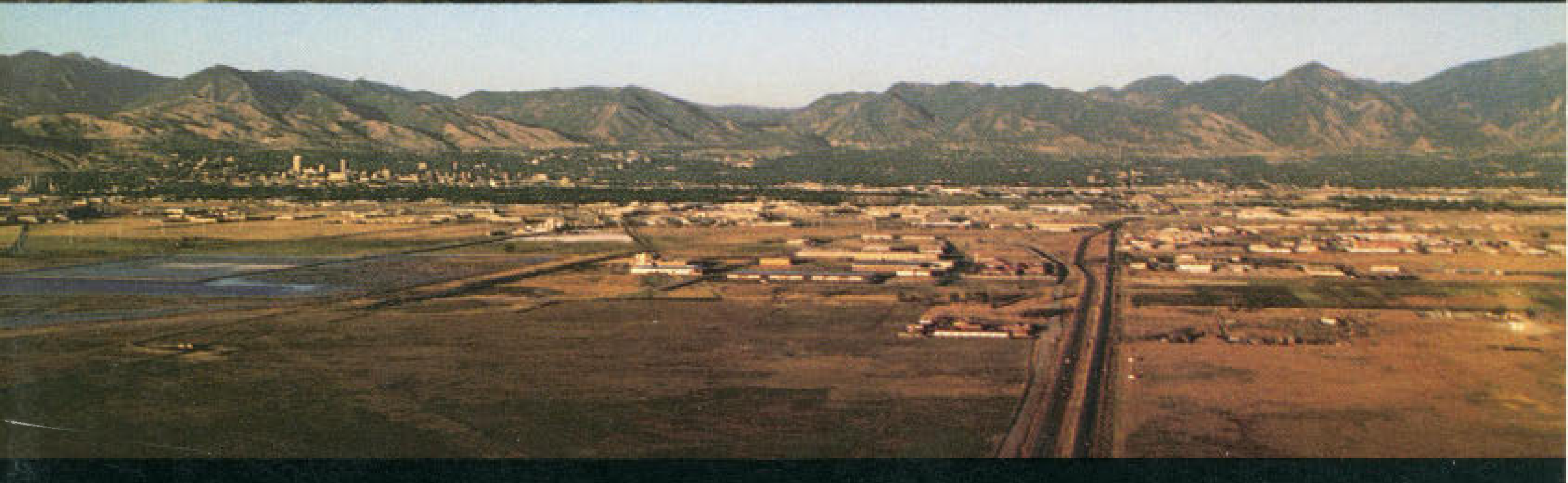
Union Pacific Corporation Annual Report 1978



Contents

Cover: The panorama of businesses that comprise Union Pacific Corporation is shown in the four photographs. *From top to bottom,* *(1)* a high-speed Union Pacific Railroad container train highballs across the Nebraska plains to a Missouri River gateway; *(2)* a Champlin Petroleum Company natural gas well in the Greater Green River Basin in southwestern Wyoming is readied for production; *(3)* Rocky Mountain Energy Company's joint-venture mine at Medicine Bow in southern Wyoming, and a 110-car Union Pacific unit train about to load 11,000 tons of coal destined for a midwestern utility; and *(4)* Upland Industries Corporation's Centennial Park, center foreground, on the outskirts of Salt Lake City, which serves the city's most rapidly-growing industrial area.

Ten Years of Progress

Union Pacific Corporation consists of four operating companies engaged in railroad, energy and other natural resource activities vital to America's economy.

- Union Pacific Railroad Company operates a 9,700-mile transportation system in 13 western states and hauls a balanced commodity mix of minerals, farm products, consumer and industrial goods and container traffic. It connects with 32 other railroads serving the U.S. and Canada.
- Champlin Petroleum Company engages in exploration, development and production of crude oil and natural gas in many areas of North America, and refines and markets petroleum products.
- Rocky Mountain Energy Company develops Union Pacific's reserves of coal, uranium and trona (from which natural soda ash is refined) in the Rocky Mountain region, and explores for minerals there and elsewhere in the U.S.
- Upland Industries Corporation manages Union Pacific's land bank of prime industrial and commercial sites and other properties held for investment, and acts as the industrial development agent for Union Pacific Railroad.

Ten years have passed since Union Pacific Railroad, which was chartered by an act of Congress in 1862, began the realignment of its corporate structure in February, 1969. Since then the size and character of the Corporation have changed dramatically. About 20 percent of its earnings was derived from natural resources activities in 1969; today they account for almost 50 percent of total earnings.

Energy development activities comprise the heart of this expansion. In 1969, Union Pacific's energy operations consisted of its crude oil production, primarily in California, one small refinery, and three active royalty arrangements involving the mining of coal on the company's land in Wyoming. By the end of 1978, the Corporation had a fully-integrated oil company, Champlin Petroleum acquired in 1970, and a total of 1,833 producing oil and natural gas wells, three refineries with a total capacity of 245,000 barrels a day, eight gas plants, and 1,430 miles of crude oil and product pipelines. By the end of 1978, Union Pacific also had partnership interests in two operating coal mines and one uranium mine and mill, as well as 22 active coal royalty arrangements, 13 with major companies. During this 10-year period, two new trona mines and processing plants were opened by soda ash producers under royalty arrangements with Union Pacific.

As the energy and natural resources businesses became substantial enterprises in their own right, Union Pacific Railroad has consistently ranked among the most efficient and profitable railroads in the U.S. It is also rightly perceived to be among the best-maintained railroads in the industry. Over the past 10 years, Union Pacific has spent $1.3 billion on new railroad equipment and an additional $2.3 billion to maintain the Railroad's equipment and track structure, while doubling earnings and increasing revenue ton-miles from 46.5-billion in 1969 to 68.2 billion in 1978.

As its operating companies have developed, Union Pacific's total earnings have grown from $84.4 million in 1969 to $264.1 million in 1978. Earnings per share, after adjustment for a two-for-one stock split in 1977, nearly tripled from $1.88 to $5.55 last year.

Financial Highlights

Union Pacific Corporation and Subsidiary Companies			Dollar Amounts in Millions Except Per Share Amounts
Total Year	**1978**	1977	% Increase (Decrease)
Revenues	**$2,989.4**	$2,554.3	**17**
Income before Federal income taxes	**397.6**	338.0	**18**
Net income	**264.1**	221.9	**19**
Operating cash flow	**526.6**	449.5	**17**
Capital investments[a]	**$ 552.6**	$ 418.1	**32**
At December 31			
Short- and long-term borrowings	**$ 932.4**	$ 968.9	**(4)**
Stockholders' equity	**2,286.0**	2,117.5	**8**
Working capital	**$ 184.5**	$ 130.6	**41**
Measurements			
Per share of common stock			
Earnings	**$ 5.55**	$ 4.68	**19**
Dividends declared	**$ 2.075**	$ 1.775	**17**
Ratios			
Return on average stockholders' equity	**12.0%**	10.9%	
Borrowings to total capital employed	**24.7%**	27.0%	

(a) Includes advances to and capital expenditures of unconsolidated affiliated companies (1978—$128.4 million; 1977—$53.9 million) in addition to consolidated capital expenditures.

To Our Stockholders:

Ten years ago, in February, 1969, and 100 years after the driving of the Golden Spike, Union Pacific Corporation was formed to provide a logical vehicle for the development of the energy, mineral and land resources owned by the Company at the time. Implicit in the establishment of the new organization was a continuing commitment to maintain our Railroad as the best in the industry. The key to the successful reorganization has been the creation of a highly-skilled team that could fully realize the development of these growing areas of opportunity. That team is now in place and functioning with great proficiency and effectiveness.

The past decade has seen the attainment of the goals set in 1969, accompanied by a strong growth of all of our businesses. These achievements are the sum total of the accomplishments of every member of the Union Pacific family, and our 1978 Annual Report to Stockholders—which also is being sent to all employees this year—is testimony to their resourcefulness, imagination and dedication.

Union Pacific Corporation capped its tenth year with new highs in earnings and revenues. Net income in 1978 was $264.1 million, an increase of $42.2-million or 19 percent over 1977's net income of $221.9 million. Earnings per share in 1978 were $5.55, compared with $4.68 in 1977. Revenues were $2.99 billion, a gain of $435 million or 17 percent over the $2.55 billion achieved last year.

All four operating companies participated in this expansion, and net income of our energy and natural resource businesses approached the income of Union Pacific Railroad Company, another corporate goal established in 1969.

The Railroad moved a record volume of freight in 1978. Champlin Petroleum Company broadened its exploration and production programs and improved its manufacturing and marketing operations. Rocky Mountain Energy Company continued to step up development of its coal, uranium and natural soda ash resources, and Upland Industries Corporation doubled its net income through rising sales of industrial sites throughout the West. These accomplishments are covered in detail in the following pages of this report.

On November 30, the Board of Directors, reflecting the Corporation's record performance in 1978 and its promising prospects in the years ahead, increased the quarterly dividend 15 percent, from 50 to 57½ cents a share. Also, in February, 1979, Union Pacific announced a stockholders' dividend reinvestment plan.

National Issues—Our nation is in a period of uncertainty, with a number of tenacious problems at hand for which there are no pat solutions. Among our concerns, three are paramount: inflation, energy development and government regulation.

The President has called the shackling of inflation the nation's first priority, and we support every reasonable effort to control it. However, a comprehensive program of wage-and-price guidelines cannot succeed unless there is an equally determined effort by the Federal government to exercise fiscal and monetary restraint, while providing appropriate encouragement for capital formation and increased productivity.

On energy matters, the precise effects of the energy legislation passed by the Congress after 18 months of debate are difficult to assess, since the Administration is still promulgating detailed regulations covering the legislation. But many experts, both within and outside the petroleum industry, believe that the new bill does not adequately stimulate development of the country's large reserves of untapped energy resources.

We are encouraged, however, by indications that the climate for bringing domestic crude oil prices into line with world prices seems to have improved in recent months. We believe that the best way to achieve this goal is to phase out price controls. Phased decontrol over a two- to three-year period would maximize crude oil development in the U.S., reduce our country's dependence on foreign sources, and minimize the inflationary impact.

We are also encouraged by the growing perception by government that a less-regulated environment would be beneficial to the nation.

On rail deregulation, for example, we see 1979 as a potentially significant year for the whole industry. Mounting pressure in the Congress, coupled with the Administration's position in favor of deregulating our truck competitors, and evolving support within the rail industry itself, promises to press rail deregulation to the forefront.

Union Pacific Railroad Company is one of the most efficient, profitable and financially-sound railroads in the world. As your Corporation's managers, we must carefully weigh the impact that deregulation would have on Union Pacific's competitive position. Accordingly, we have been participating actively in industry and government studies relating to this vital matter. We believe that our financial and management strength, outstanding physical plant and strategically-located lines place us in an excellent position to respond to—and take full advantage of—opportunities for change generated by deregulation.

E. Roland Harriman—We note with great sadness the death of E. Roland Harriman, who served as Chairman of Union Pacific from 1946 to 1969 and as Honorary Chairman until his death February 16, 1978. Mr. Harriman's stewardship of Union Pacific spanned nearly 60 years of dedicated service. He helped to develop the farsighted plan that transformed the Company from a very successful railroad into an equally successful, broad-based transportation, energy and natural resource company. His visionary counsel and kindly guidance will long be remembered.

Robert A. Lovett—Former Chairman of the Executive Committee, a Union Pacific Director since 1921 and the Chief Executive of the Company from 1953 to 1967, Robert A. Lovett retired from the Board of Directors on March 9, 1978. Mr. Lovett, in addition to his outstanding record of government service, which included serving as Secretary of Defense and Under Secretary of State in President Truman's Administration, was one of the principal planners of the modern Union Pacific Corporation. His foresight and wisdom were invaluable to senior management and his fellow directors.

New Directors Elected—E. Virgil Conway, 49, Chairman of the Board of The Seamen's Bank for Savings, New York, was elected to the Board of Directors on March 30, 1978. John R. Meyer, 51, Professor of Transportation, Logistics and Distribution at the Harvard Graduate School of Business Administration, was elected to the Board on November 30.

Outlook—There are more than the usual number of uncertainties confronting the U.S. economy, but we remain, on balance, optimistic about Union Pacific's prospects for 1979.

Although the possibility of an economic slowdown is ever-present, and severe weather in the West slowed shipments as the new year began, the Railroad's prospects for the year as a whole appear promising. We also anticipate a good commodity mix. Champlin should benefit from a strong market for refined products, expanded production of natural gas and a general improvement in gas prices. Rocky Mountain Energy anticipates startup in late 1979 of two more joint-venture coal mines and will continue its aggressive uranium exploration and development effort. We also believe that Upland's ongoing development programs and the strategic locations of its properties will generate continued vigorous real estate activity.

