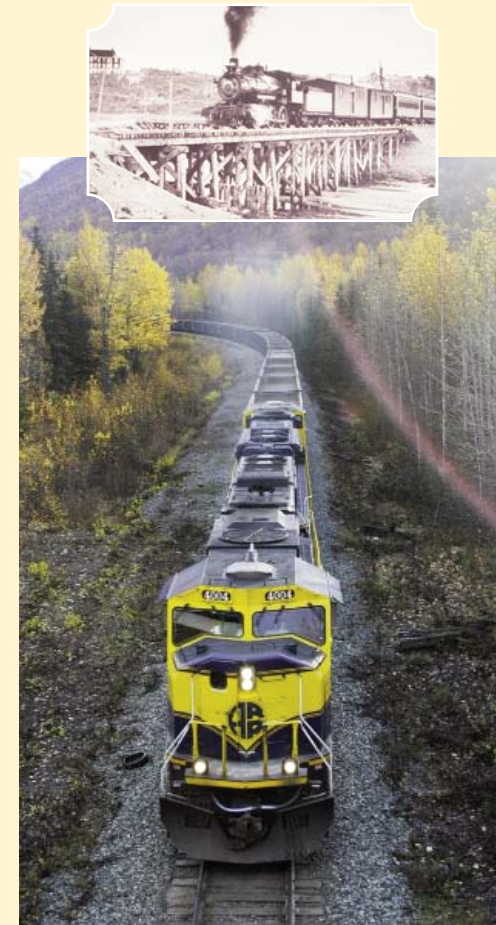




Report to the State of Alaska

January 2008





ARRC President: A Look Ahead

As defined in the Alaska Railroad Corporation Act (AS 42.40), the Alaska Railroad Board of Directors shall adopt a long-range capital improvement plan each year and shall share that plan with the governor and legislature. I am pleased to present the 2008 report which, besides the mandatory program information, includes a short synopsis of 2007 accomplishments as well as other company highlights we believe will provide context and continuity for the 2008 submission.

I would grade the Railroad's 2007 business year as an overall "solid," considering that the Alaskan economy was unremarkable. It was financially sound on the Operations and Maintenance side, quite productive on the Capital Projects side, and ended up becoming significantly introspective on the planning side. From a financial standpoint, year-end 2007 sees total revenues forecast at \$130.2 million, total expense forecast at \$115.2 million and a corporate net income forecast at \$15.0 million. While total freight tonnage was down compared to previous years, operational tempo became vigorous at times, including two substantial military moves and the addition of one more weekly Anchorage-Fairbanks freight train to better accommodate growing customer demand for consumer items and North Slope equipment headed for the Interior. Passenger ridership set a new record (again) with three of our summer service trains each growing over 8%. And for the third consecutive year our Real Estate Department surpassed its revenue record, thanks in part to an aggressive property development initiative.

2007 was a year in which we rebaselined our corporate status, and then shaped the output into a new five-year plan. As part of that assessment effort the Railroad initiated three in-depth audits, each aimed at examining key processes of our business. We studied our vehicle fleet management program, our information technology support services, and we analyzed possible causes contributing to our less than desirable operating ratio. These audits yielded fruitful recommendations, many of which are being incorporated into our new five-year program.

For 2008 and beyond, while we cannot forecast the economy of Alaska, we can be secure in the knowledge that the Alaska Railroad Corporation will continue a formidable program of capital spending throughout the railbelt. We are still investing millions each year on rail, ties, ballast, and bridges in order to refurbish the basic infrastructure. Safety and efficiency upgrades are integral in our much accelerated six-year rebuilding program, which includes straightening the main track in several areas, building longer sidings (railroad "passing lanes") to handle our longest trains, adding automated and heated switches, and installing the nation's first full up collision avoidance system. The Railroad is also looking at opportunities to better serve passengers with new facilities, better passenger ticketing and onboard services, and modernized rail equipment and technology.

Payment for the Railroad's capital projects program comes from federal funds (requiring matching dollars from the Alaska Railroad) as well as in-house full funding using Railroad earnings. In 2007 the Alaska Railroad supported a \$71.9 million capital budget. We plan on a \$64.5 million capital budget for 2008, on our way to a \$298 million five-year capital program (2008 through 2012). Details of our program are highlighted in this report and detailed descriptions of all our projects are available at the railroad's web site — www.AlaskaRailroad.com.

