Company - Analyst

Today nothing incremental though?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Nothing that I can report right now.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay and the just looking at the yield break out copy 5.9%, and I apologize if you did this, but can you breakout the mix of the fuel and the price from that?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

The mix was moderately positive at about \$4 million, and price was \$56 million for the quarter. And of course, our fuel was up \$65 million quarter over quarter.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay. And then I heard you say that there was lower purchased services and rent, and part of that was one off in the quarter. Can you remind me of what that was and how impactful that was on the quarter?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Yes. The purchase services in rent fell \$20 million from last year. We had a one-time settlement with a freight car supplier, which was a good-sized portion of the \$20 million. We also had lower equipment rents throughout the quarter due to some lease turn back and some storage initiatives.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay. And just last one for Wick. Bigger picture. And I think changing on the regulatory environment as you see it in terms of the progress of the bill and do you think that the bill is still coming from the Senate at this point or is it getting too late for that?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

I don't know about the timetable, Ed. It's certainly clear that the Senate has a fair amount on their plates. To get done in the next couple of months. There's really been no change in the past week or two or three. We continue the dialogue with the commerce committee staff. They know that this is not a piece of legislation that we can support in its current form. And so we will continue to work with them and see if we can reach agreement on legislation we can support. But there has been no change.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Has been then, are you still going to DC as often as you were going, you know, three or four months ago?

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Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

The answer is unfortunately, yes.

Ed Wolfe - Wolfe Trahan & Company - Analyst

Okay. Thanks a lot for the time, guys. Appreciate it.

Operator

Our next question comes on the line of Walter Spracklin from RBC Capital Markets. Please proceed with your question.

Walter Spracklin - RBC Capital Markets - Analyst

Thanks very much. Good afternoon, guys. The first question here is you mentioned the attrition, current employee attrition. What is the rate of attrition on a yearly basis roughly?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

About 5% or 6%.

Walter Spracklin - RBC Capital Markets - Analyst

5% or 6%. And are you finding at all when you're bringing resources back online, market price touch of it, is there any challenges that you're coming up against? I know you thought it would be a fluid process in terms of bringing employees back, bringing locos and cars back on line. Now that your starting to do it come are you seeing any challenges in that or is it a fairly fluid process?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

No, it has been a fluid process, and as far as resources go, as we have brought employees back. They have been coming back typically at the rate of about 90%. Here more recently, last month or so, that's dropped to about 85% because they are a little longer in the queue, I guess. And as far as bringing our cars and locomotives back, something we were prepared for, not the first time we have done it. So it's gone pretty smoothly.

Walter Spracklin - RBC Capital Markets - Analyst

Okay. Last question here sort of back on the pricing. You mentioned that there were some pressures and you touched on competitive pressures from rail. I was wondering, Don, if you could perhaps elaborate on that a little bit, particularly, are we seeing significant inter- rail competition? Or if you could sort of give an order of magnitude what the -- from the pressure perspective, which were the main components of that pressure versus some of the others in sort of an order of magnitude?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well the point I was trying to make there is that we saw increased competition across all modes. Trucking, rail, and barge. And I think coming through the first quarter, we saw transportation capacity clearly exceed demand, and although demand started to pick up as the quarter progressed, so we saw increased competition from all modes in the quarter. I wouldn't single out rail by itself. If I put it into order of magnitude, I would say trekking first, rail second, and barge third.



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Walter Spracklin - RBC Capital Markets - Analyst

That's perfect. That's exactly what I was looking for. Thank you very much, guys.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Thank you.

Operator

Our next question comes in the lineup Scott Malat with Goldman Sachs. Please proceed with your question.

Scott Malat - Goldman Sachs - Analyst

Thanks. I just wanted to talk quickly on the service index. And I know the weather was a pressure this quarter, but this is the third quarter in a row where it's kind of lag. I'm hoping you can take be through, I guess one, are there certain areas where maybe your on-time arrivals or departures are focused around? Are there for certain commodity types certain routes where they are focused around, and what are you doing to kind of work on that? And then second along with that, is just as volumes come back, but to get harder and harder to bring the network back from disruptions like weather, and how do we think about just the service index going forward? Thanks.