In short, the 1979 earnings performance of our railroad, oil, gas, coal, uranium, natural soda ash and land businesses should be good. We are equally confident about our long-term opportunities and look forward to our second decade with assurance born from the strong organization that has evolved since the Corporation was formed in 1969.

On behalf of the Board of Directors, we thank our stockholders, customers, dealers, suppliers and our 30,000 employees for their contributions to the success of Union Pacific in 1978, and for the solid foundation they have built for our future.

James H. Evans

James H. Evans
Chairman of the Board of Directors

William S. Cook

William S. Cook
President

Elbridge T. Gerry

Elbridge T. Gerry
Chairman of the Executive Committee

New York, NY
February 13, 1979

Left to right,
James H. Evans
William S. Cook
Elbridge T. Gerry

Union Pacific Railroad's 1978 net income increased 21 percent to $140.1-million, setting a record for the third consecutive year. Reflecting the nation's continuing economic expansion and a general freight rate increase of 4 percent in June, revenues were up 16 percent to $1.5 billion. The industry also received a 7-percent increase in December to offset rising costs, with an effective yield to Union Pacific of 6.5 percent.

The Railroad's revenue ton-miles reached 68.2 billion, up 12 percent over 1977, another new high, and the length of Union Pacific's average haul increased to 689 miles, compared to 659 miles in 1977. The Railroad's operating ratio—a key measurement of efficiency—was 83.1 compared to 83.4 in 1977. An operating ratio matches a railroad's operating expenses against its revenues. Union Pacific's ratio has traditionally been among the lowest in the industry.

The nation's increasing dependence on coal as an energy source and the 111-day strike by the United Mine Workers, which closed down most eastern mines, helped swell demand for the Railroad's services. Revenue ton-miles of coal, which constituted 20 percent of Union Pacific's total, rose by 16 percent over 1977 levels. Revenue ton-miles of grain, reflecting the movement out of storage and strong demand from abroad, more than doubled over 1977.

Union Pacific also benefited from key programs launched in prior years and further refined in 1978. Among these were expanded marketing and planning efforts; continuing modernization of yards and terminals; the upgrading of its locomotive and freight car fleet; a maintenance program for track, roadbed and rolling stock that sets industry standards; and higher efficiency through advanced computer applications.

Sales and Marketing—Through 58 offices located in the U.S. and five others in foreign countries, Union Pacific pursued business opportunities with primary shippers, shipping agencies and other transportation companies. The Railroad's sales and marketing efforts were characterized by innovative services to meet the specific needs of its customers. In many instances, specialized equipment was purchased and schedules were revamped in order to attract new business. This also has helped the Railroad to capture traffic from the trucking industry in such diverse commodities as flat glass, tractors

Running through some of the most rugged terrain in the U.S., from 8,000-foot high passes through the Rocky Mountains to snow-swept plains, hundreds of Union Pacific trains each day maintain one of the best on-time records in the rail industry. *At right,* four powerful locomotives pull enclosed auto cars through the picturesque Blue Mountains of eastern Oregon. *Above, from top down,* Union Pacific trains roll across Nebraska and Wyoming and snake through Oregon's Meachem Pass.

and chemicals. In addition, Union Pacific's piggyback traffic continued to grow.

The tonnage contribution and percentage of change in each major commodity hauled by the Railroad are shown in the Commodities Chart on page 33.

The continued expansion and development of the southern Wyoming, Utah and Colorado coal-producing regions have helped to enhance Union Pacific's traffic base. To facilitate the handling of this increased traffic, the Railroad acquired or constructed 499 open-top hopper cars during 1978.

In December, the Railroad concluded an agreement with the Chicago and North Western Railroad that, subject to ICC approval, may eventually give Union Pacific an important share of the coal traffic coming out of the southern Powder River Basin, a major coal-mining region in Wyoming. Under this agreement, the C&NW will build a new line, approximately 80 miles long, near the Wyoming-Nebraska border, to connect with Union Pacific in western Nebraska. Union Pacific will, in turn, serve as a link for traffic bound for the Midwest and Southwest. The target date for completion of the line is 1982. By 1985 this arrangement could add 25-million tons annually to Union Pacific's coal traffic.

During 1978, Union Pacific's westbound shipments of corn and sorghum in units of 25, 50 and 75 cars greatly expanded. Tonnage moved in this way more than tripled in 1978. Under this program an increasing share of Asia-bound grain, much of which had formerly been shipped via Gulf Coast ports, now moves over Union Pacific's lines to the West Coast. Such block shipments of grain simplify operating procedures and permit better utilization of equipment.

The advantages of blocking cars also have been realized by establishing run-through trains carrying a variety of other commodities. A run-through train is one that uses the same locomotives through an entire trip, even though it passes over the lines of more than one railroad. An important run-through link was established between the Southeast and the West with the Southern Railway and the Missouri Pacific. Another significant run-through connection was created with Canadian Pacific between Hinkle, Oregon, and Calgary, Alberta, to expedite traffic to and from these rapidly-growing areas.

Reflecting its resolve to increase its service to the auto industry, the Railroad carried more automotive traffic in 1978 than in any other year in its history. The Railroad's substantial investment in enclosed auto cars and its dependable service enabled it to handle increased traffic from both domestic producers and importers. Revenue ton-miles of assembled autos were up 18 percent.

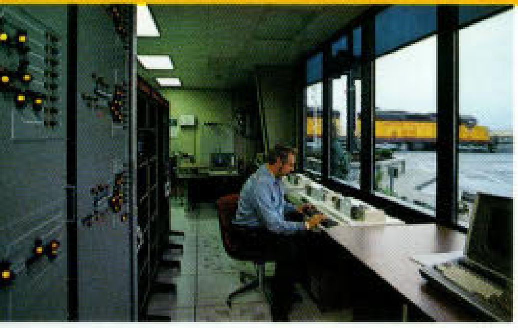
Shipment of autos by rail also was facilitated by auto loading and unloading terminals, located on the periphery of major urban centers. A $2-million unloading complex near Denver, with convenient highway access for local distributors, was completed in 1978 and supplements nine similar facilities in other major metropolitan areas.

Another area of significant growth was trailer and container traffic, which moves in conjunction with trucks and ships. Crucial to the development of this business has been the maintenance of competitive scheduling and pricing and a substantial investment in advanced lifting equipment that permits the rapid transfer of trailers and containers to and from flat cars. Carloadings of such intermodal freight increased by 10 percent last year.

Rapid shipment of record levels of freight by Union Pacific during 1978 was accomplished through the increasing use of specialized equipment and facilities, and unit trains hauling bulk commodities. Rail- and water-borne traffic meet in Seattle, *far right,* where the Railroad funnels a diversified range of shipments onto barges for growing Alaskan markets. In Long Beach, California, *top left,* a gantry crane quickly transfers truck trailers and containerized ocean-bound freight from one mode of transportation to another at Union Pacific's intermodal facility. In Portland, *center,* a new car is driven off an auto carrier at the Railroad's automotive unloading facility, and at Shelton, Nebraska, *bottom,* a worker checks a loaded hopper car of a West Coast-bound unit grain train.


NYK


TRAILER TRAIN



Increasing traffic within Union Pacific's Northwestern District is being handled by the new, fully-automated classification yard at Hinkle, Oregon, *right,* which opened in February, 1978. Employee, *above,* monitors the computer system in the yard, one of five automated yards in the Union Pacific system. The Railroad anticipates a substantial increase in traffic to the Northwest, Canada and Alaska over the next decade. The array of diesels, *right below,* is part of the Union Pacific fleet of more than 1,500 locomotives. The Railroad ordered a record 340 locomotives during the last three years.

Classification Yards—Union Pacific's new, fully-automated classification yard at Hinkle, Oregon, began operating early in 1978. Union Pacific also started construction in 1978 of a new westward classification yard at North Platte, which will double the capacity of the Railroad's existing yard. When completed in 1980, the $40.5-million yard is expected to improve service and reduce operating expenses throughout the entire Union Pacific system by about $14 million annually.

During 1978, Union Pacific increased by 72 miles its system of track operated under centralized traffic control, which, in effect, adds capacity nearly equivalent to an additional line of track. The Railroad now has 2,580 miles controlled under this system.

Equipment—Union Pacific continued to upgrade its rail fleet, allocating $179.2 million for new transportation equipment during 1978. Of this amount, $74.9 million was spent for 120 high-speed locomotives. The Railroad also purchased 1,506 freight cars, of which 1,400 are covered hoppers designed to carry grain, soda ash and other bulk commodities.

In addition, Union Pacific constructed 619 and rebuilt 785 cars in its shops in Omaha and at Albina, Oregon, near Portland. The company has spent $704-million on new locomotives, freight cars and auto racks over the last five years and has developed a fleet that is generally conceded to be the most modern in the industry.

Maintenance—Smooth, precisely-positioned track is one key to the success of a modern railroad. Heavy, high-speed trains continually cause fractional differences in the gauge, surface and alignment of the track, slowing the pace of trains if proper maintenance is ignored. To avert such problems, Union Pacific spends heavily to keep its track system in good shape. It is one of the few major railroads in the country that still has its sectionmen inspect the entire mainline on a weekly basis. Detailed knowledge of developing defects enables crews to correct problems promptly.

In 1978, Union Pacific spent $205.5 million for the maintenance of its roadbed. This included the reballasting of 1,313 miles of right-of-way, installation of 845,251 crossties and laying of 454 miles of rail, 329 miles of which was quarter-mile-long, continuous-welded rail. More than 41 percent of Union Pacific's mainline, which is 5,879 miles long, is now laid with continuous-welded rail. This track replaces 39-foot sections requiring 270 joints to the mile, all of which posed potential problems.

The Railroad continued to invest heavily in maintenance of its equipment, spending $191.4 million in 1978, $46 million of which was for major overhauls.

Computerization—During the year, Union Pacific Railroad expanded and refined its computer systems to improve operating efficiencies.

The Railroad continued to develop its Terminal Information System (TIS), which keeps an up-to-the-minute inventory of all freight cars in the terminal, allowing more expeditious car and train movements. TIS was installed at the new Hinkle classification yard and the Pocatello terminal during 1978, and is planned for installation at North Platte's new westward classification yard and the Portland terminal during 1979.

Installation of the Outbound Waybilling System, which supports waybill and freight bill preparation, was completed in 1978. This system speeds up issuance of freight bills and significantly reduces the possibility of billing errors.

The Railroad also extended its computerized car distribution system to 76 terminals. The system enables three centralized car distribution offices to direct and monitor the movement of empty cars on the Union Pacific system, improving equipment use while reducing fees paid to other railroads for the use of their cars.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Champlin Petroleum Company earnings rebounded dramatically from a sluggish first half to achieve record results in 1978. Net income was $95.1-million, a gain of 13 percent over 1977 earnings of $84.4 million. More than 65 percent or $62 million of total net income was achieved in the last half of the year. Revenues were $1.3 billion, up 17 percent over the $1.1 billion reported in 1977. The company's strong performance reflected rising refined-product prices in the last half of 1978 and increased natural gas output. These positive factors are expected to carry over into 1979.

As part of its program of diversified growth, Champlin participated in a number of significant petroleum discoveries and increased its natural gas reserves at the end of 1978 while maintaining strong levels of production. It also increased the efficiency of its Corpus Christi and Wilmington refineries, and with its joint-venture partners prepared for the start of production at the Corpus Christi petrochemical complex at the end of this year.

Exploration—Champlin expanded its exploration, development and acquisition programs to arrest natural decline of its hydrocarbon reserves. Exclusive of the nearly 7.5-million acres held in the Union Pacific land grant, Champlin increased its total lease holdings in 1978 from 1.4-million to 1.6-million acres. During the last three years, the company more than doubled its non-land grant holdings from 772,000 to 1.6-million acres.

In 1978, the company spent $163 million on exploration and production, up 33 percent over the $123 million invested in 1977. The company participated in 136 net wells (exploratory and development), of which 110 were successful. It drilled 27 net exploratory wells, of which 10 or 37 percent were successful. Champlin's chief areas of discovery and development were in the Rocky Mountain region, Canada, Kansas and Texas.