We hope this report provides you with a useful topline picture of the Alaska Railroad program. We would be happy to provide you or your staff more detail via an ARRC briefing during the 2008 legislative session.

Warm regards,

Patrick K. Gamble
President and Chief Executive Officer



Alaska Railroad Guiding Principles

Alaska Railroad Mission

- Safety... Customer Service... Profitability

Alaska Railroad Vision

“Building a great Railroad across the Greatland.”

An important element in fulfilling this vision is ARRC’s success since 1996 in qualifying for federal funding...an entitlement afforded the railroad’s public status and its passenger service mission. As a result, ARRC has been able to greatly accelerate long overdue mainline maintenance and upgrades.

In addition, other federal grants for facility improvements, such as intermodal facilities and docks, as well as improved technology, have come to ARRC via recent major federal transportation and transit bills.



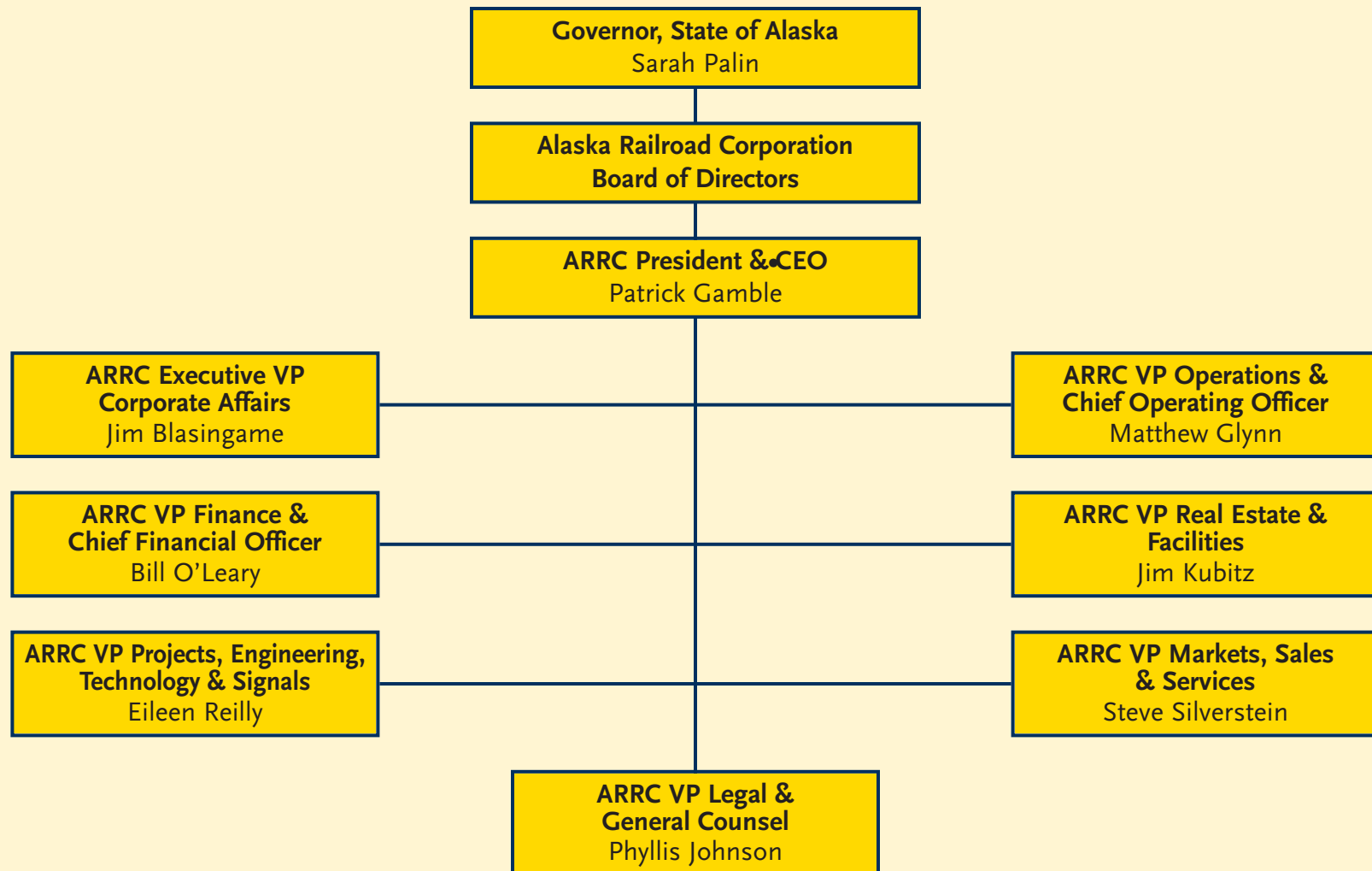
Alaska Railroad Values

We are a values based organization. Values are all about people, not things. We are all about taking care of our people. We believe who you are is as important as what you do. Character counts. Many of our values are embodied in our corporate Code of Conduct. Our fundamental core values consist of integrity, excellence, and service.

As a responsible partner, in order to accomplish the ambitious goals we set out for ourselves in conjunction with those of others along the railbelt, the ARRC must be a safe, secure, customer responsive, financially and environmentally sound, employee friendly corporation. We must provide a stable, reliable foundation that can be counted on to enhance the future economic growth of the state and the municipalities we support. If our corporate foundation is not sound, support for further state growth and development becomes problematic at best. Values and high standards are the building blocks of that foundation.



Alaska Railroad Organizational Chart





Alaska Railroad Quick Facts

Purchase Price (January 5, 1985)

Paid to federal government	\$22.3 million
Start-up costs & contributed capital	<u>\$11.9 million</u>
Total Investment-State of Alaska	\$34.2 million

Organization (following State purchase)

- Independent corporation owned by State
- Managed by a seven-member board of directors. Position qualifications are spelled out in law, members appointed by the Governor.