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

Yeah. While we have of course talk about the blow-by-blow issues we had that were weather related. And one thing I'll point out about that is that not only did we get the heavier that usual snowfalls, but we got the weather disruptions in areas where we typically don't get them. So when we loaded volume on top of that, it was pretty disruptive. But the network as a whole is coming back nicely. We really started to break on that about the middle of March. And we concentrated heavily on our intermodal network, getting it back where we needed it.

Where the on-time performance and the throughput is particularly critical, and then in the last month or so, we have really been going after the general merchandise network. And of course, we concentrate on our hump yards as far as -- as far as getting our outbound performance where it needs to be, and those numbers keep coming up. So the overall outbound performance of our trains will continue to improve, and that server seeing some improvement now.

Scott Malat - Goldman Sachs - Analyst

So then if we -- if we exclude I guess the first quarter results as we look back and kind of dissect looking back would have been third quarter and fourth quarter, were the service index declines at that point due to intermodal, and that's what you now addressed?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

You know, one point aggregate, and we had a lot of discussion about the -- our service in the third and fourth quarter. One of the things is that we saw there, which is something we saw in March was when you look at our low point in volumes last year, which was in May, and you look at our high point in October, which there was a 20% Delta in carloads. So we were in that third and fourth quarter also trying to react very quickly to what were unusually strong surges in traffic for the way our network usually runs.

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So I think that had some significant amount to do that. The other thing I would say about our service index, which is slightly different from other folks, is when we look particularly at on-time train performance, which is part of the index, we try to measure every train. I mean, we schedule coal trains, we schedule grain trains, we schedule every train that runs across the network. And I'm looking at our numbers right now, for example, for our merchandise and our intermodal trains, and really there was almost no difference in performance first quarter of 2009 to first quarter 2010, where we really saw some degradation was in the bulk network, the coal and the grain network. And as we said, before we got behind on coal because we had a lot of receivers who couldn't take coal because it froze up and our southern receivers didn't have thaw sheds. So I would say as Mark had said, there's just a lot of moving parts to this. We've done a lot of analysis, and we are confident that we are A, maintaining the service levels on our most service sensitive traffic, but B. getting the network spool back up as well.

Scott Malat - *Goldman Sachs - Analyst*

Okay. That's really helpful. Thanks. When just quick follow-up on the pricing stuff, and I don't want to harp on this, but was there a legacy contract that was renewing in the first quarter? I thought that I had that in my notes for this quarter.

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

No.

Scott Malat - *Goldman Sachs - Analyst*

That was not. Okay. So how much legacy do you have left?

Wick Moorman - *Norfolk Southern Corporation - Chairman, Pres. and CEO*

We have very little legacy impact letter the one legacy contract that I mentioned was the automotive contract, and we renegotiated that in the fourth quarter of 2009. Effective January 1. And we will see some impact on automobile volumes in that service network as a result of that redesign.

Scott Malat - *Goldman Sachs - Analyst*

So that was reset on January 1, which is where you get the benefit in the first quarter, right? Thanks.

Operator

Our next question comes from the line of Justin Yagerman with Deutsche Bank. Please proceed with your question.

Justin Yagerman - *Deutsche Bank - Analyst*

Hey, good afternoon. I basically wanted to get a sense of where you guys are, and you talk a little bit about service levels in your intermodal network right now. I remember back in the fourth quarter, I think it was JB Hunt's investor Day talked about you guys being in the low '80's, and on the West Coast seeing low to mid 90's type of on-time service levels. And we were very optimistic about it as the intermodal corridor projects they have underway are going on. That the on-time service had obviously improved over time. So I guess I wanted to get a sense of where you are now, where we should expect it to go by the end of the year, and I guess a long side of that, an update on where you are with some of these corridor projects that you have underway.

