Norfolk Southern Corporation NYSE:NSC

FQ1 2024 Earnings Call Transcript

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Presentation

Operator

Greetings, and welcome to Norfolk Southern Corporation's First Quarter 2024 Earnings Call. [Operator Instructions] As a reminder, this conference is being recorded. It is now my pleasure to introduce Luke Nichols, Senior Director of Investor Relations. Thank you, Mr. Nichols, you may now begin.

Luke Nichols
Senior Director of Investor Relations

Thank you, and good morning, everyone. Please note that during today's call, we will make certain forward-looking statements within the meaning of the safe harbor provision of the Private Securities Litigation Reform Act of 1995. These statements relate to future events or future performance of Norfolk Southern Corporation, which are subject to risks and uncertainties and may differ materially from actual results. Please refer to our annual and quarterly reports filed with the SEC for a full discussion of those risks and uncertainties we view as most important.

Our presentation slides are available at norfolksouthern.com in the Investors section, along with our reconciliation of any non-GAAP measures used today to the comparable GAAP measures, including adjusted or non-GAAP operating ratio. Please note that all references to our prospective operating ratio during today's call are being provided on an adjusted basis as referenced in our earnings release. Turning to Slide 3. It's now my pleasure to introduce Norfolk Southern's President and Chief Executive Officer, Alan Shaw.

Alan H. Shaw
President, CEO & Director

Good morning, everyone, and thank you for joining Norfolk Southern's First Quarter 2024 Earnings Call. Here with me today are Mark George, our Chief Financial Officer; Ed Elkins, our Chief Marketing Officer; and our new Chief Operating Officer, John Orr. I am excited to have John on the Norfolk Southern team. John is a 40-year railroad industry veteran and a proven PSR expert who has worked with Hunter Harrison, Claude Mongeau and Keith Creel to implement PSR railroads across 3 countries.

I promised you that we would focus on productivity in 2024, and we're taking action to do just that. Bringing in someone of John's caliber was another step to accelerate our operational improvement. John is going to share the progress in our operating metrics that he and his team are already driving and his plans for furthering productivity in our merchandise network to deliver immediate margin enhancement. Our strategy is about balancing service, productivity and growth with safety at its core.

This strategy is anchored on a PSR-driven operating plan and designed to deliver top-tier earnings and revenue growth with industry competitive margins. When we say industry competitive margins, it has to be within 100 to 200 basis points of the industry average.

Let's recall where we've been and discuss our path forward. Last year, in response to East Palestine, we prioritized investments in safety and service to protect our franchise and our shareholders, and we delivered on both fronts. We are operating one of the safest networks in North America and are producing service levels better than anything we've seen since 2019.

Despite that progress, more work remains to be done to get us back to industry competitive margins. We were not delivering the productivity, and we were not running fast enough or efficiently enough. I needed to make changes to accelerate our progress and to introduce greater operational discipline into our culture. To that end, we started making organizational and process changes last fall, culminating with the recent hiring of John Orr.

Now we have safely built the foundation to drive substantial gains in productivity, and we've committed to a 400 to [450] basis point OR improvement in the second half of this year. We will close that margin gap with peers. We will deliver a sub-60 operating ratio in the next 3 to 4 years, and we will do it at a safe, sustainable manner that recognizes our current operating environment and brings key constituents, including our shareholders, customers, employees and regulators along with us on our mission.

We will urgently deliver productivity through disciplined operational excellence that continues to safely serve our customers, positions us to grow by meeting markets as they evolve and allows us to generate outsized returns for our shareholders. I'll now turn it over to Mark to review our first quarter financial results.

Mark R. George
Executive VP & CFO

Thanks, Alan. As seen on Slide 5, our GAAP results in Q1 were impacted by 4 items that we've called out for you. Earlier in the month, we announced the $600 million agreement in principle to resolve a consolidated class action lawsuit relating to the East Palestine derailment. That addresses the most significant remaining legal exposures for our shareholders.

Including other cleanup costs and insurance recoveries in the quarter, our operating income was adversely impacted by $592 million. You'll note at the bottom, another $108 million of insurance recoveries in the quarter. That brings our recoveries to date in excess of $200 million toward our $1.1 billion insurance coverage tower.

Moving to the right. We told you last quarter about our initiative to drive a 7% reduction in non-agreement headcount, for which savings will begin to materialize in Q2. That initiative, along with our operations leadership change resulted in a $99 million charge. Next, our advisory costs associated with our now very public shareholder matter recorded in nonoperating. Finally, we also called out here a favorable deferred tax adjustment affecting our income tax expense. For the remaining slides, I'll speak to our adjusted results, excluding these items, as shown here on the far right.

Moving to Slide 6, let's focus on the adjusted variances compared to Q1 of 2023 in the year-over-year columns. Those results were impacted by 4% lower revenues driven by meaningfully lower fuel surcharge as well as headwinds in Intermodal that Ed will detail later. Operating expenses were up 3% from inflation and the increased workforce. You'll see an OpEx year-over-year waterfall in the appendix that provides more detail.

Not on this page is nonoperating income, which was down $17 million from lower gains on our company-owned life insurance. That decline, coupled with the lower operating income drove the net income and EPS reductions you see here on a year-over-year basis.