- Mandated to be self-sustaining, responsible for all its own financial and legal obligations

Financial Statistics

January 1-December 31, 2007 (unaudited)*

Total Assets	\$ 840 million
Total 2007 revenues	\$ 130.2 million
Total 2007 expenses	\$ 115.2 million
2007 net income	\$ 15.0 million
2008 net income budget	\$ 14.1 million

Operating Data

Miles of main line	467
Miles of branch line	77
Miles of yards and sidings	107
Total miles of track	651
Freight cars (owned & leased)	1,238
Passenger cars	54
Locomotives	57

Operating Statistics

January 1-December 31, 2007

Passenger ridership	563,491 passengers
Freight tonnage	6.05 million tons

Employees (as of January 2008)

Number of year-round employees	801
Average years of service	10.4
Average age	43.9
Male	659
Female	142

Unions (as of January 2008)

Most of ARRC employees are members in one of five unions:

United Transportation Union	148
Transportation Communication Union	48
International Association of Machinists	65
American Federation of Govt. Employees	305
American Train Dispatchers Department	10

Benefits

- Corporation provides a fully funded defined benefit pension plan
- Corporation provides for health and life insurance
- Corporation provides for retiree medical benefits

* ARRC audits are normally complete by March 31.



Alaska Railroad Mileposts

Each year the Alaska Railroad forecasts its long term objectives and unmet challenges. From this annual analysis, the Alaska Railroad management team establishes an annual rolling 5-year baseline of goals and objectives covering both the short and long terms. At the end of the year, ARRC scores itself against progress made towards meeting these challenges. As objectives are permanently achieved, they are dropped and new ones take their place.

ARRC Five-Year Objectives

- Reduce employee injuries to no more than 2.0 per 200,000 man hours.
- Eliminate 25% of at-grade highway/railroad crossings.
- Achieve and sustain an operating ratio of at least .98 by 2011
- Generate and sustain company-wide cash flow, measured as net earnings plus depreciation, of \$39 million per year by 2011.
- Generate and sustain cash flow from real estate activities of \$9 million per year by 2010.
- Work to harmonize ARRC business and development plans with railbelt community business and development efforts.
- Maximize return from existing business relationships and seek out new profitable opportunities without sacrificing world class customer service.
- Fully implement Collision Avoidance System technology by 2008.