Overthrust Belt—A broad belt of complex geology running through Utah, Wyoming, Montana and north into Canada, the Overthrust Belt since 1975 has become the focus of the most intensive and productive drilling activity in the U.S. Much of this activity has taken place on the southern part of the Overthrust within the 40-mile-wide land grant, in which Union Pacific owns alternate 1-mile-square sections. To date, 12 new fields have been discovered in the Overthrust—several of which

Pumping tirelessly at sunset, Champlin's wells at the Wilmington Field, *above*, near Long Beach, California, produce 15,900 barrels a day. Champlin's aggressive exploration program has produced important discoveries in Texas, Kansas, Canada and the Rocky Mountain region. A significant find in which Champlin participated in 1978 was the Whitney Canyon No. 2 natural gas well, *right*, near the Aspen Mountains on the Overthrust Belt in southwestern Wyoming. Whitney Canyon No. 2 flowed at 20-million cubic feet a day and holds the potential of being part of a giant field, with a multi-trillion cubic foot gas reserve at a number of levels.

produce from two or more formations—and Champlin has participated in 10 of these discoveries. The company has achieved approximately an 18-percent participation in discoveries on the land grant through a 100-percent working interest in retained acreage, and a 15-percent royalty interest in the remainder.

A recent major discovery in the Overthrust Belt—Whitney Canyon in southwestern Wyoming—promises to be one of the most productive natural gas finds in the Rockies and may have total reserves of several trillion cubic feet of gas. The latest success in this region, the Carter Creek discovery eight miles north of Whitney Canyon, may be part of a 15-mile-long structure linking the two areas. The largest part of this anticipated structure appears to be on the land grant and Champlin expects to have as much as an 18-percent stake in that portion.

One of the most important Overthrust discoveries, Clear Creek in the northern portion of the 19,000-acre Painter Reservoir Unit, also in southwestern Wyoming, tested 25-million cubic feet of gas and 700 barrels of oil a day from the Nugget Formation. Champlin should realize approximately a 22-percent interest in Clear Creek's production.

Elsewhere in the Overthrust Belt, Champlin's net production from three wholly-owned wells and from its working and royalty interests in the Pineview Field in northeast Utah averaged 4,070 barrels a day in 1978. In addition, in the third quarter, the company acquired from Oxy Petroleum Inc. an additional 10-percent interest in Pineview and Elkhorn properties, which increased Champlin's output by 800 barrels a day. Champlin's other principal areas of activity in the U.S. and Canada include:

Table Rock/Higgins—This highly productive natural gas region in the Greater Green River Basin of south-central Wyoming continued to provide Champlin with an expanding gas reserve. By the end of 1978, the company was involved in 44 wells, 18 of which are productive from depths below 15,000 feet. Champlin holds nearly a 50-percent interest in the fields' proven gas reserve, which was 826-billion cubic feet at the end of 1978.

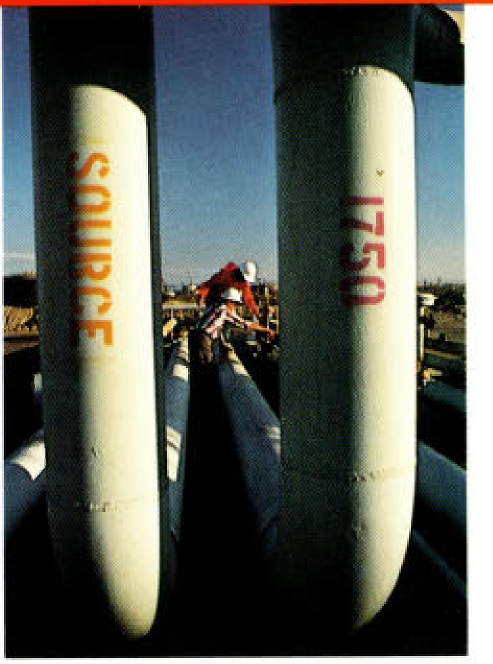
Canada—West Pembina, near Edmonton, Alberta, has been the scene of intense exploration for two years, ever since experts termed the original oil discovery the most promising Canadian find in 10 years. Champlin has 11,000 acres under lease in the West Pembina area, and during 1978 made a significant oil discovery on this acreage. At Erith, also in Alberta, the company has 7,700 acres under lease and a 25-percent interest in three gas wells. It is anticipated that gas production will begin in late 1982 or early 1983 when Gulf Oil Canada, the operator, completes construction of a gas-processing plant with its partners.

Texas and Kansas Fields—Champlin substantially expanded its drilling effort and, in turn, its natural gas reserves in the East Texas, South Texas and Mid-continent regions. During 1978, the company completed 12 producing wells in the Carthage Field in East Texas, seven producing wells in the Stratton Field in South Texas, and 15 producing wells in the Panoma Field in the Hugoton area of Kansas.

Offshore California—Champlin has interests in 10 offshore California tracts which it acquired in 1975 for $22.3 million. Four of these tracts are located in the Outer Banks area, 100 miles southwest of Los Angeles. To date, Champlin has participated in three wells on two Outer Banks tracts, none of which has been successful. Closer inshore, in the San Pedro area where Champlin has a 6.25-percent interest in one tract, nine of the 13 wells drilled have encountered oil. The feasibility of commercial development in this area is under evaluation.

Production—During 1978, Champlin announced that its reserves of crude oil, condensate and plant liquids at the end of 1977 were essentially unchanged, while its reserves of natural gas had increased 21 percent. This was achieved after the production of 20.8-million barrels of crude oil, condensate and plant liquids and 82.1-billion cubic feet of natural gas in 1977.

Although output from Ryckman Creek and Pineview Fields increased by 54 percent, declines from mature fields such as the Wilmington Field in Long Beach, California, caused Champlin's production of crude oil (including royalty production) to decline 4 percent, from 16.6-million barrels in 1977 to 15.9-million barrels in 1978. A summary of production and refinery runs is given on page 33. The company held Wilmington's decline to 9 percent, compared to a 13-percent decrease in 1977. Price relief from the Department of Energy enabled Champlin to carry out comprehensive production and maintenance work in this mature field, which was discovered in 1936.



Towering over the Corpus Christi ship channel, Champlin's refinery, *right*, produces 160,000 barrels of diversified refined products a day, which are transported by pipelines, barges and ships for marketing in the Southeast and East. Corpus Christi and Champlin's other refineries at Enid, Oklahoma, and Wilmington, California, produce 245,000 barrels a day. A secondary-recovery system, *above*, using 500,000 barrels of salt water daily, helps keep Wilmington Field crude oil flowing to Champlin's nearby refinery.

Champlin's drilling programs are primarily responsible for the higher natural gas reserve and the increase in gas production (including royalty production) from 82.1-billion cubic feet in 1977 to 91.6-billion cubic feet in 1978. The company's program to modernize its gas-processing plants helped it to sustain plant liquids production at 4.1-million barrels last year.

Manufacturing—Over the past five years, the company spent $308 million to expand its total refining capacity by 65 percent, to increase the number of crude oil grades it can process, and to upgrade the types of products it can refine. Champlin's Corpus Christi refinery is among the most versatile in the U.S. As a key result of Champlin's planning and expansion program, it is now capable of dedicating 55 percent of its production to refining gasoline—and 60 percent of this capacity to producing unleaded gasoline. These capabilities are well above the industry average and place Champlin in a position to respond quickly to the changing needs of the marketplace. In February, 1979, Champlin announced a $120-million modernization and expansion program at the Wilmington refinery, which, when completed in early 1981, will double crude oil capacity from 30,000 to 60,000 barrels per day. The program also will provide downstream processing capability for production of higher-value refined products such as unleaded gasoline, jet fuel and low-sulfur fuel oil. In 1978, the company raised its total refinery throughput to 228,257 barrels per day from 226,346 barrels in 1977.

Ethylene Complex—Construction of the $630-million joint-venture ethylene complex at Corpus Christi is proceeding toward its planned startup in late 1979. The joint-venture partnership formed in 1976 consists of Champlin (37.5 percent); ICI Americas Inc., a subsidiary of Imperial Chemical Industries Ltd. (37.5 percent); and Soltex Polymer Corporation, a subsidiary of Solvay & Cie (25 percent).

The new facility is designed to produce 1.2-billion pounds of ethylene a year, plus polymer-grade propylene, benzene and crude butadiene, which are key ingredients in plastics, synthetic rubber, synthetic fibers, anti-freeze and detergents. Champlin's partners expect to take more than 80 percent of the ethylene, along with one-third of the propylene. All of the benzene and the fuel by-products have been contracted to the partners or outside customers. With this built-in demand, coupled with an ability to run on the cheaper of the two feedstocks, naphtha or gas-oil, the cost-competitive facility should be well-positioned to generate an attractive return by the mid-1980's.

Champlin's $27-million cumene plant, now under construction adjacent to the Corpus Christi refinery, is on schedule and will begin production in 1980. A major industrial company has contracted to buy a substantial portion of the plant's output of 400-million pounds a year and other sales contracts are being negotiated. Cumene is a basic building block for high-performance plastics, home-building materials, such as laminates, and nylon.

Marketing—Champlin, which markets refined products through 950 service stations, benefited from strong demand in the last half of 1978, and from a significant increase in self-service stations. These stations, which tripled in number from 40 in 1976 to 126 in 1978, have enjoyed striking gains in gallons pumped and revenues generated. In its wholesale marketing effort, Champlin benefited from steadily rising demand for all refined products in the Gulf Coast marketing area.

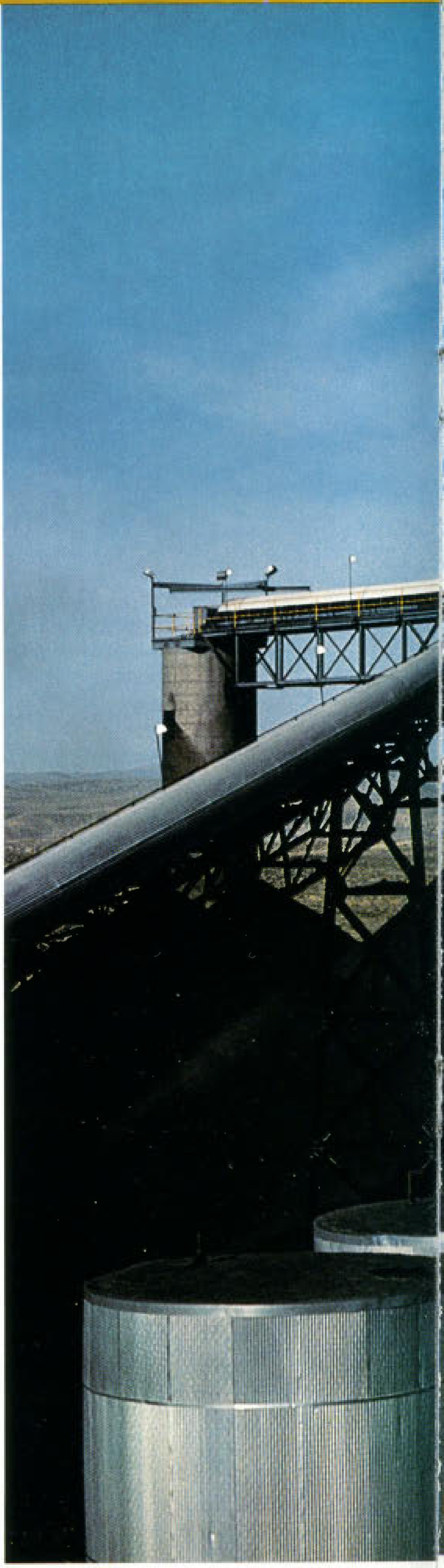
Dwarfing men and machines on the site, the 125-acre, 1.2-billion-pound-per-year ethylene complex at Corpus Christi nears completion. Champlin and subsidiaries of Imperial Chemical Industries Ltd. and Solvay & Cie are partners in the $630-million joint venture. Ethylene and other petrochemicals produced at the facility will be used in the manufacture of plastics, synthetic rubber and fibers, anti-freeze and building materials. Vital feedstocks will be supplied to the plant from Champlin's Corpus Christi refinery.

In 1978, Rocky Mountain Energy, in combination with its partners, made important strides toward developing two new coal mines, each of which has substantial reserves of low-sulfur coal. It embarked on a major expansion of its uranium joint venture at Bear Creek, in northeastern Wyoming, and laid the groundwork for new investments in uranium mining and milling operations elsewhere. The company also negotiated additional leases for development of its trona deposits. RME's earnings reached $27.6 million in 1978, up 19 percent over 1977.

Coal—The single most important source of RME's income from coal was the company's interest in the Medicine Bow Coal Company in south-central Wyoming. Medicine Bow, a joint venture with Arch Mineral Corporation, shipped 3.1-million tons in 1978, an increase of 10 percent over 1977. All of its production is committed under long-term contracts to three utilities—Northern Indiana Public Service Company, Iowa Public Service Company and Kansas Power and Light Company. Royalty income from coal produced on RME lands also rose in 1978.