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Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

As far as our service performance goes, but we speak to his our composite performance. And that includes all of our different business groups. But the intermodal has it continued to improve performance in both our premium as well as our standard intermodal has continued to improve performance. And that's been ongoing ever since March. And we continue to see it now. So the velocity is increasing.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

In terms of the corridor projects, Heartland is still on schedule. It should be completed third quarter of the year. Our big Crest Quarter initiative, as you know, is underway. We received significant funding from the Tiger grant, \$105 million. We had the process well under way to get the permitting and get construction started on the two big intermodels or actually the three big intermodal terminals at Memphis, Birmingham, and Green Capital, Pennsylvania. Our Pan Am southern project in terms of the track upgrades is largely done. We have seen a big improvement in consistency and transit time up there. So we feel very good about all of our corridor projects right now, particularly as they relate to the intermodal network, certainly the Meridian Speedway is running well. And I think that we and JB Hunt are very confident in the level of our service both today and in the improvements we're making on a go forward basis.

Justin Yagerman - Deutsche Bank - Analyst

Thanks. I appreciate the update. Mark, the efficiency data that you went through, and that scorecard was pretty impressive. And I guess, you know, when I think about what's going on in this cycle versus past cycles, one of the biggest things I would jump out at me would be maybe some of the technological advances that you guys have put into place. Can you talk a little bit about, you know, when you are doing your train start planning, what's change, maybe as you look at this, you know, recovery versus last in terms of tools that you're using to decide and make those decisions in terms of deploying assets?

Mark Manion - Norfolk Southern Corporation - COO

As we change the operating plan in order to meet the volumes, whether they are volumes that are decreasing or volumes that are increasing, we use technology that we've had now for several years, which is operating plan developer, OPD. And it's been extremely helpful. What was a very laborious manual task in the past is something that we use our computer modeling and capability for in order to understand the impact of the changes we make. In other words, as we decide to make a change in train design, we can see what impact that we'll have in terms of the number of handlings to the traffic, the number of miles that the individual shipments will make, as well as the overall cycle time. And so we make the changes in a way that's not disruptive to the railroad. It's not costly. When we sized the train plan, and so OPD has been extremely helpful, and that helps us from the standpoint of customer service and it also helps in terms of cost control.

Justin Yagerman - Deutsche Bank - Analyst

Thanks. Appreciate the time.

Mark Manion - Norfolk Southern Corporation - COO

Thank you.

Operator

Our next question comes from the line of Matt Troy with Citigroup. Please proceed with your question.

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Matt Troy - Citigroup - Analyst

Thanks. A quick one for Jake on the housekeeping side. PTC, and when we blasted our update on PTC, I think you guys said you expected to spend more than \$700 million total for the project. And \$40 million of that being carved out as expected 2010 capital outlay for PTC. Any update to that or are we still in the ballpark with those figures?

Jake Allison - Norfolk Southern Corporation - VP and Controller

We have updated those figures, Matt. The \$700 million is still there. We have added to the \$700 million in additional \$400 million for costs we're going to have to bring forward by the PTC deadline in order to make the 2015 PTC deadline. So our total number is around \$1.1 billion.

Matt Troy - Citigroup - Analyst

Okay. That bring forward is on the backend this year? Are still expected to be in that \$40 million or so range?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

If you look at when we made the analysis, and this is the analysis, I think, that all of the big carriers have made on what needs to really be done, in addition to just installing the pure PTC technology, we kind of also took a look at what we're spending this year in CapEx and these other arenas. And I think the number, Jake, is closer to \$80 million. All in. That's not an increase to what we announced, it's just we categorized that additional \$40 million as money that's part of this \$400 million.