Let's talk on the right side about the sequential variance from Q4 2023, where we guided to a 100 to 200 basis point deterioration in our OR, which is in line with normal seasonality. That's exactly where we landed right at the lower end of that range. On the next couple of charts, we'll detail the sequential revenue and OpEx walks from Q4.

So revenue here on Slide 7 moved down sequentially driven by fuel surcharge headwinds and overall lower volumes driven by coal and Intermodal. Coal pricing was weaker and Intermodal faced difficult conditions with volumes down 3% and continued adverse mix from softness in our higher-yield premium business.

Slide 8, turning to our operating expenses. They were down 1% as compared to Q4. We faced typical sequential headwinds associated with the reset of payroll taxes, and we had meaningful headwinds from returning to normal incentive compensation accrual levels as well as no property sales in the first quarter. We offset those headwinds by lower spend in purchased services, efficiency gains in comp embedded as well as favorable fuel prices.

While fuel expense was down 6% sequentially, recall that surcharge revenue was down 17% sequentially, and that drives a 40 basis point OR headwind on a sequential basis. As we turn to the balance of the year, we will see our margins improve materially from here. We are finally starting to see excess service costs unwind and they will accelerate downward in Q2. That trajectory, along with the reduction in non-agreement headcount as well as other productivity initiatives leave us confident in a strong productivity story for Q2.

We anticipate a modest seasonal volume lift sequentially, although there is some pressure to our Coal business from the Baltimore Bridge disruption. Despite the port closure, we still believe we will be within the first half 67% to 68% OR guidance range, assuming that the channel reopens at the beginning of June. The revenue impact from the channel closure is in the $25 million to $35 million per month range. More productivity momentum builds in the back half as well as stronger volumes, and that provides us with confidence in the 400 to 450 basis points of OR improvement. John will talk more about the productivity runway in front of us. But first, I'll hand over to Ed to discuss revenues.

Claude E. Elkins
Executive VP & Chief Marketing Officer

Thank you, Mark, and good morning to everyone on the call. Starting on Slide 11, I'll go over our commercial results for the quarter. Overall, volume grew by 4% versus last year, driven by Intermodal. Revenue for the first quarter came in just above $3 billion, down 4% year-over-year as total RPU fell 8%.

Starting with merchandise, volume was flat versus last year, while revenue ticked down 1% driven by lower fuel surcharge revenue. RPU less fuel increased by 3% year-over-year setting an all-time quarterly record, which also led to a new all-time quarterly record for revenue less fuel. This marks the 35th out of the prior 36 quarters that merchandise RPU grew year-over-year, and once again, reaffirms our commitment to price and the increasing value of our service.

Turning to Intermodal. Volume grew 8% year-over-year, primarily on strength in International. However, revenue decreased 8% as RPU excluding fuel and storage and fees declined by 6% overall. Revenue was also impacted by the lane rationalization across Intermodal that simplified our network. This decision demonstrates how marketing, operations and finance are aligned to increase productivity and drive smart and sustainable growth.

Digging into coal, volumes for the quarter declined by 4% as weakness in the utility market was only partially offset by export strength driven by a historically strong export quarter as our cross-functional efforts to boost throughput at our Lamberts Point terminal yielded positive results. These results are a great example of NS pulling together to deliver strong value for our shareholders and for our customers.

Let's move to Slide 12, where I'm introducing a new view of our results that helps frame the main first quarter drivers of revenue and revenue per unit. Overall, fuel surcharge revenue was the single largest headwind in the quarter, declining by $115 million.

The first quarter was also the last one where Intermodal storage and fees are a substantial year-over-year headwind with revenues declining by $35 million. In Coal, we experienced positive mix from higher export volumes and higher utility shipments in the South. This positive mix was more than offset by lower realized price and export shipments as seaborne coal prices weakened significantly throughout the quarter.

Merchandise revenue, excluding fuel, was driven higher by pricing gains across the entire book. Overall pricing and volume increases in our metals franchise were boosted by improved network fluidity from increased car velocity. That same velocity and fluidity helped volumes in automotive remained flat despite manufacturing headwinds at several of the plants that we serve.

Intermodal revenue, excluding fuel and storage and fees increased as higher volumes more than offset adverse mix and continued slight capacity in the domestic truck market created headwinds to RPU. Higher international shipments and lower domestic premium shipments were the main drivers of adverse mix. Additionally, RPU was impacted from higher international empty shipments as these grew 57% year-over-year in the quarter. We believe elongated ocean transit times are a driving factor pushing ocean carriers to deploy their capacity back on the water as soon as possible, which increases the need to reposition empty containers back to the ports.

Turning to Slide 13. Let's go over our market outlook for the remainder of '24. The macro landscape presents a mixed bag with uncertainty regarding inflation and future Fed rate actions overshadowing the recent recovery in manufacturing. However, our improving service product places us in an excellent position to capitalize on growth opportunities.

Starting with our view on the widely varying merchandise markets, we generally see support from volume from the normalization of auto production and the continued strength in infrastructure projects across our network. A positive price environment will continue, which is supported by the increase in network fluidity. Improved cycle times, equipment availability and network velocity will be a broad positive tailwind across our portfolio and merchandise. And we also expect to drive incremental volumes through project development, such as our recently announced Great Lakes reload acquisition, the merger of TDIS into Triple Crown Services and continued industrial development wins.