Stansbury Coal Company, a joint-venture mine with Ideal Basic Industries, continued to experience operating difficulties in 1978. RME's net income for the fourth quarter was affected by a $3.5-million net after-tax charge, which represented a writeoff of a portion of its Stansbury investment, principally related to depleted and otherwise uneconomic seams.

Crushed coal at Rocky Mountain Energy's joint-venture Medicine Bow mine in Hanna, Wyoming, *right*, ready for loading onto a Union Pacific train. Medicine Bow dragline, *below*, removes nearly 80-cubic yards of overburden in a single scoop. An earthmover grades Black Butte mine site, *bottom*, in southwestern Wyoming. RME's largest joint-venture coal operation, it is scheduled to open later this year.



Two significant new coal operations are scheduled to come on-stream in 1979. The larger of the two is the Black Butte Coal Company, a joint venture between RME and Peter Kiewit Sons'. In December, Black Butte became the first major mine to receive a Federal mine permit under the Surface Mining Act of 1977. Black Butte is expected to start production during the latter part of 1979; full production is expected in 1981, when the mine's annual output should reach 6.3-million tons, nearly double the combined output of RME's joint-mining ventures in 1978. Virtually all of Black Butte's output will be sold to Commonwealth Edison plants in the Midwest under a long-term contract. The second mine scheduled to go into production in 1979 is Carbon County Coal Company in Hanna, Wyoming, a joint venture with Dravo Corporation of Pittsburgh. This underground mine is expected to produce 1.5-million tons annually. Its output has been contracted to Northern Indiana Public Service Company under a 20-year agreement.

Rocky Mountain Energy also has been active in developing other possible joint-venture mines. Five mine sites have been designated in southwestern Wyoming with combined coal reserves of approximately 220-million tons for future development within the next five years. Only two will require Federal coal leases to complete blocks large enough to make mining feasible.

Uranium—Despite governmental and public concerns over U.S. policy regarding nuclear development, 88 new nuclear plants are currently under construction and will more than double the nation's nuclear generating capacity by 1985.

Bear Creek Uranium Company, an RME-operated joint-venture mine-and-mill complex with Mono Power, a subsidiary of Southern California Edison, consistently operated above its rated capacity of 1,000 tons per day, and its mined ore was of a higher grade than had been anticipated. In November, RME began an expansion, scheduled to be completed by the spring of 1979, that will raise the mill's base capacity to 2,000 tons per day. The major portion of Bear Creek's output is committed to Southern California Edison and San Diego Gas and Electric under long-term contracts. Most of the capacity currently being added will be used to process ore for Kerr-McGee Corporation.

RME is also developing other uranium properties. During 1978, it operated a pilot plant at Nine Mile Lake in central Wyoming that successfully employed in situ leaching, a sophisticated, subsurface method of recovering uranium without disturbing large tracts of land. Late in 1979, RME expects to begin construction at this site of a uranium-recovery plant capable of producing up to a half-million pounds of uranium oxide annually. During 1979, RME also plans to pilot test in situ leaching in the Reno Ranch area of eastern Wyoming. Participants in these ventures with RME are Halliburton Services and Mono Power.

In the Copper Mountain area of central Wyoming, RME has identified substantial uranium deposits, estimated to be as much as 10-million pounds. With its partners in this project, Mono Power and Great Basins Petroleum, it is evaluating the feasibility of constructing a major mine-and-mill complex that could produce 500,000 to 1-million pounds of uranium annually. In partnership with Mono Power, RME also is conducting an extensive uranium exploration program. Activities in 1978 included exploration in seven states at a cost of $5.5 million.

Natural Soda Ash—In the Green River Basin of southwestern Wyoming, Rocky Mountain Energy owns a half interest in the largest trona deposit in the world. Natural soda ash, which is refined from trona ore, is an increasingly valuable mineral and a primary ingredient in the production of glass. It is also extensively used in the production of pharmaceuticals, biodegradable detergents and baking soda. The use of natural soda ash has risen dramatically in recent years because of environmental problems and high energy costs associated with manufacturing synthetic soda ash. In 1978, more than 80 percent of America's soda ash came from trona compared to 30 percent 10 years ago.

The four companies presently mining trona under royalty arrangements with RME are Stauffer Chemical Company of Wyoming, in which RME has a 49-percent equity interest, FMC Corporation, Allied Chemical Company and Texasgulf Inc. During 1978, RME concluded a lease agreement with Tenneco Oil Company, which plans to construct a one-million-ton-per-year soda ash plant, scheduled to go into production in the early 1980's. During 1978, additional trona reserves were leased to Allied Chemical and to Stauffer Chemical of Wyoming.

An intricate network of conveyor belts at Stauffer Chemical Company of Wyoming's mine in Green River, *above*, carries thousands of tons of trona ore and its by-product, refined natural soda ash, daily to and from the company's processing plant. Stauffer of Wyoming, in which Rocky Mountain Energy has a 49-percent interest, is one of four companies actively mining in the Green River area, which holds the largest trona reserve in the world. *At left*, a shuttle car loads trona ore 900 feet below the surface at the Stauffer mine. *At far left*, the Bear Creek Uranium Company, another RME joint venture, is mining uranium reserves in northeastern Wyoming. Bear Creek's adjacent mill produces nearly a half-million pounds of refined uranium ore, or yellowcake, annually. Its open pits descend to depths of 150 feet.

Upland Industries Corporation

For Upland Industries Corporation, 1978 was a landmark year, with revenues and earnings reaching the highest levels in the company's history. Virtually all of Upland's geographic markets achieved significant sales increases. This reflected the strengthening of the marketing staff, the implementation of new marketing programs, and the realignment of Upland's corporate organization.

Net income for the year was $8.48 million, double that of $4.22 million in 1977. Revenues from sales, royalties and leasing reached a new level of $34.6-million, compared with $26.6 million for 1977, an increase of 30 percent.

As manager of Union Pacific's extensive land holdings, Upland administers more than 1.2-million acres of land and 7-million acres of mineral rights in 13 growing western states, from Nebraska to the West Coast. This acreage, which includes the land grant and purchases made in recent years, provides a source of choice industrial and commercial sites near expanding urban centers. Additionally, certain parcels are becoming increasingly suitable for residential site developers, as processing and manufacturing facilities relocate closer to western energy reserves and transportation centers.

The company is currently carrying out an extensive study of its land holdings to identify opportunities for future joint ventures and to develop new and innovative land uses.

Industrial Parks—Upland currently owns, develops and markets prime sites in 59 rail-served industrial parks and districts. Each park incorporates convenient access roadways, proper grading and drainage, and essential power and water facilities. In 1978, effective marketing of these strategically-located industrial properties enabled Upland, in cooperation with Union Pacific Railroad, to attract over 150 new facilities to sites served by the Railroad. Resulting freight revenues are expected to exceed $25 million annually. Seattle, Salt Lake City, Los Angeles and Denver led brisk sales of Upland sites during the past year. In the last five years, Upland, in concert with the Railroad, attracted over 800 facilities to rail-served sites, resulting in freight revenues of over $100 million annually.

Upland's industrial sites draw a broad cross-section of commercial customers, including manufacturing, warehousing and distribution businesses. For example, in the company's 1,800-acre Centennial Park in Salt Lake City, sites were selected in 1978 for construction of a $15-million General Telephone and Electronics' office and production facility; a $5-million Pepsi-Cola bottling plant and warehouse; a $3-million office and inventory warehouse; a $1.5-million Miller Beer products office and distribution facility; and a $1.8-million photographic film sales and processing center.

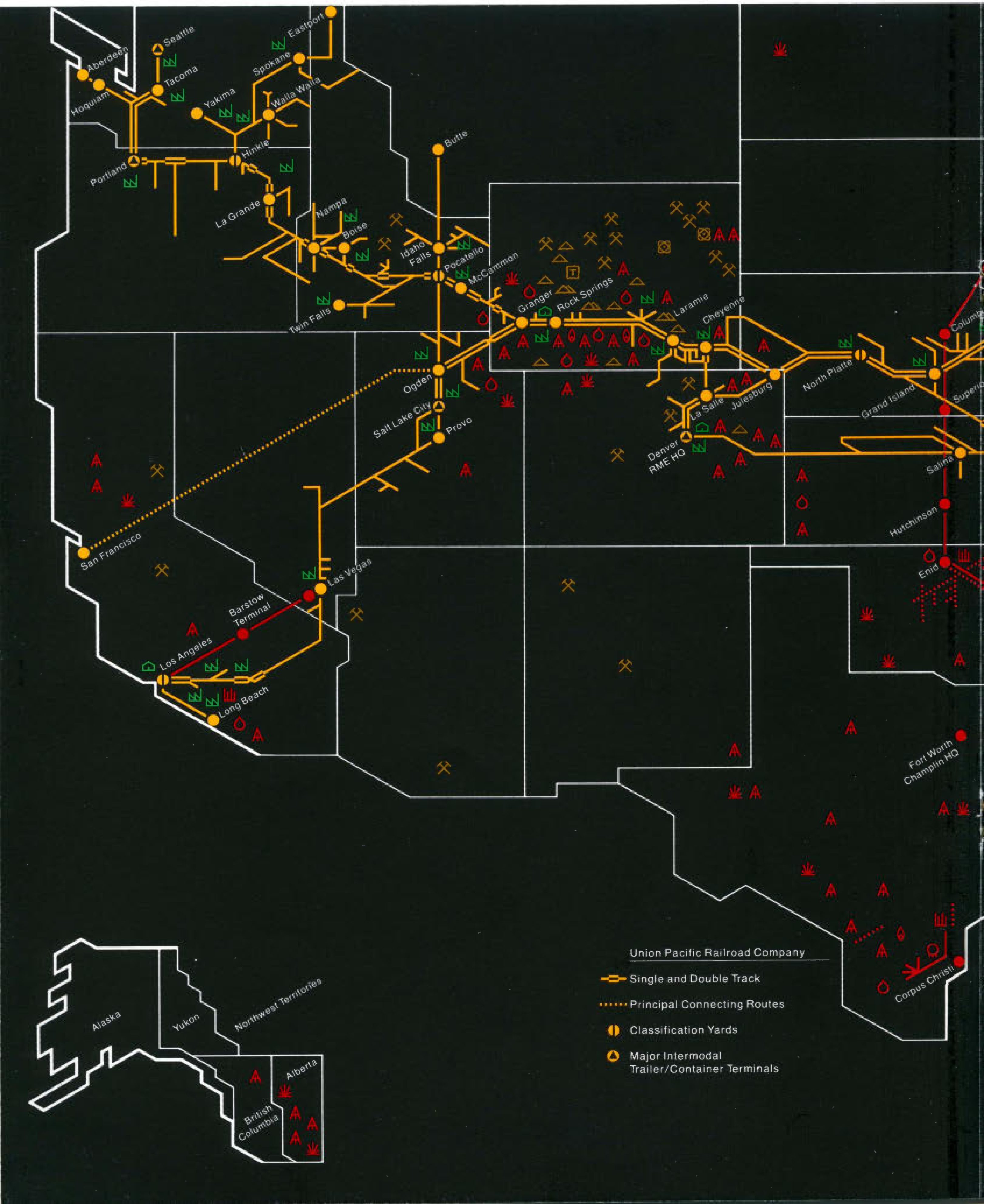
In Kent, Washington, five sites were selected for new facilities in the 137-acre Upland Industrial Park. They include: a $10-million Sears' merchandising distribution center; a $3-million public warehousing facility; a $2.8-million steel processing and distribution facility; a $2.8-million merchandising distribution center; and a $1.6-million specialty pipe manufacturing plant and warehouse. Elsewhere, projects planned for Upland sites include a $4-million liquor products distribution warehouse in Aurora, Colorado; a $3.4-million tire distribution center in Omaha; a $3-million office and inventory warehouse in Portland; and a $2.3-million sofa-bed manufacturing facility in City of Industry, California. All of these sites are served by Union Pacific Railroad.

Planning is continuing for properties in Las Vegas, Nevada, and Wilmington, California, which hold high potential. Upland and Union Pacific Railroad own a prime 320-acre site adjacent to the hotels and casinos in downtown Las Vegas. And, in Wilmington, a 1,000-acre waterfront property is strategically located near the burgeoning port areas of Los Angeles and Long Beach. Development of new industrial sites on properties Upland now holds is planned in several major urban areas, including a 108-acre expansion at Centennial Park in Salt Lake City; 52 acres at Cheyenne; 80 acres at City of Industry, California; 69 acres at Long Beach; 120 acres at Portland; and 172 acres near Seattle.

Residential Site Development—Upland continued to market residential sites in Wyoming to relieve housing shortages created by the rapid expansion of energy- and mineral-related activities in the state. Working in close cooperation with state and local planning officials, the company has developed 1,400 sites for sales to local and national builders since the program began. A total of 6,700 acres has been made available by Upland for industrial, commercial, residential, public and community purposes since 1970.