Matt Troy - Citigroup - Analyst

Okay, got it. Second question, I guess for Don, we would theoretically be moving into a sweet spot for intermodal. You've got fuel and prices creeping back up. Everyone's frenzied about a potential PL capacity crunch. You've got the consumer returning, although not like it was two years ago, but it seems like we're triangulating or it's a good potential multiyear run in intermodal shared gain off of highway. I get a conceptually, but I was just wondering if tactically you could talk about what you folks are doing, how you are inserting your salesforce to go out and chase this business. As we all know, it doesn't just walk in the door. If you could help us in terms of tactically how you go out, ring the bushes, and bring some of this business onto rail?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Thanks. That's a good question. It's an effort that we've been pursuing for quite sometime, laying the groundwork for this next phase of opportunity. And if you look at 2009, our domestic intermodal, and we pointed this out in the January call, was flat for the year in a very tough downturn recessionary environment.

In the fourth quarter, that business expanded by 5%. And then in the first quarter of this year, as we just reported, the domestic intermodal business grew by 23%. And we are seeing that actually accelerate in April. So I think that one, the results show that we are well-positioned and we have been working at that avenue extensively leading up to this hopefully more favorable phase of the economy and the opportunity. Number two, we've been making the investments in our network, as we've discussed with respect to the quarters, and number three, we have been working diligently with our intermodal partners to position ourselves properly. And we're spending -- number four, we're spending a lot of time with beneficial owners that actually received the intermodal freight. Getting the intermodal product in front of them, and that's the major big-box stores, chains, on the domestic side. And of course, also the shipping industry on the international side.



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Matt Troy - Citigroup - Analyst

Thank you. That's helpful. Are you seeing interest in reverse inquiries, given more fuel as the essential capacity folks are being more proactive in reaching out to you as a railroad? Or is it still pretty much still a sales and educational effort? Are you seeing that reverse inquiry yet?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I think we're beyond the education phase. I think intermodal has run beyond that point, and the awareness of the intermodal product in North America is very good. We have a lot of customers that have sustainability programs underway, and the environmental aspect of intermodal, in addition to the economic aspects of intermodal, our dual objectives that those companies have to increase the percentage of rail. And intermodal is certainly in the mix, and the awareness of that is very high at the beneficial owners.

Matt Troy - Citigroup - Analyst

My point being that fuel NTL capacity at the margins should be an incremental help going forward. But the numbers speak for themselves. Thank you very much.

Operator

Our next question comes from the line of Chris Wetherbee from FBR Capital Markets. Please proceed with your question.

Chris Wetherbee - FBR Capital Markets - Analyst

Great, thanks. Good afternoon, guys. Just two quick ones here. First on the headcount side, can you give us a sense of what headcount looked toward the end or at the end of the quarter as we kind of look at that surgeon volumes that you guys had in March and how you were able to manage that given your current resources?

Wick Moorman - Norfolk Southern Corporation - Chairman, Pres. and CEO

We're going to scramble around and see if we can find the marks on that.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I can do that. The end of March headcounts were fairly comparable to what you're seeing for the first quarter averages. Ever so slightly above, as we were hiring throughout February and March. But very comparable to what you're seeing for the averages.

Chris Wetherbee - FBR Capital Markets - Analyst

Okay. And is there a sense that hiring up is going to continue in April as you are seeing the trend move in a positive direction?

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Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Yeah, I would anticipate because we think we are going to have to get some folks trained and in the pipeline because we've really worked through so many of the furloughed people just because of attrition, that you're going to see our numbers go up just a little bit, and it's just going to reflect trainees.

Chris Wetherbee - FBR Capital Markets - Analyst

Okay, that's helpful. Appreciate it. And one quick follow-up, it may be down on your side for fuel, just thinking about kind of the XCap for the fuel escalator component. As you move into the second quarter, just the benefit of that and what that might kind of be as it impacts overall core pricing on a sequential basis?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, with respect to the RCap, the projected RCap has been published for the second quarter. And while we saw 1.6% increase in the first quarter, that projection is 24.7% for the second quarter. So we will see the RCap significantly higher in the second quarter. And we will see the fuel impact continue to move upward as oil prices and diesel fuel prices have increased.