Intermodal volumes are increase as international trade remains robust. We expect continued mix impacts from higher international empty shipments as geopolitical tensions remain elevated, but a weak truck market continues to drive stubbornly low truck rates, which will dampen domestic nonpremium Intermodal pricing. Additionally, we expect volumes in our domestic premium business to fall as challenging LTL market forces reduced freight demand for parcel shipments.

Finally, coal volumes will be challenged as high stockpiles and low natural gas prices reduce utility shipments. In addition, export shipments will be affected by the Baltimore port shutdown. We are diligently working with our customers to provide alternate supply chain solutions, and the increased network fluidity is providing the capacity necessary to execute on those solutions.

Finally, seaborne coal prices have weakened as supply has outstripped global demand and this headwind is expected to continue throughout the remainder of the year. Before I turn it over to John, I'd like to close by making our customers for trusting Norfolk Southern to move their freight.

John F. Orr
COO & Executive VP

Thank you, Ed. I arrived at NS in late March and immediately got to work immersing myself in the operations and connecting with our people. I've had boots on the ground assessing terminals and engaging craft colleagues and frontline supervisors. I've also met with our stakeholders from labor, regulatory and community leadership. What I've seen confirms that NS is a robust franchise with a talented team and the resources to deliver impressive results when properly executed. Our safety performance as shown on Slide 15,

has trended favorably. I have observed a strong safety commitment, and we are building on that. My first action as COO was a system safety blitz to provide clarity around the value of safety.

Turning to Slide 16. It is imperative that we closed the profitability gap with our peers. We are now delivering encouraging trends in productivity. Our strategy is balanced. Our operating efficiency and service excellence are achieved in tandem. Our approach is a flywheel of value creation where people, processes and accountability intersect to drive performance, anchoring our service and profitability proposition. Accountability is key. We're providing our team with the metrics they need to track their performance.

In my first 30 days, we have removed approximately 200 locomotives from the available fleet. Most of these have gone into stored status or driven off-line for [indiscernible]. Our availability count is now below 2,500 units. As shown on the slide, we will be able to increase locomotive drawdown over the next 6 months. Terminal 12 has improved by 8%. We are driving more waste by fine-tuning workload in our terminals through disciplined planned execution. Near term, we are targeting 20% improvement.

Car miles have improved by 8%. And this is another productivity measure, we target for double-digit improvement. Recrews are trending down 22% as network and terminal improvements are combining to improve fluidity across the main line. And lastly, we are reviewing the entire train service plan. This will drive core rationalization in the range of 4%, resulting from these initiatives. We are driving out excess cost as we close the gap to our peers.

Referring to Slide 17, network update. To accelerate improvements and address network underperformance, I have established a network optimization team that identifies areas for immediate improvement. I have deployed 2 task force to drive field productivity and throughput at 2 major terminals.

The outcomes from these efforts will rapidly go out to scale throughout the network. We are training our operations leaders to think differently to make faster decisions and to eliminate waste more vigorously. My commitment is to develop PSR railroaders to instill the discipline for continuous improvement and to streamline execution by relentlessly managing assets in context to our commercial obligations. The initial results across the entire network have been promising. Our people are driving PSR results.

To create accountability and to track progress, we're introducing a comprehensive set of metrics. I've laid out challenging and urgent near-term targets, and I'm taking an aggressive disciplined approach to achieve our long-term financial glide path. And I can tell you, now we have a significant runway on cost reduction. As our fleet becomes more efficient, we benefit in rents and materials by shedding assets and from improving the fleet composition and getting out more costly cars.

Our locomotive fleet now has significant capacity. I believe we will be able to scale down discretionary capital spending on the fleet. And we have a robust terminal footprint, covering a rich array of industrial activity. And as we optimize our terminals, we are challenging the historic use to create value through consolidation and efficiencies. I am proud and excited to have the opportunity to lead the operations team at NS. I look forward to your questions, and I will turn the call back to Alan.

Alan H. Shaw
President, CEO & Director

Our strategy is designed to mirror the great success stories of the Canadian railroads who have recognized that PSR is about more than tearing a railroad down to its studs at slashing costs regardless of the fallout. As our Board member, Claude Mongeau, demonstrated when he was CEO of Canadian National, a PSR operating model, when part of a customer-focused balanced strategy, can deliver top-tier revenue growth and a sub-60 operating ratio. John Orr was an integral part of Claude's leadership team at CN and thus, a perfect fit from Norfolk Southern as we turbocharge productivity in pursuit of industry competitive margins and top-tier earnings growth.

Core to this are the men and women of Norfolk Southern. I'm incredibly proud of all they've done to progress the execution of our differentiated strategy. So my colleagues, thank you for everything you do for Norfolk Southern, our shareholders, our customers and your fellow team members. Together, we are on a transformational journey to a safer more profitable railroad, poised for growth with strong execution from an experienced leadership team.
We will now open the call to questions. Operator?

Question and Answer

Operator

[Operator Instructions]

Our first question comes from Brian Ossenbeck with JPMorgan.