Planning for Upland's prime 1,000-acre holdings in the heart of the busy Los Angeles/Long Beach port area, *outlined at upper left,* will maximize future industrial, commercial, and port-related uses of the site. Sales and leasing of Upland industrial sites in Seattle's West Valley Industrial Park, *above*, which is served by Union Pacific Railroad, were strong throughout 1978. An adjacent 192-acre property, extreme right in photograph, will be developed this year. Spur lines of the Railroad in the Denver Industrial Park, *right*, serve a container manufacturer and 90 other customers in this rapidly-growing facility. Upland's successful marketing program, in cooperation with the Railroad, attracted 154 customers to its industrial parks in 1978.

Transportation, Energy and Natural Resources




Rock Rapids
Omaha UPRR & Upland HQ
Council Bluffs
Lincoln
St. Joseph
Kansas City
Topeka
St. Louis
Oklahoma City
Chicago
Corporate HQ
New York
Champlin Petroleum Company
Major Petroleum Producing Areas
Petroleum Drilling Activities
Petroleum Seismic Research
Refineries
Gas Processing Plants
Petrochemical Complex
Crude Pipelines
Product Pipelines and Terminals
Rocky Mountain Energy Company
Coal Production/Distribution
Coal Projects Pending/Planned
Trona Activities
Uranium Operations
Mineral Exploration
Upland Industries Corporation
Major Commercial/Industrial Properties
Sites for Residential Developers

Human Resources—The continued growth of Union Pacific depends on the availability of able and dedicated men and women, expert in their fields and capable of taking on new challenges. The Corporation maintains a variety of training and educational programs to improve the skills and to widen the horizons of its more than 30,000 employees, whose total salaries, wages and benefits amounted to $817 million last year.

In 1978, more than 5,000 employees participated in courses offered by Union Pacific Railroad, which maintains three fulltime training facilities at Cheyenne, Salt Lake City and Omaha. At Cheyenne, classes were held for over 300 prospective locomotive engineers; a unique air-brake trainer was used to simulate actual operating situations. The Railroad also continued its Officer Training Program in which candidates for future managerial assignments receive classroom and departmental training over a 2- to 15-month period.

Champlin Petroleum's Corpus Christi apprenticeship program, which runs from 33 to 60 months, upgrades technical skills through job and classroom training, and home study. Rocky Mountain Energy provides specialized training for geologists, engineers and other employees; and Upland provides outside courses and seminars related to real estate for many of its employees.

More than 1,300 employees acquired job-related skills or enhanced existing ones through participation in Union Pacific's Tuition Assistance Program. Under this program, the Corporation reimburses employees for the cost of taking educational courses that are related to their work. Union Pacific spent nearly $300,000 for this purpose in 1978. As part of the Corporation's efforts to insure strong future leadership, executives participated in management development programs at the Carnegie-Mellon Institute, Cornell, Harvard, M.I.T., University of Pittsburgh, Stanford and the University of Utah. All components of the Corporation are also striving to increase the number of women and minority employees in hourly and salaried positions.

Community Relations—As responsible corporate citizens, Union Pacific's operating companies maintain a variety of civic and community relations programs. All four operating companies work closely with community leaders, planners and citizen groups to make certain that their ventures will have a beneficial impact on the communities in which they will be located. Special care is taken to ensure the availability of adequate housing and community services when undertaking any substantial new investment.

Union Pacific Railroad's "Operation Lifesaver" program has helped to reduce accidents at rail crossings by 19 to 30 percent in several western and midwestern states. The program, which was developed jointly with western railroads and government agencies, is a comprehensive educational campaign that uses film and other materials developed by the Railroad's public relations department. Because of the program's success, the National Transportation Safety Board has recommended its adoption nationwide.

The Railroad's Youth Recognition Programs in Nebraska and Wyoming select a high school senior each month, on the basis of leadership and citizenship, as the state's youth of the month. Monthly winners receive a $100 savings bond and are eligible for consideration as the state's youth of the year and a $1,000 scholarship. In 1978, 101 young members of Future Farmers of America and 4-H Clubs in the region served by Union Pacific Railroad were awarded scholarships of $400 each.

Union Pacific Railroad also continued its program of donating vintage railroad equipment to local communities and historical societies. Old depots were given to Mead, Nebraska, and Saratoga, Wyoming, during 1978, and a 125-ton diesel switch engine was donated to Utah to power the state's excursion train running from Heber City to Bridal Veil Falls. Forty Union Pacific steam locomotives had previously been given to various parks and recreation areas around the country. The Railroad also provided a passenger train for the Denver Symphony's five-day concert tour of Wyoming and Idaho.

Environmental and Conservation Activities—As a company engaged in the development of natural resources, Union Pacific Corporation has a special responsibility to preserve the lands and ecological systems in which it interacts. Union Pacific companies spent $11-million on various programs to improve and conserve the environment during 1978.

Prominent among these activities were the reclaiming of 267 acres of land that had been mined by Rocky Mountain Energy's Bear Creek uranium joint venture in Wyoming and the reclaiming of 229 acres by the Medicine Bow Coal

Union Pacific Corporation in 1978 received the first annual award, *left*, from C. I. T. Financial Corporation for innovative corporate contributions programs supporting higher education.

Training and development programs broaden Union Pacific employees' educational backgrounds and prepare them for greater responsibilities. On completion of the Railroad's Officer Training Program, *far left*, men and increasing numbers of women will assume management responsibilities.

Reclamation of mined areas during 1978 by Rocky Mountain Energy included 267 acres at the company's Bear Creek Uranium mine-and-mill complex in northeastern Wyoming, *above*. Filled in with overburden, then resurfaced with topsoil to an average thickness of 16 inches, the area will be planted with grasses, plants and shrubs this spring.

Company. In both instances, the mined areas were filled in, surfaced with top soil and planted with a mixture of grasses and shrubs at a cost of more than $3,000 per acre. When reclamation work is completed, both areas will be as environmentally sound as they were before mining activities began.

Champlin Petroleum's environmental programs centered on various activities to check hydrocarbon emissions. At the Corpus Christi refinery, floating tank roofs were installed that reduced hydrocarbon vapor losses by 90 percent. A gas-treating system that limits hydrocarbon emissions also was installed at the company's Wilmington refinery. And operating managers from all Champlin refineries participated in seminars on methods for limiting environmental risks.

Union Pacific Railroad expanded its comprehensive program to conserve energy at its main facilities and administrative buildings in 1978. Through various programs initiated over the last five years, the Railroad has been able to reduce locomotive fuel consumption by 11 percent per gross ton-mile.

Corporate Contributions—During 1978, the Union Pacific Foundation continued its support of a broad range of educational, cultural and philanthropic institutions. Total Foundation grants, which were $2.4 million in 1978 compared with $1.8 million in 1977, were dispersed to more than 500 organizations in the states in which Union Pacific does business. Among the projects funded were the installation of a telephone switchboard for the blind at the Braille Institute of America, Los Angeles; the purchase of an intensive-care unit for the newborn at Primary Children's Hospital in Salt Lake City; and a grant to the Plains Indian Museum at the Buffalo Bill Historical Center in Cody, Wyoming.

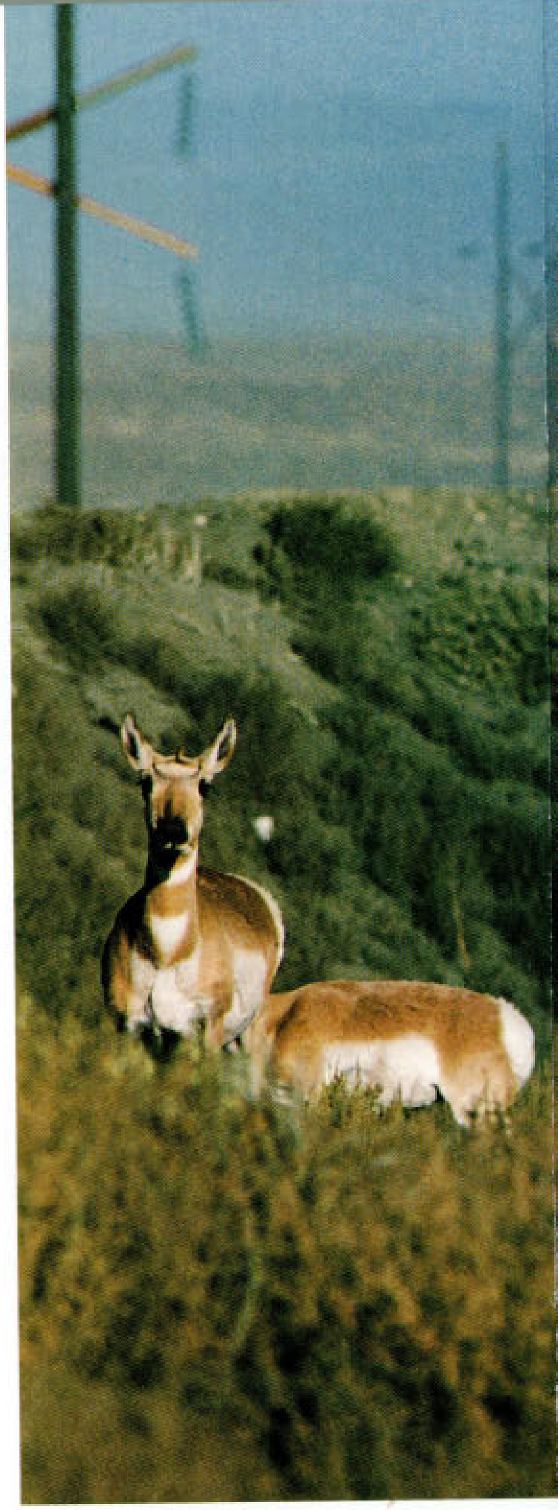
An important aspect of the Foundation's educational giving is the priority it gives to projects that will result in continuing savings that far exceed the amount of the grant. Because of its emphasis on this approach, Union Pacific became the first recipient of a new award given by C.I.T. Financial Corporation to recognize the American company that had, in the judgment of its jurors, initiated the most innovative program in support of higher education. The award was developed to honor the 25th anniversary of the Council for Financial Aid to Education, which selected Union Pacific from 68 companies under consideration. Formally presented on June 14, 1978, the award was a $10,000 donation to the College of Idaho in Caldwell, Idaho, the institution designated by the Foundation.

Among the money-saving projects that caught the attention of the Council for Financial Aid to Education were those funded by grants to Occidental College in Los Angeles for a computerized college information system; to Rockhurst College in Kansas City, Missouri, for the installation of energy-saving thermal glass windows; and to the University of Portland to upgrade its electrical system and thereby significantly reduce its energy requirements.

Almost 150 educational institutions benefited last year from Union Pacific's Matching Gifts Program. The program is designed to encourage employee participation in the support of education. In 1978, the Corporation matched, dollar-for-dollar, individual employee gifts of up to $2,000 to accredited, tax-exempt private educational institutions beyond the elementary school level. In December, 1978, the Board of Directors voted to expand this program by raising the Corporation's matching grant to double the contribution of each employee.

Union Pacific Railroad also gave scholarships of $400 each to 106 children of employees in 1978. The scholarships were awarded on a competitive basis.

Management Changes—Union Pacific Corporation made various executive appointments during 1978. William F. Surette, who had been Vice President-Finance for Union Pacific Corporation since 1973, was elected Senior Vice President-Finance. Richard W. Anthony, who had been Director of International Public Relations for Ford Motor Company, was elected Vice President-Corporate Relations. Charles L. Eaton, who had been Vice President-Finance and Administration of the Rocky Mountain Energy Company, was elected Vice President-Corporate Planning. Harry B. Shuttleworth, who had been Treasurer since 1969, and Chester A. Rose, who had been Controller since 1975, were elected vice presidents.



Antelope play near RME's joint-venture Medicine Bow Coal mine. Since the mine started up in 1975, wildlife has continued to thrive as an extensive reclamation program restores the land to its premining condition. RME's Environmental Department continually reviews its operations to ensure that its activities are ecologically sound and in harmony with nature.

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Partner, Brown Brothers
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Of Counsel, Shea Gould
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[2] Member of the Audit Committee
[3] Member of the Executive Compensation Committee
[4] Member of the Trust Investment Committee

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Uranium

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William I. Kennedy
Vice President
Special Projects

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Charles R. Burris
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C. Barry Schaefer
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Vice President
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Vice President
Business Development

Byron D. Strattan
Vice President
Law

Charles R. Burris
Director of Engineering

The following comments are intended to provide an overview of operating results and selected supplementary financial information, which should be read in conjunction with the other sections of this report. A ten-year summary of key financial data appears on page 44.