Chris Wetherbee - FBR Capital Markets - Analyst

Okay. Thanks very much for your time. Appreciate it.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Thanks.

Operator

Our next question comes from the line of Gary Chase from Barclays Capital. Please proceed with your question.

Gary Chase - Barclays Capital - Analyst

Hello, everybody. Wanted to clean up a few quick things. Two for Jake and maybe one for Don. Jake, you mentioned that within that recovery in purchase services from the freight car supplier that there were some offsets. Was there anything major in their that we should understand? I think the comment you made was that it was principally offset by other factors.

Jake Allison - Norfolk Southern Corporation - VP and Controller

You know, I mentioned the offset there due to higher expenses from haulage. The haulage was the primary asset. We have some new haulage arrangements and some increased volumes there, increasing the haulage expenses.

Gary Chase - Barclays Capital - Analyst

Of the \$34 million that you saw in increased, you know, stock-based an incentive comp for the quarter, how much of that should we roll forward into the coming quarters?



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Jake Allison - Norfolk Southern Corporation - VP and Controller

Gary, that's a little bit like reading tea leaves, but our best estimate going forward is that the head wind in the second quarter for stock based and incentive comp is going to be about \$30 million. The stand alone effects within third and fourth quarter we think are negligible.

Gary Chase - Barclays Capital - Analyst

Okay. And then for Don, I just want to clarify, you said that you expected auto volumes to be, I think you said, slightly positive. Presumably that was versus the prior year. And just curious if you -- the issue with Ford and the 33,000 annualized carload count, is that something that was in full effect in the first quarter or is it something that's taking effect as we enter the second?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

The answer is that started in the first quarter. And we will see that effect each of the quarters of the year of 2010. And with respect to the first part of the question, yes, we're talking about year-over-year comparisons because not only did we have the 33,000 loads that will not be moving in and out of the former mixing service centers, but we've also got 11,000 loads that I mentioned that won't be in the network that was overhead traffic associated with that service network as well.

Gary Chase - Barclays Capital - Analyst

Okay. And that was in full effect for Q1?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Correct.

Gary Chase - Barclays Capital - Analyst

For all of Q1. Okay. Thanks very much, guys.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Thank you.

Operator

Our next question comes from the line of Anthony Gallo with Wells Fargo. Please proceed with your question.

Anthony Gallo - Wells Fargo - Analyst

Good afternoon. Thank you. My question is on the export net coal business. Are there any capacity constraint that you face? I guess it deals mainly with the ports. Can you just talk about that briefly?



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Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I heard the question with respect to capacity available for export coal, and we have added capacity at Lamberts Point. Our capacity, nameplate capacity there is about 35 million tons per year. We would need to adjust some manpower to handle that level of coal if the coal production was there to support it. So we feel very comparable that we have added capacity substantial additional capacity at the Port of Norfolk and we also have additional capacity at river terminals like Wheelersburg, Ohio, where we have capacity of about 9 million tons there and our run rate is about five.

Anthony Gallo - Wells Fargo - Analyst

And the follow-up, other any trade-offs that you need to make between the export net coal and the domestic net coal? Are they somewhat different calls on your resources?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I don't think there's any trade-offs there. They are similar coals. They are in great demand. And I think that as the steel industry ramps up domestically and the steel industry continues to ramp up internationally, the coal supply and coal production will be the question marks.

Anthony Gallo - Wells Fargo - Analyst

Fantastic. Thank you.

Operator

Our next question comes from the line of Jon Langefeld with Robert W. Baird. Please proceed with the question.

Ben Hartford - John W. Baird - Analyst

Hi. This has Ben Hartford in for John. I just wanted to focus on the intermodal side. The list price increases that are going to be coming into effect in the second quarter, can you tell us how much of a businesses does apply to?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, Ben, as you know, we have a general rate increased announced on the intermodal. I can't get into what that applies on and what that amount is here in the call. But we are seeing intermodal demand pick up and capacity drop in the truckload sector. And we think that's going to continue to be good for pricing ahead. So our general rate increase that we've announced effective May 1st reflects that.