Brian Patrick Ossenbeck
JPMorgan Chase & Co, Research Division

Just wanted to understand, going back to the Meridian Speedway concession. Does that actually have an impact? Or does that cover anything related to traffic originating or terminating out of Mexico? And then secondarily, maybe something for John or the team. Can you just give us some sense behind the underlying assumptions as you're benchmarking these productivity savings going down to 60 OR in the next 2, 3 years? And why can't you go there faster? What's holding you back from that? Maybe you can help with walking through some of the assumptions under your numbers versus what else we see out there?

Alan H. Shaw
President, CEO & Director

Thanks for the question, Brian. Let me be really clear. The agreement related to the Meridian Speedway is by no means a consequential concession, and it does not impact Mexico. We said it impacts the Dallas business, which is largely defined by abundant truck capacity. John, do you want to handle the second part of his one question.

John F. Orr
COO & Executive VP

Sure. Brian, nice to talk to you. And I'll tell you, I've been out assessing the network, and I'm really confident with the plans that I've got underway today that we're on track for the 400 to 500 basis points by year-end. And I'll tell you, our operating costs are a direct reflection of our asset management. And speed and accuracy are really essential to that. And our ability to rapidly cycle assets reduces our need for them, which is why we're focused on accelerating all of our operations simultaneously while taking out costs.

And I'm very confident with our dwell, our over-the-road performance, the discipline we put on our locomotive fleets and the crew productivity and some of the smart investments that we're making to unlock the value, we're well underway.

Operator

Next question is from the line of Scott Group with Wolfe Research.

Scott H. Group
Wolfe Research, LLC

So Mark, you're guiding 400 to 500 basis points of sequential improvement into Q2. Just help us think about the drivers there? How much volume? How should we think about cost ex fuel? And there's a lot going on with the proxy. So I do want to ask also, Alan. A, what's -- any expectation in terms of timing for ISS and then there is a lot of focus on this Meridian Speedway thing. It looks like there was another a second amendment that you guys filed yesterday. Any color on what that second amendment is?

Mark R. George
Executive VP & CFO

Yes, I'll start. First, I think the amendment was just really formalizing with the SEB who had requested that things get filed, the whole exchange that we want -- that we had the 8-K and some of the other stuff. They just wanted to see it formally filed. So we did exactly that. That's all it is, nothing new than what's already been communicated. ISS, we don't control it. We would imagine that comes out likely at the end of this week, early next week, but we don't know.

And with regard to the Q1 to Q2 walk, Scott, really, what we would expect here is kind of the modest seasonal volume increase that you typically would see going into the second quarter, call it 1 point or 2 of increased costs. But then I think you're going to really start to see the cost lines start to show relief here, especially in comp and ben. We've started to actually experience the unwinding of service costs in March, and that's going to really accelerate into the second quarter. And I think most of those will be gone by the end of the second quarter going into the third quarter. So we've made tremendous progress there.

In addition, we've got restructuring benefits, the reduction of the 300-plus non-agreement workers. Most of those have already left here in middle of April and there's a few more that leave at the end of May, but we're going to start really harvesting those benefits. And fuel is another area where we're going to see some benefits with efficiency.

John is very focused on that right now. And then, of course, we've got all of the other productivity stuff that's really starting to build. The productivity related to crew start savings, over time, car rents, things like that. So you're going to see it show up in a lot of the P&L lines, especially in com and ben.

Alan H. Shaw
President, CEO & Director

And Scott, recall in John's prepared remarks, you had a chart that said about $250 million in productivity over the next 6 months.

Operator

Our next question is from the line of Tom Wadewitz with UBS.

Thomas Richard Wadewitz
UBS Investment Bank, Research Division

Yes. Alan, I wanted to get your thoughts on, I guess, how -- you've had a pretty big change, obviously, the new COO, who is, John stated, been very aggressive. The team has been aggressive with taking locomotives out, changing the schedule. How do you think about the risks of that? Because I think your prior approach was something where you thought it would be better for customers to kind of have the resiliency approach. So I guess how do you think about the change in tack on operations and some of the risks of going that way and I guess also recognizing that before you kind of pointed to a lot of risks of being too aggressive on the -- I guess, on reducing people and assets?

Alan H. Shaw
President, CEO & Director

Tom, thanks for the question. Let me be really clear. We we're still focused on that same strategy that we laid out a couple of years ago. And that's that balance between service productivity and growth with safety at its core. And we made a lot of improvements last year in service. We made a safer road even safer, but we weren't delivering the productivity. We weren't running fast enough, and we weren't running efficiently enough.

And so I needed to make some changes, and that's what a CEO does. And I needed to accelerate our operational improvements, and we made a number of process changes and personnel changes starting last fall. Most recently, we hired John Orr and what John is doing is he's driving productivity and continued service improvements. And so that -- that's the balance of our strategy. That's what customers want. They want service and they want us to be productive. John, you got some thoughts on that?

John F. Orr
COO & Executive VP

Yes. And as I've said in my prepared remarks, they're not mutually exclusive. In fact, they're complementary to each other. And my approach is, as I evaluate the network, and restructuring our yard and local plans, what are basically on-ramps to our corridor that touch our service, touch our customers and creating efficiencies, new standards and accelerating through our current dwell times, making improvements year-over-year, but also making improvements on the individual cars and the handoffs on those cars, it drives performance.