Operating Results
Revenues of $2.99 billion were $435.1 million or 17 percent higher than 1977. Net income rose to a new high of $264.1 million, up 19 percent from 1977 earnings of $221.9 million. Earnings per common share in 1978 were $5.55 compared to $4.68 in 1977, a 19-percent gain.

The 1978 growth in net income was essentially due to greater volume from expanded or new business operations in each of the business segments and improved prices for refined products and natural gas.

Return on average stockholders' equity increased to 12.0 percent for 1978 from 10.9 percent for 1977. Net income as a percent of revenues for 1978 was 8.8 percent compared with 8.7 percent for 1977.

Operating cash flow advanced 17 percent in 1978 to $526.6 million from the 1977 level of $449.5 million. This positive trend helped to finance a substantial portion of the increased capital investment program.

Contributions to revenues and net income by business segment for the years ended December 31, 1978 and 1977 are set forth below:

Revenues

Millions of Dollars		1978		1977
Transportation	**$1,528.7**	**51.1%**	$1,313.6	51.4%
Oil and gas	**1,330.7**	**44.5**	1,141.0	44.7
Mining	**69.1**	**2.3**	47.2	1.9
Land	**34.6**	**1.2**	26.6	1.0
Other income	**26.3**	**.9**	25.9	1.0
	$2,989.4	**100.0%**	$2,554.3	100.0%

Net Income

Millions of Dollars		1978		1977
Transportation	**$140.1**	**53.1%**	$116.3	52.4%
Oil and gas	**95.1**	**36.0**	84.4	38.0
Mining	**27.6**	**10.4**	23.2	10.5
Land	**8.5**	**3.2**	4.2	1.9
Corporate, net	**(7.2)**	**(2.7)**	(6.2)	(2.8)
	$264.1	**100.0%**	$221.9	100.0%

Transportation earnings increased $23.8 million or 21 percent over 1977. Revenues of $1.53 billion were an improvement of $215.2 million (16 percent) from 1977 primarily as a result of significant revenue ton-mile gains in grain, coal, motor vehicles and parts, intermodal trailer traffic, and soda ash. Revenue ton-miles in 1978 rose to 68.2 billion, 12 percent above the 60.9 billion in 1977, while carloadings increased 5 percent. Revenues for 1978 included freight rate increases aggregating $85.6 million; however, these increases were virtually offset by the effects of inflation.

Transportation operating expenses rose $178.1 million, up 16 percent from 1977, and included labor cost increases of $102.0 million. Higher wage rates and benefit costs accounted for $64.3 million and the remainder resulted from expanded traffic volume and maintenance programs. Materials and supplies, including diesel fuel, were $41.2 million higher than 1977, of which approximately one half resulted from inflation and the balance from traffic volume. Maintenance, including labor and other related costs, increased $63.3 million or 19 percent in 1978 to $396.9 million.

Oil and gas earnings were $95.1 million, up $10.7 million or 13 percent from 1977. Sales and royalties increased $189.7 million or 17 percent, due largely to higher sales volumes ($111.4 million) of refined products and natural gas, as well as improved price levels. Sales volume of refined products, notably gasoline, increased 10 percent over 1977 to approximately 3.1 billion gallons as a result of stronger seasonal demand in 1978.

Oil and gas operating costs rose $166.0 million or 17 percent over 1977. Most of the increase ($128.9 million) was associated with higher sales volumes and higher crude oil prices, together with increased costs of utilities, operating supplies, and maintenance. Expanded oil and gas exploration and production activities caused a $13.7 million increase in depreciation, depletion and amortization.

Mining net income was $27.6 million, up $4.4 million or 19 percent from 1977, despite the effect of a $3.5 million loss provision applicable to the Stansbury coal operation. Sales and royalties increased $21.9 million, or 46 percent over 1977, principally as a result of increased uranium and coal volume at Bear Creek and Medicine Bow. Earnings also benefited from bonus payments received under trona leases.

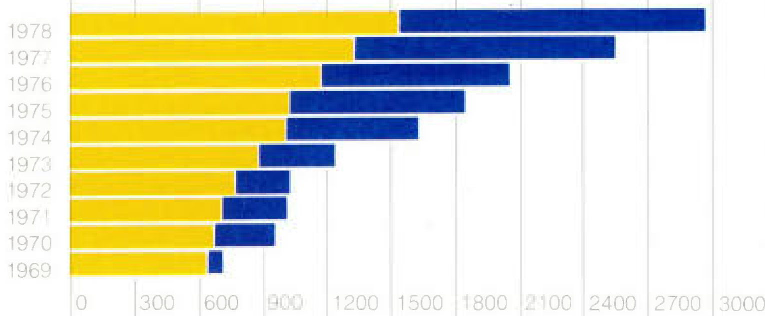
Land earnings were $8.5 million, more than double last year. Increased sales volume of industrial and commercial property in the Rocky Mountain and the Pacific Northwest areas was the principal factor in this improvement.

Financial Position
As summarized in the following table, Union Pacific maintained its strong financial position during 1978:

Millions of Dollars	1978	1977	% Increase (Decrease)
Working capital	**$ 184.5**	$ 130.6	41%
Net properties	**3,292.4**	3,039.5	8
Debt due after one year	**(843.1)**	(864.9)	(3)
Other assets (liabilities), net	**(347.8)**	(187.7)	—
Stockholders' equity	**$2,286.0**	$2,117.5	8%

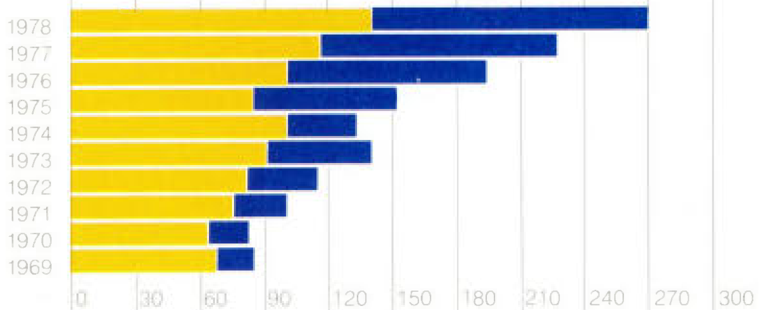
Revenues
Transportation
Natural resources and other

Consolidated compound annual growth rate 17%



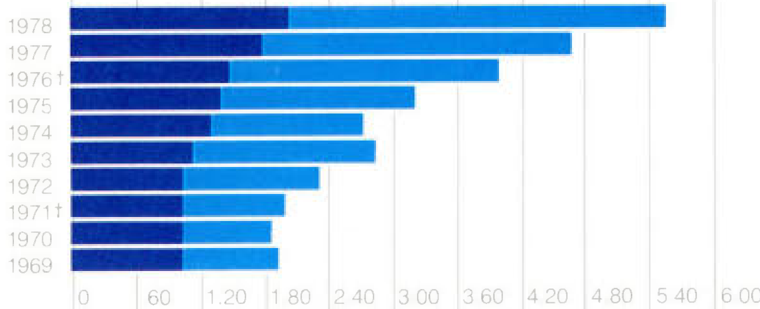
Income Before Extraordinary Item*
Transportation
Natural resources and other

Consolidated compound annual growth rate 14%

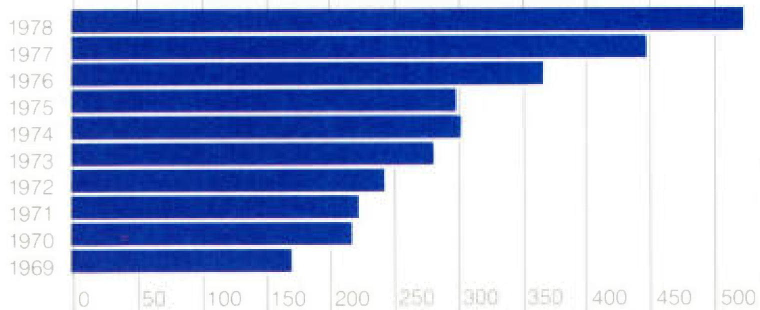


Earnings Per Common Share
Dividends

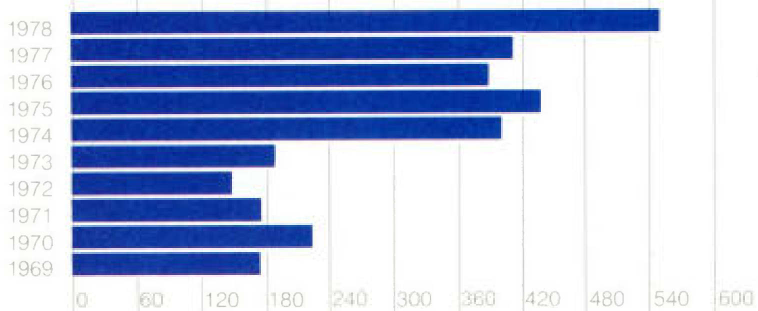
Compound annual growth rate of earnings per common share 13%



Operating Cash Flow



Capital Investments



All graphs in millions of dollars except per common share amounts

*Before corporate expenses which are unallocated

†Before extraordinary item

Capital Investments

During 1978, Union Pacific's capital investments aggregated $552.6 million, an increase of 32 percent over 1977. Direct capital expenditures totaled $424.2 million compared with $364.2 million in 1977. Union Pacific's share of capital investments of joint-venture and affiliated companies was $128.4 million in 1978 and $53.9 million in 1977. Total capital investments by business segment for the past two years are set forth below:

Millions of Dollars	**1978**		1977	
Transportation	**$241.7**	**43.8%**	$204.2	48.8%
Oil and gas	**275.4**	**49.8**	182.7	43.7
Mining	**31.5**	**5.7**	28.4	6.8
Land	**4.0**	**0.7**	2.8	0.7
	$552.6	**100.0%**	$418.1	100.0%

Transportation expenditures in 1978 include equipment acquisitions of $179.2 million, up $42.1 million or 31 percent from 1977. These 1978 expenditures included 120 locomotives and 2,910 freight cars compared with 90 locomotives and 2,087 freight cars in 1977. Expenditures for roadway and structures were $62.4 million in 1978 and $66.9 million in 1977. Most of the oil and gas capital investments for 1978 were expenditures for exploration and development programs in North America ($148.4 million), and $98.8 million for the Corpus Christi Petrochemical joint-venture facility scheduled for startup in late 1979. Joint-venture mining investments for 1978 included the Black Butte and Carbon County coal mines, which are scheduled to open in late 1979, and the expansion of the Bear Creek uranium complex.

Planned 1979 capital investments total $722 million, a 31 percent increase over 1978. Capital spending for energy, natural resource, and petrochemical projects account for 61 percent of this program and transportation the remaining 39 percent.

Financing

Short- and long-term borrowings aggregated $932.4 million at December 31, 1978, representing a net decrease during the year of $36.5 million, due mainly to the repayment of all commercial paper during 1978. New 1978 financing consisted of the sale of $51 million in railroad equipment trust certificates used to fund a portion of rolling stock acquisitions. Financing obtained by the Corpus Christi Petrochemical complex in 1978 enabled this affiliate to repay approximately $82 million of advances from Union Pacific. Furthermore, certain Railroad funds previously segregated for capital expenditures by escrow arrangements or government regulation provided an additional $107 million. These sources, together with funds from operations, reduced the need for further financing in 1978 while increasing working capital by $53.9 million at December 31, 1978. Borrowings to total capital employed decreased to 24.7 percent at December 31, 1978, compared with 27 percent at year-end 1977.

Stockholders' Equity

Stockholders' equity of Union Pacific aggregated $2.3 billion at December 31, 1978, an increase of $168.4 million over last year. Book value per common share also increased $3.44 to $47.98 at December 31, 1978. The 47,591,922 shares of common stock outstanding were held by 68,456 stockholders of record on December 31, 1978, while the 233,800 shares outstanding of 4¾ percent convertible preferred stock, Series A, were held by 1,441 stockholders of record. The $14.9 million principal amount of 4¾ percent convertible debentures outstanding at year-end were held by 5,271 owners of record.

Common stock dividends declared during 1978 amounted to $98.7 million, up $14.6 million or 17 percent from 1977. On November 30, 1978, the Board of Directors raised the quarterly dividend rate 15 percent from $0.50 to $0.575 per share, or $2.30 per share on an annual basis. Common dividends per share increased from $1.775 per share in 1977 to $2.075 in 1978, the sixth consecutive annual increase. Union Pacific has paid dividends to its common stockholders for 79 consecutive years. Dividends of $0.475 per share were paid on outstanding convertible preferred stock in 1978 and 1977.