Ben Hartford - John W. Baird - Analyst

Okay. But in your view is the extent to which intermodal pricing can lead, typically truckload rates move higher than intermodal falls. Can intermodal -- is demand strong enough is capacity tight enough, these rate increases, can they lead improvement that we see in the truckload space?

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Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I can't really speculate on that.

Ben Hartford - John W. Baird - Analyst

Okay. And then I guess one last question. Can we see a second round of intermodal rate increases on the back half of the year, aside from these rate increases that are going in place in the second quarter? Meaning, can you get more than one round of rate increases in a given calendar year?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

It all depends on the continuation of the economic recovery, retail sales, the consumer themselves in terms of them being active in the market and their confidence.

Ben Hartford - John W. Baird - Analyst

Okay. And then one last one if I could, and a concern on your end of the availability of containers as you move to the balance of the year given the tremendous amount of growth that you've realized in domestic intermodal?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Certainly we see container supply tightening. And if we continue to see the trend upward, which we, in April we are certainly seeing that. We are somewhat cautious about declaring victory for the year, because we still have those clouds that have to clear up. But I certainly would say that we are seeing a tightening of the container fleet in the domestic market through North America.

Ben Hartford - John W. Baird - Analyst

Okay, great. Thanks for the time.

Operator

Our next question comes from the line of John Larkin, with Stifel Nicolaus. Please proceed with your question.

John Larkin - Stifel Nicolaus - Analyst

Good afternoon, gentlemen. I had a question on the utility coal, a picture, I think Don, you had mentioned that some of the utilities, particularly in the Southeast were down to something in the order of eight to 10 days surplus inventory. If we have a normal spring and summer burn, when we do anticipate that they would bring their deliveries back to what I would call more of a normal level?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

I think there are two dynamics there. One, the weather pattern in terms of the shorter month burned, but also the continuation of the increase in industrial demand for electricity. We're seeing an increase in electrical production and our service territory was up between 6% and 7% for the quarter. Part of that is driven by an improving economy. So if we get normalized weather



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patterns, continued economic improvement, we certainly think that by June, by late May or June, we're going to see increased utility activity. In fact, we're already beginning to see some activity in the northern region of our network in the month of April.

John Larkin - *Stifel Nicolaus - Analyst*

That's terrific color. Also in your comments, you had mentioned on a couple of occasions that there were some projects that were going to help fuel the car load growth here as we work our way through the year. I think you touched on ethanol projects. Are there any other meaningful projects that will be coming on stream in terms of new plants, auto or otherwise, that will be coming on stream later this year?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

We have several automotive plant expansions that will help us as we move forward, both on inbound parts as well as finished automobiles, as well as steel for stamping. Stamping activity as auto production continues to improve, hopefully. Ethanol is certainly a growth market for us and we are continuing to expand our distribution network. We're also seeing a lot of activity with respect to natural gas production. With sand, chemicals, etc. for that type of project work as well. And then we continue to have a rather large project, hauling a flash from TBA of Kingston, Tennessee to a disposal site. So that type of activity, those projects will continue to bolster volume.

John Larkin - *Stifel Nicolaus - Analyst*

Are they already in full swing now or will they be kicking in later in the year?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

They are already moving.

John Larkin - *Stifel Nicolaus - Analyst*

Thank you. And lastly, maybe on intermodal, terrific growth in the domestic piece of the business, up 23% year-over-year. And I was wondering how much of that do you think was due to the new JB Hunt agreement that you entered into last year? How much of it might be due to some of the early stages of the corridor improvement programs, and how much of it was just due to the old-fashioned rebounding economy?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

All of the above is the proper answer. We saw growth in all of our intermodal partners, and we are also seeing some early returns from our corridor work.