And then the overall speed of the network picks up as there's more reliability. So that's why I talk to not only our craft employees and our frontline supervisors in my first few days, but also union leadership and the regulators to make sure they understood, we're going to go at a quick pace, give them a forecast of what we're doing. And I was very clear, even with our union leadership that I'm going to ask our people to do more, give them the resources, give them the training, give them the skills to do it.

But they're going to be stretched in ways that they'll be proud of in the coming years, and we're going to do it sustainably. We're going to grow a team of capable PSR-driven leadership and do it in a way that produces amazing results.

Operator

Our next question is coming from the line of Jon Chappell with Evercore ISI.

Jonathan B. Chappell

Evercore ISI Institutional Equities, Research Division

John, I want to follow up on a couple of things that have been touched on already as it relates to the things that you've done in the last 30 days. The volumes so far this quarter have been relatively strong for Norfolk Southern, on a year-over-year basis, [indiscernible] easy comps. But as you go through the next 6 months and you deal with things like laying off 300 more locomotives or reducing merchandise families by 10%, is there a situation where you don't maybe chase volume recovery as quickly as you would otherwise? Or it's more about getting the network where it needs to be and worrying about volume and I guess, the top line beyond that next 6-month period?

Alan H. Shaw
President, CEO & Director

John, why don't you talk about that? And then, Ed, why don't you talk about the market?

John F. Orr
COO & Executive VP

Yes. I think that the most imperative thing we can do is to close the gap on performance, reliability and drive the value of the network. As far as the capacity, we're unlocking capacity in the existing terminals by being more efficient, more effective and driving those on-ramps to the network more effectively. What are in that pipeline? We have ample capacity to grow more trains or grow longer trains to get yield out of that even a single line capacity.

So I don't see it as being one or the other. It's both. And whether or not the volume is there, depending on what the economy gives, we're going to drive performance, we're going to close the gap faster than anyone else. So Ed, I'll turn it to you.

Claude E. Elkins
Executive VP & Chief Marketing Officer

Sure. And you're absolutely right, John. We've seen volume so far this month and we're encouraged by that. Our customers are encouraged by the level of service that we're delivering. And to be clear, in Intermodal, the level of service we're delivering is the best in a generation and it's sustainable and it's going to continue to be that way, and we're earning trust from our customers to do that. We're seeing very good response on the bid front for new volume converting from the highway, which we're very encouraged by in Intermodal.

On the merchandise side, look, we spent the last 6 months building a sales conversion pipeline, which includes technology augmentation as well as institutional rigor and we are going to deliver growth from highway converting freight in the merchandise space that should be moving on Norfolk Southern. The capacity that John is unlocked and we're going to use to go out and get back the freight that should be ours.

Operator

Our next question is from the line of Justin Long with Stephens.

Justin Trennon Long
Stephens Inc., Research Division

I guess to follow up on some of the commentary about Intermodal. You've talked about rationalizing some lanes. I wanted to get an update on where you are in that process? Is that now complete? Or is there more to come? And then similarly or along those lines, thinking about these multi-year OR targets, how do you envision the mix of the business changing? Do we need to see a shift to more general merchandise freight? Or is that not necessary to hit these OR objectives?

Claude E. Elkins
Executive VP & Chief Marketing Officer

I'll talk about the Intermodal piece first. I think that was your first question. Look, we took a very, very disciplined view of our Intermodal network and did a couple of things. Looked at lanes that were very low density, looked at lanes that were not strategic in terms of their capability for our customers, and then thirdly, looked at lanes where we did not believe that there was going to be long-term growth potential that we have line of sight on.

Once we pass all those filters, we talked to our partners that were engaged in those lanes that includes our port partners and some others, and we made some tough decisions. It's about 15% of the Intermodal lane portfolio, but only about of the Intermodal revenue portfolio, which should tell you something about the density there.

Are we done? We're always looking at our network to make sure that we are applying our resources where the greatest growth potential is. And one thing that this exercise taught us is we can redeploy some of that capacity that we're freeing up toward our powerhouse lanes where we're delivering exceptional value for our customers.

Mark R. George
Executive VP & CFO

And I would say with regard to kind of the mix question. Intermodal is going to grow because that's where the growth is. We serve the consumers. But at the same time, merchandise has probably suffered more in the past couple of years from the service challenges we have. So just unlocking the network and doing everything that John is doing, should enable Merchandise to really return to better growth rates as we start to recover, and of course, that will help mix.

Claude E. Elkins
Executive VP & Chief Marketing Officer

Absolutely. And the -- as I said, the sales pipeline approach that we're taking has a very disciplined view toward conversion from the high labels in the Merchandise as well as the Intermodal space.

John F. Orr
COO & Executive VP

And I would say as far as capacity is concerned, we're improving execution and plan compliance, and that facilitates blocking deeper into our network, which ultimately increases car velocity, train speed and really drives performance. That applies to Intermodal, Merchandise and [Boat]. And we're actively engaging and challenging every asset that we've got out there. Just in the last 30 days, I've approved the elimination of over 487 turnouts that were redundant. We're turning over every rock, big or small, to look for improvement and consistency.