Dividends Declared by Quarters	**1978**	1977
Common Stock		
1st Quarter	**$.50**	$.425
2nd Quarter	**.50**	.425
3rd Quarter	**.50**	.425
4th Quarter	**.575**	.50

A preferred stock dividend of $.11875 per share was declared in each quarter of 1978 and 1977.

Market Price	**1978**		1977	
Common Stock	High	Low	High	Low
1st Quarter	**$48⅞**	**$40⅞**	$55	$47⅞
2nd Quarter	**50⅞**	**42¾**	58½	50¼
3rd Quarter	**55¾**	**42½**	57⅜	48
4th Quarter	**60¼**	**50¾**	50½	42⅞
Preferred Stock				
1st Quarter	**$17**	**$14½**	$19⅜	$16⅞
2nd Quarter	**17⅜**	**14¾**	20⅜	18
3rd Quarter	**19**	**15**	19⅞	16¾
4th Quarter	**20⅝**	**17½**	17½	15¼

1977 Operating Results in Retrospect

In 1977, revenues were $2.55 billion, an increase of $489 million or 24 percent over 1976. Net income in 1977 of $221.9 million was up $34.2 million or 18 percent from the 1976 income of $187.7 million before an extraordinary credit of $7.5 million. Earnings per share in 1977 were $4.68 compared with $4.02 before the special credit in 1976.

Transportation revenues increased $139.0 million or 12 percent over 1976, due mainly to an increase in ton-miles of freight moved in intermodal trailer traffic, coal, soda ash and motor vehicles and parts and general freight rate increases. Revenue ton-miles increased 7 percent to 60.9 billion. Sales and royalties rose $342.0 million due primarily to greater production from the Corpus Christi refinery, completed in late 1976, and sales price increases for oil and gas products.

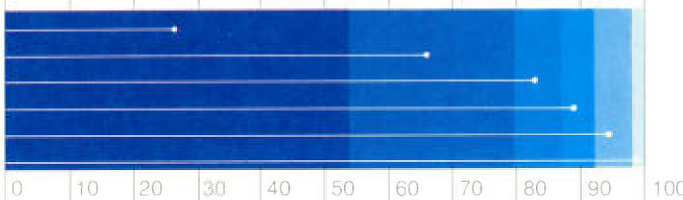
Costs and expenses increased $398.5 million. Crude oil and other petroleum raw materials rose $186 million, mainly as a result of refined products sales volumes and increased crude oil prices. Materials and supplies increases of $41.1 million reflected higher costs and greater maintenance activities. Utility and other costs increased $87.8 million, primarily as a result of inflationary impacts, expanded refining, coal and uranium production, and costs of real estate sold.

Allocation of Revenue

Union Pacific received revenues of $2,989 million in 1978 ... 100%

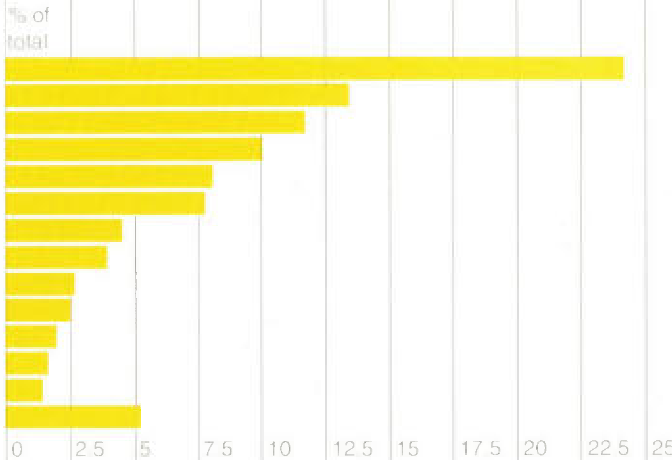
This revenue went for

Crude oil, supplies and other costs	$1,572	53%
Wages, salaries, payroll taxes and employee benefits	$ 786	26%
Taxes—Federal, state and local	$ 200	7%
Depreciation, depletion, amortization and retirements	$ 167	6%
Earnings reinvested in the business	$ 165	5%
Dividends to stockholders	$ 99	3%



Freight Traffic by Commodities in 1978

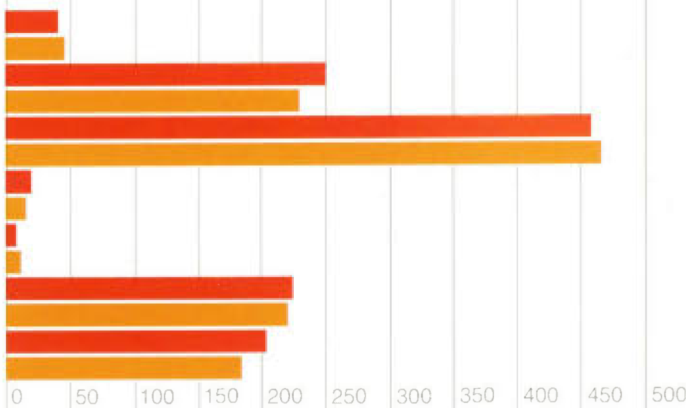
Freight Traffic by Commodities in 1978	Tons Carried	% Increase (Decrease) from 1977
Coal	23,125,168	13.6
Farm products	13,371,946	11.7
Soda ash, other chemicals and allied products	11,722,394	7.6
Food and kindred products	9,925,148	1.4
Nonmetallic ores	8,059,703	12.5
Lumber, wood products, furniture and fixtures	7,797,473	(1.1)
Iron and metallic ores	4,745,802	(1.9)
Stone, clay and glass products	3,868,889	2.8
Primary metal products	2,591,801	10.7
Intermodal trailer traffic	2,526,492	8.3
Pulp, paper and allied products	2,247,303	2.8
Motor vehicles and parts	1,959,476	13.8
Petroleum products and coke	1,778,682	6.1
Miscellaneous	5,189,840	(4.4)
	98,910,117	7.1



Summary of Production and Refinery Runs

■ 1978
■ 1977

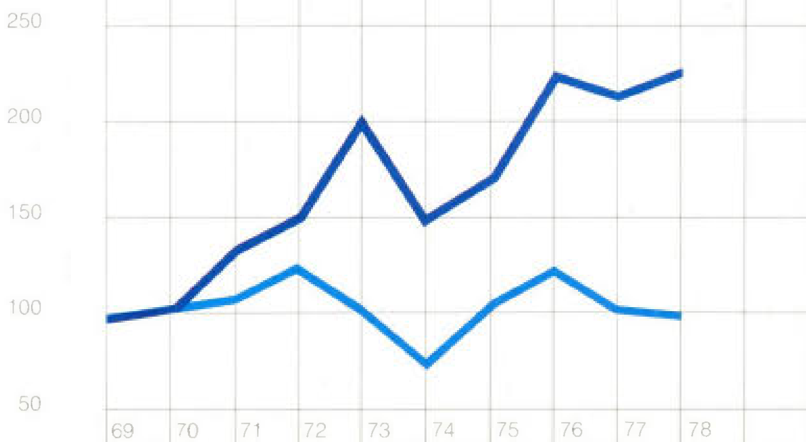
	Daily average in thousands
Net crude oil and field condensate,	43,684
in barrels, including royalty production	45,580
Net interest in gas from all sources,	251,000
in thousand cubic feet, including royalty production	225,000
Gas processed,	461,759
in thousand cubic feet	467,549
Plant products recovered,	21,944
in barrels	21,034
Net interest in plant products from all sources,	11,103
in barrels, including royalty production	11,346
Net production from refineries,	228,257
in barrels	226,346
Petroleum product sales,	204,787
in barrels	186,783



UPC Stock Price vs. Dow Jones Industrial Index Since Formation of the Corporation

■ Union Pacific common stock
■ Dow Industrial Index

This chart compares the year end price of Union Pacific common stock to the Dow Jones Industrial Index on a common scale in which 1969=100. The price of Union Pacific's stock has more than doubled over the past ten years.



Statement of Consolidated Income

Union Pacific Corporation and Subsidiary Companies

	Thousands of Dollars	
	1978	1977
Revenues		
Transportation	**$1,528,739**	$1,313,567
Sales and royalties	**1,434,422**	1,214,849
Equity and other income	**26,267**	25,879
Total	**2,989,428**	2,554,295
Costs and Expenses		
Salaries, wages and employee benefits	**785,877**	668,026
Crude oil and other petroleum raw materials	**762,653**	654,729
Materials and supplies	**364,275**	314,646
Depreciation, depletion, amortization and retirements	**166,801**	147,629
Utilities	**112,869**	100,915
Interest expense	**68,342**	66,817
State and local taxes	**66,956**	60,045
Other costs	**264,076**	203,499
Total	**2,591,849**	2,216,306
Income Before Federal Income Taxes	**397,579**	337,989
Federal Income Taxes (Note 5)	**133,469**	116,080
Net Income	**$ 264,110**	$ 221,909
Earnings Per Common Share	**$ 5.55**	$ 4.68
Dividends Per Common Share	**$ 2.075**	$ 1.775

The accompanying accounting policy disclosures and notes to financial statements are an integral part of these statements.

Statement of Consolidated Financial Position

Union Pacific Corporation and Subsidiary Companies

	Thousands of Dollars	
December 31	**1978**	1977
Assets		
Current Assets		
Cash (Note 6)	**$ 21,521**	$ 25,250
Temporary cash investments (Note 3)	**160,485**	4,459
Accounts receivable—net	**337,850**	322,198
Inventories (Note 2)	**195,491**	192,300
Deferred Federal income tax benefit (Note 5)	**—**	29,514
Other current assets	**52,746**	37,386
Total	**768,093**	611,107
Investments (Note 3)		
Investments in and advances to affiliated companies	**116,810**	117,558
Other investments	**62,256**	59,474
Land held for future development, at cost	**46,318**	51,559
Total	**225,384**	228,591
Properties (Notes 4 and 6)	**4,442,106**	4,168,751
Less accumulated depreciation, depletion and amortization	**1,149,667**	1,129,283
Net	**3,292,439**	3,039,468
Excess of Investment in Consolidated Subsidiaries over Equities in Recorded Net Assets	**71,740**	71,740
Other Assets and Deferred Charges	**79,455**	165,519
Total Assets	**$4,437,111**	$4,116,425
Liabilities and Stockholders' Equity		
Current Liabilities		
Short-term borrowings (Note 6)	**$ 42,000**	$ 54,000
Accounts and wages payable	**193,004**	143,557
Income and other taxes (Note 5)	**83,250**	57,214
Interest	**22,107**	21,537
Dividends	**28,109**	24,455
Debt due within one year (Note 6)	**47,278**	49,974
Other accrued and current liabilities	**167,843**	129,777
Total	**583,591**	480,514
Debt Due After One Year (Note 6)	**843,119**	864,935
Deferred Federal Income Taxes (Note 5)	**634,518**	570,413
Other Liabilities and Deferred Credits	**89,918**	83,034
Stockholders' Equity (page 37)	**2,285,965**	2,117,529
Total Liabilities and Stockholders' Equity	**$4,437,111**	$4,116,425

The accompanying accounting policy disclosures and notes to financial statements are an integral part of these statements.

Statement of Consolidated Changes in Financial Position

Union Pacific Corporation and Subsidiary Companies

	Thousands of Dollars	
	1978	1977
Source of Funds		
Operations		
Net Income	**$264,110**	$221,909
Charges not requiring current outlay of working capital		
Depreciation and other non-cash charges	**165,897**	135,199
Non-current deferred Federal income taxes	**57,721**	88,271
Working capital provided by operations	**487,728**	445,379
Proceeds from long-term financing	**51,000**	141,000
Changes in funds segregated for capital expenditures	**106,634**	(56,771)
Repayment of advances to affiliated companies	**95,970**	24,689
Other items—net	**36,875**	34,811
Total	**778,207**	589,108
Application of Funds		
Dividends declared	**98,787**	84,237
Reduction of long-term debt	**76,088**	59,438
Capital expenditures		
Transportation	**241,749**	204,189
Oil and Gas	**176,543**	147,243
Other	**5,906**	12,789
Advances to affiliated companies	**125,225**	37,765
Total	**724,298**	545,661
Increase in Working Capital During Year	**53,909**	43,447
Working Capital at Beginning of Year	**130,593**	87,146
Working Capital at End of Year	**$184,502**	$130,593
Components of Increases (Decreases) in Working Capital		
Cash	**$ (3,729)**	$ (17,593)
Temporary cash investments	**156,026**	1,869
Accounts receivable	**15,652**	84,396
Inventories	**3,191**	61,042
Deferred Federal income tax benefit	**(29,514)**	—
Short-term borrowings	**12,000**	(4,000)
Accounts and wages payable	**(49,447)**	(25,850)
Accrued liabilities, taxes and interest	**(64,672)**	(55,582)
Other—net	**14,402**	(835)
Increase	**$ 53,909**	$ 43,447

The accompanying accounting policy disclosures and notes to financial statements are an integral part of these statements.