John Larkin - *Stifel Nicolaus - Analyst*

So presumably the growth would have been a little less without the Hunt agreement and without the quarter work?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Well, I think it took everyone to generate that type of increase. And we saw it across the board.

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John Larkin - *Stifel Nicolaus - Analyst*

Got it. And then on the intermodal pricing increase that is anticipated here in the near term. What kind of feedback have you gotten from you're third-party partners, particularly the IMC's in terms of their ability to pass that through to their customers?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Well, in our deliberations with our intermodal partners, they are seeing the same thing we're seeing, and that's improving dynamics in the freight market as demand continues to pick up and capacity is diminished.

John Larkin - *Stifel Nicolaus - Analyst*

If they have trouble passing that price increase along, would there be any second thoughts on your part to perhaps being a little less aggressive?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Well, I don't think we're at that point of having that discussion.

John Larkin - *Stifel Nicolaus - Analyst*

All right. Well, thank you very much for the color.

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Thank you.

Operator

Our next question comes from the line of Ken Hoexter from Banc of America Merrill Lynch. Please proceed with your question.

Ken Hoexter - *Banc of America Merrill Lynch - Analyst*

Great. Good afternoon. I just want to follow on John's question there on the coal site. Are you already seeing because of the -- do see any dynamics with the export coal really starts to take off, the utilities feel the need to maybe reserve their train sets and keep up ordering? Are you seeing any of that as the exports start to improve?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Ken, I certainly could see that developing. We expect the export market to stay strong for the year. We expect domestic net coal to stay strong for the year. And as utilities reenter for replenishment -- reenter the market for replenishment, we will see that activity develop.

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Ken Hoexter - Banc of America Merrill Lynch - Analyst

Okay. What level capacity do you think -- I just kind of want to understand, I know you have the Heartland and the Crescent Quarter programs going on, but how much capacity do you have on your network before you start need to increasing some of the capacity they so what's left in storage?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

You know, it's hard always to come up with a number. Capacity comes in many shapes and forms. But I think if you just look at historically what we've handled over the past few years, the numbers that Mark gave you, I think we are confident that we have a significant amount of capacity remaining.

Ken Hoexter - Banc of America Merrill Lynch - Analyst

All right. And you're in region competitor announced a revised agreement with one of the western rails in intermodal. Is that shifting any out, or is enhancing maybe flows of intermodal volumes in any way? Do you see any reaction from that?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

You know, we really don't speculate too much about what the other folks do. And I would just say we really haven't seen any impact in the marketplace in particular.

Ken Hoexter - Banc of America Merrill Lynch - Analyst

Okay. And then lastly, I saw on your safety chart, the one that Mark put up, I guess you've moved into second place. Is that -- is there something structural there, anything that you want to focus on? Did anything occur in the quarter that shifted that ranking?

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

No, not at all, Ken. You know, first of all, we're going to see the whole industry keeps getting better. We're going to keep our focus on it just as we always have, and our aim is to get all of our employees home safely at the end of their workday. So we've got good strength and our safety process, and we will keep that up.

Ken Hoexter - Banc of America Merrill Lynch - Analyst

So just to clarify, is that others moving past you, or did your rankings, your levels of move up a bit? At the end of the quarter, not a trend view.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, the 1.7 that we have reported for this first quarter is not as good as our first quarter last year, 1.02. But frankly, we had a good March. We've got a lot of strength in the process. So there is nothing of a systemic issue that would be a problem.

Ken Hoexter - Banc of America Merrill Lynch - Analyst

All right. Thanks for the time.

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Operator

Our next question comes from the line of Jeff Kauffman from Sterne Agee. Please proceed with your question.