Operator

Our next question is from the line of Jason Seidl with Cowen.

Jason H. Seidl
TD Cowen, Research Division

John, I wanted to talk a little bit about the new PTO and sick leave regulations and how much of an impact that you've seen there and sort of what you expect going forward? And I guess a quick follow-up is when you look at sort of the whole network, how are you viewing some of the yards? And is there a chance that you look to close a yard or two down the road?

John F. Orr
COO & Executive VP

Yes. Obviously, the sick leave is a national issue. I think no different than any other regulated or introduced crew limitation, we all have to deal with it. What I'm really focused on is crew productivity and yard productivity and increasing the capabilities of each assignment to do more within the time frame they've got to work. And so delivering more, getting accountability to connections, getting yield on our trains, that's the most important piece, and we're balancing that.

I'm on the team every day on crew availability to make sure that whatever we've committed to with our labor organizations or through the CBA process that we're living up to that. And on the flip side, making sure that the unions understand that they have an obligation to come to work within the time frames, dressed and ready to deliver for our customers each and every day. So it's both sides of that coin.

As far as the terminals are concerned, the reason why I started with hump yards is because they can add a lot of value. They can drive a lot of mechanized performance. But as we all know, they're costly. I want to get the most yield I can get out of them. I've already challenged our yard plan from yard to yard, node to node.

And we've started to eliminate power imbalances at a place like Chattanooga. We've reduced the bunching in the terminals by reestablishing a terminal clock at all of the major terminals. And we've even decreased a number of assignments that were moving

cars and causing multiple handlings between the yards. So I would say everything is open. I'm challenging the historic reason for a yard so that whatever we do is going to meet the operational need of today and tomorrow.

So everything is on the table. Everything is being scrutinized, and we will be rolling out a redefined yard operating plan and yard operating strategies in the next 30 days. And that will then drive or redesign of most of the operating plan over the next 60 to 90 days.

Operator

Our next question comes from the line of Jeff Kauffman with Vertical Research.

Jeffrey Asher Kauffman
Vertical Research Partners, LLC

John, just kind of a question on your impression coming in. As you were an outsider, you had a certain view of what Norfolk might not have been able to do. Now you're an insider, you've had a chance to see an operation. I guess my question is twofold. Number one, what's different about when you actually came on board and got a chance to get out there and see what's going on. And then my second aspect of that is, what do you think somebody on the outside might not appreciate about the Norfolk network and what can and can't be done?

John F. Orr
COO & Executive VP

Well, that's a great question. I'm glad you asked it. I'll tell you, in my first official act with boots on the ground was to go to East Palestine and really understand the scope of that issue. I'll tell you, I've been a railroader for over 40 years. I've been the incident commander at a number of derailments, some very consequential and some that I've had to make those same decisions that were made here to resolve imminent safety concerns. And understanding the scope and scale of the commitment that NS has made to that community, I've never experienced anything like that.

And so I came in with a bias and really had to understand the magnitude of that event and how that could have had a more lasting impact across not only NS, but the sector. As I looked at our operations, I always have a bias for yards because I think yards, especially in a merchandise environment where cars and customers kind of coincide. So how we handle them, how do we accelerate or drag is really important to evaluate.

And so I was pleasantly surprised at the richness of the terminals, but also quickly realized as I got under the hood that that was where a lot of the underperformance was happening. And that's why I set up a task force to kind of look at the data and drive performance through data, but also had a field component to check in a balance to make sure that we were driving was actually going to add performance and not undermined or burn something down that didn't need to be, either intentionally or unintentionally.

So I think having a good perspective of what the network looks like, as an outsider, you have biases. As an insider, you start to get under the hood and realize, okay, here may be a big rock issue, but then you get to know the smaller rocks that need to be moved out of the way to create that momentum. I've made a career out of going across Canada and the United States and Mexico, unclogging drains and creating a lot of momentum and then leveraging that momentum to build very competent, capable service plans; very competent, capable operators of those service plans; and creating sustained improvements. And that's what I'm seeing right now.

I think the architecture of NS is solid and it does come down to execution, and it's a very complex nonlinear network. That's what the east is all about. I've spent 35 of my 40 years in the east, either a craft employee or as a leader, as a senior leader in the United States, a senior leader in Eastern Canada. And I mean I know networks, I know the industrial complex that we're working in. It's very similar to the density that I just converted in Mexico.

So I think we've got lots of work to do. But as I said in my prepared remarks, it's a robust franchise with a talented team and the resources to deliver impressive results. We just have to properly execute.

Operator

Our next question is from the line of Stephanie Moore with Jefferies.

Stephanie Lynn Benjamin Moore
Jefferies LLC, Research Division

I appreciate the color, especially from you, John, on just the detailed plans in place around productivity initiatives and creating a PSR mindset across the organization. With this focus as a clear priority, what has been the customer response just given the changes

underway. How does this translate into incremental volumes? Is there a natural lag from customers? Does they kind of get convinced of the changes happening? Any color there would be helpful.

Alan H. Shaw
President, CEO & Director

Ed, why don't you address that?