- Reduce average running time for freight trains between Anchorage and Fairbanks to consistently under 10 hours.
- Complete the entire Reliability Excellence transition plan by 2009.
- Set up an annual programmatic investment plan for ARRC facility infrastructure, including yards and marine facilities, to meet business, growth, employee, and community requirements.
- Ensure ARRC attracts and retains excellent employees by being known as a premier Alaskan employer and by continuously improving our employee training working environment, remuneration, and benefits.
- Build the bridge across the Tanana River.
- Extend the rail line to Delta Junction.
- Complete the accelerated Track Rehabilitation Program plan by 2012.



Five-Year Forecast — Capital Budget

<i>(in millions)</i>	2008 Budget	2009 Forecast	2010 Forecast	2011 Forecast	2012 Forecast	TOTAL
ARRC Internally Generated	\$ 16.6	\$ 20.9	\$ 21.4	\$ 22.7	\$ 25.3	\$ 107.0
Bond Funded	33.7	27.9	19.1	22.0	8.6	111.2
Federal Transit Administration	39.3	41.7	43.0	44.3	45.6	213.8
less: Preventive Maintenance Reimburse	(10.3)	(10.7)	(11.1)	(11.6)	(12.0)	(55.6)
Less: Debt Service Grants	(16.2)	(15.9)	(15.9)	(15.9)	(15.9)	(79.9)
Federal Highway Administration	0.9	0.9	—	—	—	1.7
Other	0.6	—	—	—	—	0.6
Total Capital Budget	\$ 64.5	\$ 64.7	\$ 56.4	\$ 61.5	\$ 51.6	\$ 297.9

Five-Year Forecast — Operating Budget

<i>(in millions)</i>	2008 Budget	2009 Forecast	2010 Forecast	2011 Forecast	2012 Forecast	TOTAL
Operating Revenue	\$ 126.1	\$ 132.2	\$ 136.7	\$ 140.2	\$ 144.4	\$ 679.5
Operating Expenses	\$ (100.2)	\$ (107.6)	\$ (111.7)	\$ (116.0)	\$ (116.4)	\$ (551.9)
Net Income-Real Estate	\$ 7.9	\$ 9.9	\$ 9.7	\$ 10.4	\$ 11.2	\$ 49.1
Other Income	\$ 0.9	\$ 1.0	\$ 1.1	\$ 1.2	\$ 1.2	\$ 5.4
Net income (before Depreciation & Interest)	\$ 34.7	\$ 35.6	\$ 35.7	\$ 35.7	\$ 40.4	\$ 182.1
Depreciation	\$ (15.9)	\$ (16.4)	\$ (16.6)	\$ (16.5)	\$ (18.0)	\$ (83.5)
Interest Expense	\$ (4.7)	\$ (4.9)	\$ (4.6)	\$ (4.2)	\$ (7.2)	\$ (25.2)
Net Income	\$ 14.1	\$ 14.3	\$ 14.5	\$ 14.9	\$ 15.1	\$ 73.0

Five-Year Capital Project Plan-Internal Funding

	2008 Budget	2009 Forecast	2010 Forecast	2011 Forecast	2012 Forecast	TOTAL
Nondiscretionary Projects	\$ 7,016,000	\$ 7,149,800	\$ 6,904,200	\$ 7,289,351	\$ 9,124,842	\$ 37,484,193
Continuing Program Projects	5,189,000	4,235,700	3,802,933	2,940,700	2,663,600	18,831,933
Strategic Business Initiatives	3,424,285	2,955,000	2,810,000	2,875,000	2,875,000	13,793,000
Ranked Projects	1,368,000	6,559,900	7,886,567	9,627,649	10,634,158	36,076,274
Total - Internal Funding	\$ 16,997,285	\$ 20,900,400	\$ 21,403,700	\$ 22,732,700	\$ 25,297,600	\$ 106,185,400