Jeff Kauffman - *Sterne Agee - Analyst*

Thank you very much. Congratulations. Most of my questions have been answered, so let me just fire a quick cash flow question at Jake. Jake., the first quarter operating cash flow operation was terrific. But when I break it down, non-net income, it looks like there was about \$330 million, \$340 million that was classified as income taxes payable and other net. Could you give me an idea of what made that up and whether some of that reverses in terms of trying to forecast free cash the year, or if there's something that's changed in the operating cash flow as this continues to drive?

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

Okay, Jeff. There are a couple of things going on in cash flows that are bolstering the operating cash for the first quarter. We did reach a settlement related to one of our insurance claims situations. That's helped bolster -- that's a one-time event for first quarter 2010. The income tax, as you're aware, income taxes are paid April 15, our estimated taxes paid April 15 for the first quarter. That is a fairly sizable benefit over last year.

Jeff Kauffman - *Sterne Agee - Analyst*

That's about \$140 million for the income tax. How much was the insurance claim to the extent you're comfortable ballparking it?

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

The settlement's confidential.

Jeff Kauffman - *Sterne Agee - Analyst*

Okay. Well when I'm looking at the other \$200 million, then what else would be making that up? I'm just trying to figure out the timing issues versus consistent cash flow.

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

Jeff, the \$200 million or so that you're talking about are really events that occurred in the first quarter 2009.

Jeff Kauffman - *Sterne Agee - Analyst*

So it's just a converted issue, last year versus this year. Okay, guys. Thanks so much and again, congratulations.

Jake Allison - *Norfolk Southern Corporation - VP and Controller*

Thank you.

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Operator

Our next question comes from the line of Carter Leake with Davenport & Company. Please proceed with your question.

Carter Leake - *Davenport & Company - Analyst*

Just two quick follow-ups on net coal. The first one is do you think you can be at or near the 2008 volume levels, and second, is there an easy comp our of Baltimore that explains the 125% increase?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

Well, certainly, with respect to the Baltimore portion of the question, we've had weakness in export last year and were coming off comp that are pretty favorable to all business this year. Our export markets started to pick up in the third and fourth quarters last year, and as we pointed out, we had a terrific fourth quarter, the best we've had in 10 years. So the Baltimore and Lamberts Point tonage at this point benefited from comps that weren't robust last year.

Carter Leake - *Davenport & Company - Analyst*

And then on 2008 volumes, I'm not sure if you have commented on that before or if I heard that elsewhere, but on net coal exports, if you have commented before --

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

We have not reached 2008 levels, volumes across our network yet. In some of that was obviously export coal this quarter and in the fourth quarter we exceeded 2008 levels. But we still have room to go before we reach 2008 levels.

Carter Leake - *Davenport & Company - Analyst*

Okay, great. Thank you.

Operator

Our last question comes from the line of Peter Pickral from Stephen's Inc. Please proceed with your question.

George Pickral - *Stephen's, Inc. - Analyst*

Hey. This is George Pickral. A follow-up on your capacity question. Just to make sure I understand it correctly, as we stand today, based on what you're seeing in terms of your demand trend. Do you think is going to be a need to order new cars this year? Where are we still in a situation where we could work through the 10,000 or so that you have storage?

Don Seale - *Norfolk Southern Corporation - Chief Marketing Officer*

We don't have any plans to order any cars this year. And as I say, I think we're comfortable that we have more capacity. Mark?

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Mark Manion - Norfolk Southern Corporation - COO

Absolutely. And keeping in mind, we're nowhere near 2006 levels. And since 2006, each year we have continued -- we've added infrastructure, we've added flexibility, and so a lot of room to grow.

George Pickral - Stephen's, Inc. - Analyst

Perfect. Thanks for the clarification there.

Operator

I'd like to hand the call back over to management for closing comments.

Don Seale - Norfolk Southern Corporation - Chief Marketing Officer

Well, thank you very much, everyone, for your time and your patience and we look forward to talking with you next quarter and seeing a lot of you in the interim. Many thanks.

Operator

Ladies and gentlemen, this does conclude today's conference. Thank you for your participation. You may disconnect your lines at this time and have a wonderful day.

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