Claude E. Elkins
Executive VP & Chief Marketing Officer

Sure. And thank you, Stephanie, for the question. As I said earlier, our customers are encouraged by a couple of things. Number one, the velocity of change that they see happening in terms of service improvement. And you think about our first quarter, we absorbed double-digit growth in our international book as well as low single-digit growth in our domestic book, held serve on our merchandise freight and improved service throughout that time and into April. So they're encouraged.

On the Intermodal front, like I said, it's really the best service in a generation that we're delivering. And I have a lot of confidence that we're going to continue to deliver that same level of service, which is only going to deliver more value for our customers. On the merchandise side, in some cases, our customers are going to have to unwind alternatives that they've got in place.

But you know what, have an exceptional service that is reliable and really just a conveyor belt, that's what they want. That's what allows them to unwind those alternatives and come back to where the natural value for them is, which is Norfolk Southern.

Alan H. Shaw
President, CEO & Director

You know, I've had a number of customers approach me, Stephanie, over the last month since John was announced, encouraged by our approach, encouraged by our direction and supporting our strategy. Our customers, as John noted, in the east are familiar with John in large part. And they've seen what he's done, wherever he's been to enhance service and enhance safety and enhance productivity, and that's what customers are looking for.

Ed, I don't know if you know it, but just this morning, we got an e-mail from one of our largest customers, thanking us for another excellent week of service.

Claude E. Elkins
Executive VP & Chief Marketing Officer

I was just about to close that. Thank you for another week of excellent service. You know who you are out there.

John F. Orr
COO & Executive VP

And we've had to make hard decisions. Ed and I have had to try to take very decisive decisions on car flows, even on how customers are interacting with some of our service facilities. It is -- but having the work on the front end, engaging with people, helping them understand what we're doing, helping them understand where they fit into that, whether it's union leaders, it's regulatory leaders or our customers, that really, Stephanie, helps them understand what we're doing, why we're doing it and how we're going to work together to create these standards.

Alan H. Shaw
President, CEO & Director

And Stephanie, that is our strategy, is making sure that we bring along our customers and our employees and our regulators and our shareholders with us as we transform Norfolk Southern into a more profitable organization with a safe and service product that is poised for growth.

Operator

Our next question is from the line of Jordan Alliger with Goldman Sachs.

Jordan Robert Alliger
Goldman Sachs Group, Inc., Research Division

Yes, maybe, this is in some ways a follow-up, but I'm just sort of curious. You have a pretty extensive list of things to do over the next 6 months and then 12 to 24 months. As you sort of come in, knowing what Norfolk had done already per you getting there and the gap that's been talked about. How much of this would you say, as what you would call basic blocking and tackling versus real sea changes in operational scope? Basically trying to assess your degree of confidence level in achieving and kicking all these things off and being able to hit the margin expectations in the coming years.

John F. Orr
COO & Executive VP

Well, I'll tell you this, that all across Canada, the U.S. and Mexico, I've been a change agent and an architect of PSR. I haven't had the luxury of looking in the rearview mirror very often. And so I don't spend a lot of time looking at what could have been or what was rather than what the current situation is and how fast can we get to the desired state. Desired state is having -- closing the gap for sure, having an operation that is focused on asset management with speed and accuracy to reduce the cycle times, reduce the dwell times and drive out waste.

So that's taking on an approach where it has a network overview. So there's a very strategic point of view on how do we create speed, accuracy by reducing dwell, increasing over-the-road performance, looking at long lead resources like locomotives and crews and how do we meet them as productive as we can and then create resiliency and elasticity for network response like we've seen in Baltimore.

And then really look at our smart investments, how do we leverage those things like capitalizing locomotive renewals, refurbishing locomotives that can be pushed off into the future because we're creating our own locomotives by having them more productive. I think this is a natural evolution on some of the linear elements that were started in the past. Now taking a multidimensional point of view on it, not focusing on one particular thing, but elevating the entire suite of operating efficiencies at the same time in tandem with one another. Disciplined railroading, disciplined service, accurate handling of cars and reduction of waste and cost is really the plan.

And that will show in the form of yard operating plans, disciplined operations and terminals, disciplined and progressive ways of moving the train service plan to the meet the commercial needs of today. I am highly confident, highly confident that we'll achieve the targets and we'll do it in a way that's sustainable and we'll do it in a way that fosters growth and we are on the path today. We're well underway. So that increased my confidence.

Operator

Our next question is from the line of Walter Spracklin with RBC Capital.

Walter Noel Spracklin
RBC Capital Markets, Research Division

I know you've put a lot of time under this, but I do need to come back to it and that is the -- trying to square up the changes that John is making here. They are substantial with the lack of any customer disruption. It used to be, and maybe I'm dating myself here, but it used to be when I ride, we saw PSR change. It didn't -- if customers weren't disrupted, then it wasn't happening, was kind of the view.

And when you take out 200 locomotives, soon to be 500 locomotives, I mean that kind of has to have leave a mark. We know there's been lane reductions, I guess, feedback from those customers must have been quite negative. So I just -- just wondering, are you just refocusing on those other customers and you're getting good service to them, and they're coming back to you with some good feedback and perhaps some of the less or lower-margin customers are going to be shed a little bit?