Five-Year Capital Project Plan — Federal and Bond Funding

	2008	2009	2010	2011	2012	TOTAL
Federal Transit Administration						
Passenger Equipment: Rehabilitation	1,300,000	900,000	1,000,000	900,000	900,000	5,000,000
Track Projects:						
Ship Creek Intermodal	278,551	—	—	—	—	278,551
Track Rehabilitation	1,733,964	6,875,282	12,701,561	11,727,335	13,885,754	46,923,896
Siding Extensions/Upgrades	3,005,0495	1,000,000	1,000,000	1,000,000	1,000,000	7,005,495
<i>Track Project Subtotal</i>	5,018,010	7,875,282	13,701,561	12,727,335	14,885,754	54,207,942
Bridge Replacements/Upgrades:						
Bridge 352.7 Sheep Creek	—	625,000	250,000	—	—	875,000
Bridge 148.3 Matanuska River	1,850,000	1,150,000	—	—	—	3,000,000
Bridge 432.1 Permafrost Bridge	2,500,000	1,300,000	—	—	—	3,800,000
Bridge 422.9 Permafrost Bridge	—	—	—	600,000	—	600,000
Bridge 447.7 Permafrost Bridge	—	—	—	—	600,000	600,000
Bridge 29.5 Trail Lake	—	2,500,000	425,000	—	—	2,925,000
Bridge 284.2 Hurricane Gulch	—	200,000	—	2,000,000	800,000	3,000,000
<i>Bridge Program Subtotal</i>	5,300,000	4,750,000	250,000	3,600,000	—	16,900,000
Docks: Whittier Marginal Wharf	650,000	—	—	—	—	650,000
Debt Service Subtotal:						
2006 Bond Issue Debt Service	7,179,796	7,165,330	7,169,413	7,148,837	7,141,197	35,802,573
2007 Bond Issue Debt Service	9,039,073	8,771,957	8,275,374	8,751,006	8,751,540	44,063,950
Debt Service Subtotal	16,218,869	15,935,287	15,919,787	15,899,843	15,892,737	79,866,523

Five-Year Capital Project Plan — Federal and Bond Funding (continued)

	2008	2009	2010	2011	2012	TOTAL
FTA... continued						
Preventive / Safety / Security:						
Preventive Maintenance Reimbursement	10,268,099	10,678,823	11,105,976	11,550,215	12,012,224	55,615,337
Moody Tunnel Rehabilitation	850,000	—	—	—	—	850,000
CMMS Preventive Maintenance System	175,000	100,000	100,000	100,000	—	475,000
Transit Enhancements	210,093	223,494	230,199	237,105	244,218	1,145,109
Transit Security	210,093	223,494	230,199	237,105	244,218	1,145,109
<i>Preventive/Safety/Security Subtotal</i>	<u>11,713,285</u>	<u>11,225,811</u>	<u>11,666,374</u>	<u>12,124,425</u>	<u>12,500,660</u>	<u>59,230,555</u>
Total Federal Transit Administration	39,250,164	41,711,380	42,962,722	44,251,603	45,579,151	213,755,020
Less: Preventive Maintenance Reimbursement	(10,268,099)	(10,678,823)	(11,105,976)	(11,550,215)	(12,012,224)	(55,615,337)
Less: Debt Service Grants	(16,218,869)	(15,935,287)	(15,919,787)	(15,899,843)	(15,892,737)	(79,866,523)
Total FTA for Federal Capital Projects	12,763,196	15,097,270	15,936,959	16,801,545	17,674,190	78,273,160
FTA-Backed Revenue Bonds (2006)						
2006: Track Rehabilitation Program	17,656,463	—	—	—	—	17,656,463
FTA-Backed Revenue Bonds (2007)						
Passenger Equipment: Bi-Level Dome Cars	5,480,000	—	—	—	—	5,480,000
2007: Track Rehabilitation Program	<u>10,532,147</u>	<u>27,852,368</u>	<u>19,061,013</u>	<u>21,994,000</u>	<u>8,605,485</u>	<u>88,045,013</u>
Total FTA-Backed Bond Receipts-2007	11,111,446	25,876,680	22,615,129	20,788,719	80,391,974	
Federal Highway Administration						
South Wasilla Realignment Land Acquisition	173,300	—	—	—	—	173,300
Community Rail Realignment	<u>697,317</u>	<u>870,617</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>1,567,934</u>
Total Federal Highway Administration	870,617	870,617				1,741,234
U.S. Forest Service						
Chugach Forest Whistle Stop	<u>200,000</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>200,000</u>
Total Federal & Bond Funding	<u>47,502,423</u>	<u>43,820,255</u>	<u>34,997,972</u>	<u>38,795,545</u>	<u>26,279,675</u>	<u>191,395,870</u>