Just really surprised that we're not hearing more customer blowback from some of these significant and important changes that you're making.

Alan H. Shaw
President, CEO & Director

Walter, that's our strategy. That's what we're committed to doing. We're going to implement and we have been implementing PSR in a responsible and sustainable manner. We saw what happened in our peer in 2017. And we're not tearing this thing down to the studs. John knows how to do it without tearing it down to the studs as the activist COO has said he would have to do.

Ed is close to our customers. Our customers appreciate and see the improved service. We're focused on safety, and we're focused on a sustainable plan for Norfolk Southern that drives long-term shareholder value. John, you want to talk about how you're doing this in the right way.

John F. Orr

COO & Executive VP

And I think Walter, by the way, it's nice to hear from you. I would say, it's what we said at the very onset, that we're taking a balanced approach. I've laid out really challenging and urgent near-term and midterm targets and I'm taking an aggressive disciplined approach to manage it. And I view as the George Foreman Grill example, you don't set and forget operations. You sweat it out and you can't drive this alone.

So creating a team of capable railroaders focused on the big rocks and small rocks at the same time, delivering the fundamental of safety, creating stability across the network and then challenging every asset that we have, every standard that we have and building compliance and building momentum around those things is really important. So yes, it is sweat equity in a lot of respects, Walter. And it is really the key focus areas of yard time and dwell and you know what that does.

When we drive our current dwell down from mid-'23s to '22, and we'll be taking that down even further. Not only are we handling the cars better in the terminals, but we're getting more cars on trains, getting to the customers sooner. And even the bad order count, taking it down by double digits -- by almost 50%, means those -- the discipline of handling those cars in the terminal and getting them back into the flow of our core service offerings, customers are seeing those cars faster than they would have otherwise seen them.

So I would think that they see that as a value and rather than a negative disruption, a positive indication that we're building momentum and commitment to them while at the same time reducing handlings and costs.

Mark R. George
Executive VP & CFO

And just to close a loop, Walter, on say the locomotive specifically. Remember last year, we actually had to add locomotives back into service. We spent a fair amount of money in materials, trying to get locomotives that have been stored, back up and running so we could dig out of the top hole we were in following the East Palestine derailment.

It's how we got service really back on the right trajectory. And now we're able to start attacking some of those resiliency costs we've added and remove locomotives and some of the other costs we had to throw at the system. So there's a lot of opportunity here to remove costs that will be nondisruptive to the customers.

Alan H. Shaw
President, CEO & Director

And to summarize, the service level improvements, the dramatic service level improvements and what the customers are reacting to, and that is across our markets and across our customer base.

Operator

Our next question is from the line of David Vernon with Bernstein.

David Scott Vernon
Sanford C. Bernstein & Co., LLC., Research Division

So John, you've been at the property a little over a month. I'd love to kind of get your perspective on kind of what the root cause is here that you see as far as kind of what drove the problems? Is it a question of kind of what Norfolk was trying to do or how they were doing it? And kind of any thoughts you have on that would be helpful.

And then as you think about kind of taking 200 locomotives out, maybe another 300 locomotives. What is that for headcount? Because I would assume that the sequential headcount number was up a little over 500. Obviously, the non-craft trades -- the non-craft job action coming out, a couple of hundred heads will be down. But what are you thinking about the operating head count as you start to free up assets and run more fluidly?

Mark R. George
Executive VP & CFO

Actually, I'll handle the headcount question before John talks to you a little bit about his assessment of the challenges. You may recall, we guided last time where we said overall headcount would likely be flat over the course of the year. We were taking 300 non-agreement people out, but we would likely have to add some agreement folks that would offset it. We actually see now with John in the room here, a pathway for total headcount to be down around 2% by the time we end the year. So that's the path on headcount. John?

John F. Orr
COO & Executive VP

Yes. And just to add emphasis to that. As we get more productivity out of our yard and locos and more accuracy on our over-the-road transits and performance, we'll see more people virtually come alive, and we'll be able to have more availability and more crew flexibility. And I have frozen all hiring from operations. There may be 1 or 2 critical paths like C&S where -- signals and communications. That's a very specialized scale that we will need to continue to evolve as we bring our OT and IT and that kind of perspective into -- more into our safety plans.

But I would also say that it gets back to the basics. I'm not going to really be too critical of what I inherited. Rather, I saw a lot of things in flight that I'm able to leverage very quickly on. And at the same time, the basics of railroading, the basics of giving a great service plan at the lowest cost in the safest way possible is the recipe and building out discipline around that, creating visibility, accountability and driving purpose so that we improve these things is part of the challenge that I've laid out. And that's how we're delivering short term and midterm, and that's what we're going to continue to do.

Operator

At this time, we've reached the end of our question-and-answer session. I'll turn the call back over to Luke Nichols for closing comments.

Luke Nichols
Senior Director of Investor Relations

Thanks, Rob. Appreciate everyone's time and joining our call this morning. I recognize there's a few folks that didn't get a chance to ask your questions. I want to let you know Investor Relations is here through the rest of the day. Please feel free to reach out to us. We look forward to seeing everybody through the quarter.

Operator
Ladies and gentlemen, thank you for your participation. This does conclude today's teleconference. You may disconnect your lines, and have a wonderful day.