Statement of Consolidated Changes in Stockholders' Equity

Union Pacific Corporation and Subsidiary Companies

	Thousands of Dollars	
	1978	1977
Capital Stock (Note 8)		
Preferred Stock, no par value (authorized 10,000,000 shares); 4¾% Convertible Preferred Stock, Series A; $10 stated value—outstanding		
Balance at beginning of year (281,189 shares in 1978, 357,177 in 1977)	**$ 2,812**	$ 3,572
Less shares converted into Common Stock (47,389 shares in 1978, 75,988 in 1977)	**474**	760
Balance at end of year (233,800 shares in 1978, 281,189 in 1977)	**2,338**	2,812
Common Stock, $5 par value (authorized 60,000,000 shares)—outstanding		
Balance at beginning of year (47,476,530 shares in 1978, 47,050,846 in 1977)	**237,383**	235,254
Issuance of shares upon		
Conversion of 4¾% Convertible Debentures and Preferred Stock (88,913 shares in 1978, 315,484 in 1977)	**445**	1,578
Exercise of stock options (26,479 shares in 1978, 110,200 in 1977)	**132**	551
Balance at end of year (47,591,922 shares in 1978, 47,476,530 in 1977)	**237,960**	237,383
Paid-in Surplus		
Balance at beginning of year	**108,887**	97,937
Issuance of Common Stock in excess of par upon		
Conversion of 4¾% Convertible Debentures and Preferred Stock	**2,093**	7,432
Exercise of stock options	**917**	3,518
Balance at end of year	**111,897**	108,887
Retained Earnings (Note 6)		
Balance at beginning of year	**1,768,447**	1,630,775
Net income	**264,110**	221,909
	2,032,557	1,852,684
Dividends declared (Note 8)	**98,787**	84,237
Balance at end of year	**1,933,770**	1,768,447
Total Stockholders' Equity	**$2,285,965**	$2,117,529

The accompanying accounting policy disclosures and notes to financial statements are an integral part of these statements.

Union Pacific Corporation and Subsidiary Companies					Thousands of Dollars
	1978	1977	1976	1975	1974
Revenues[a]					
Transportation	**$1,528,739**	$1,313,567	$1,174,544	$1,004,342	$1,000,266
Oil and Gas	**1,330,743**	1,141,044	826,746	731,528	591,128
Mining	**69,122**	47,190	24,809	19,145	5,594
Land	**34,557**	26,615	21,256	19,674	15,942
Equity and other income	**26,267**	25,879	17,609	75,413[b]	10,474
Total	**$2,989,428**	$2,554,295	$2,064,964	$1,850,102	$1,623,404
Operating Profit					
Transportation	**$ 252,087**	$ 214,991	$ 179,604	$ 148,294	$ 186,036
Oil and Gas	**186,264**	162,589	113,628	14,778[c]	30,276[c]
Mining	**15,621**[e]	17,783	10,210	7,883	1,701
Land	**10,734**	3,509	5,865	3,239	3,640
Total	**$ 464,706**	$ 398,872	$ 309,307	$ 174,194	$ 221,653
Equity and other income	**26,267**	25,879	17,609	75,413[b]	10,474
Interest expense	**(68,342)**	(66,817)	(60,672)	(48,352)	(39,992)
Corporate expenses	**(25,052)**	(19,945)	(19,063)	(13,678)	(11,551)
Income Before Federal Income Taxes	**$ 397,579**	$ 337,989	$ 247,181	$ 187,577	$ 180,584
Assets at December 31					
Transportation	**$2,859,160**	$2,796,562	$2,587,498	$2,459,493	$2,267,539
Oil and Gas	**1,142,687**	1,055,093	827,806	710,555	491,575
Mining	**119,175**	98,982	80,230	59,472	41,822
Land	**92,326**	102,661	115,476	120,147	126,712
Corporate[d]	**223,763**	63,127	82,736	68,581	100,805
Total	**$4,437,111**	$4,116,425	$3,693,746	$3,418,248	$3,028,453
Depreciation, Depletion, Amortization and Retirements					
Transportation	**$ 91,572**	$ 86,397	$ 80,288	$ 75,310	$ 71,744
Oil and Gas	**72,599**	58,925	47,894	121,941[c]	90,397[c]
Mining	**1,403**	1,122	312	795	557
Land	**724**	682	719	852	1,014
Corporate	**503**	503	503	357	140
Total	**$ 166,801**	$ 147,629	$ 129,716	$ 199,255	$ 163,852
Capital Expenditures					
Transportation	**$ 241,749**	$ 204,189	$ 177,943	$ 205,780	$ 195,760
Oil and Gas	**176,543**	147,243	187,135	205,917	189,566
Mining	**5,140**	12,339	12,958	20,335	8,596
Land	**766**	450	273	2,620	6,311
Corporate	**—**	—	—	5,098	3,780
Total	**$ 424,198**	$ 364,221	$ 378,309	$ 439,750	$ 404,013

(a) The Corporation operates principally in the United States. Intersegment sales are immaterial.
(b) Includes a $59.9 million gain from sale of interests in British North Sea.
(c) After provision for losses of $60.8 million in 1975 and $60.0 million in 1974 to fully reserve Champlin's interest in certain unproductive leaseholds.
(d) Corporate assets are principally cash, temporary cash investments and marketable securities.
(e) After $6.7 million writeoff of a portion of the Stansbury coal mine venture as a result of depleted and otherwise uneconomic coal seams.

The accompanying accounting policy disclosures and notes to financial statements are an integral part of this information.

Union Pacific Corporation and
Subsidiary Companies

Principles of Consolidation
The consolidated financial statements include the accounts of Union Pacific Corporation (Corporation) and all subsidiaries. Investments in affiliated companies (companies in which the Corporation owns between 20% and 50% of the voting stock) are accounted for on the equity method. All material intercompany transactions are eliminated. Certain 1977 amounts have been reclassified to conform with the 1978 presentation.

Inventories
Materials and supplies are valued at average cost. Refined products and raw materials—crude oil are valued at cost under the last-in, first-out method (LIFO). Real estate developed and held for sale is carried at the cost of land and improvements thereto; however, administrative costs, property taxes and other carrying charges are expensed currently. All inventories are valued at the lower of cost or market.

Oil and Gas Accounting Policies
In 1978 Champlin Petroleum Company (Champlin) modified its successful efforts method of accounting for oil and gas exploration costs to conform with FASB Statement No. 19. These changes had an insignificant effect on the results of Champlin's operations.

Costs of developing producing properties, including drilling costs and applicable leasehold acquisition costs, are capitalized. Drilling costs of unsuccessful exploratory wells, geological and geophysical costs and carrying costs are charged to expense when incurred.

Depletion and amortization of producing properties, including depreciation of well and support equipment, are recorded by a unit-of-production method based upon proved reserves. Acquisition costs of unproved properties are amortized from date of acquisition on a composite basis which considers past success experience and average lease life.

Mining Accounting Policies
Leasehold and development costs are capitalized and subsequently amortized on a unit-of-production method when production commences. Carrying costs of mineral rights are expensed currently.

Depreciation
Provisions for depreciation are computed principally on the straight-line method based on estimated service lives of depreciable properties, except for rails, ties and other track material owned by Union Pacific Railroad Company (Railroad) for which the generally accepted industry alternative of replacement accounting is utilized. Under this method, replacements in kind are charged to expense and betterments (improvements) are capitalized.

Retirements
When property is sold or retired, the cost and accumulated depreciation and depletion are written off and related gains and losses are reflected in income, except for railroad equipment or depreciable road property, where the cost less salvage value is charged to accumulated depreciation.

Excess of Investment in Consolidated Subsidiaries over Equities in Recorded Net Assets
This cost relates primarily to the acquisition of Champlin and is not being amortized because, in the opinion of management, there has been no diminution in the underlying value of the investment.

Investment Tax Credit
Benefits from the investment tax credit are recorded currently in income.

Earnings Per Common Share
Earnings per common share is based on the weighted average number of shares outstanding during the periods after giving effect to preferred stock dividend requirements. Shares issuable upon the exercise of outstanding common stock options and upon conversion of outstanding convertible securities are excluded in the computation because their effect is not material.

Union Pacific Corporation and
Subsidiary Companies

1. Business
Union Pacific Corporation consists of four operating companies engaged in: railroad transportation of manufactured goods, minerals, and farm products; oil and gas exploration, development, production, refining and marketing; mining of coal, uranium and trona; and land sales and leases of industrial and commercial sites. Financial information for these business segments for the years ended December 31, 1978 and 1977 is an integral part of these financial statements and is presented on page 38.

2. Inventories
Inventories consisted of the following at December 31:

Thousands of Dollars	**1978**	1977
Materials and supplies	**$ 88,167**	$ 75,289
Raw materials—crude oil	**50,067**	67,840
Refined products	**43,204**	29,720
Real estate developed and held for sale	**14,053**	19,451
	$195,491	$192,300

The excess of current replacement cost over the carrying value of inventories for which cost has been determined under the LIFO method at December 31, 1978 and 1977 approximated $42,300,000 and $31,800,000, respectively.

The Corporation's 1978 Annual Report on Form 10-K contains unaudited information on the effects of the estimated replacement costs of inventories not carried under the LIFO method.

3. Investments
Temporary cash investments are carried at cost which approximates market.

Investments in affiliates are carried at equity. Equity in net income of affiliates was $8,449,000 in 1978 and $9,477,000 in 1977.

Other investments at December 31, 1978 and 1977 include $46,791,000 of marketable equity securities carried at written-down cost. At December 31, 1978 and 1977 quoted market value exceeded the carrying value of such securities by approximately $30,268,000 and $27,156,000, respectively.

Marketable equity securities include an investment in 2,149,319 shares of IC Industries, Inc. common stock with a carrying value of $35,195,000 at December 31, 1978. The Corporation has agreed to dispose of the entire investment by 1982. The Corporation's plan of divestiture provides that one-third of the stock is to be sold by the end of 1980 and the remaining stock to be sold by August 10, 1982.

4. Properties
Major property accounts as of December 31 are as follows:

	Properties	Accumulated depreciation, depletion and amortization
1978	Thousands of Dollars	
Transportation		
Road	**$1,258,950**	**$ 125,062**
Equipment	**1,912,570**	**560,880**
Other	**14,403**	**6,044**
	3,185,923	**691,986**
Oil and gas		
Exploration and production	**665,788**	**298,058**
Refining and other	**520,089**	**143,538**
	1,185,877	**441,596**
Other	**70,306**	**16,085**
	$4,442,106	**$1,149,667**
1977	Thousands of Dollars	
Transportation		
Road	$1,207,145	$ 119,697
Equipment	1,801,151	545,711
Other	12,850	7,102
	3,021,146	672,510
Oil and gas		
Exploration and production	589,672	322,346
Refining and other	493,067	121,040
	1,082,739	443,386
Other	64,866	13,387
	$4,168,751	$1,129,283

In lieu of depreciation, the Railroad charges repairs and replacement of track structure to income ($107,673,000 in 1978 and $91,766,000 in 1977). Other maintenance expenditures at the Railroad were $289,236,000 in 1978 and $241,851,000 in 1977.

Costs incurred in oil and gas producing activities, including costs capitalized, are as follows:

Thousands of Dollars	**1978**	1977
Property acquisition costs	**$39,484**	$18,141
Exploration costs	**34,787**	37,078
Development costs	**98,796**	79,244
Production costs	**89,577**	79,830

The inflationary trend of the general economy in recent years has resulted in increasingly higher costs for replacement of "productive capacity." The accompanying financial statements are based on historical costs; hence, the impact of inflation has not been fully reflected therein. Supplementary unaudited information concerning estimated replacement costs of properties may be found in the Corporation's 1978 Form 10-K.

5. Federal Income Taxes

Components of Federal income tax expense are as follows:

Thousands of Dollars	1978	1977
Current	$ 46,234	$ 27,809
Deferred	87,235	88,271
	$133,469[a]	$116,080[a]

(a) Excludes effect of 1% benefit of the Corporation's Employee Stock Ownership Plan. Related dollar amounts are not material.

The tax effect of differences in the timing of revenues and expenses for tax and financial statement purposes is as follows:

Thousands of Dollars	1978	1977
Excess of tax over book depreciation	$47,049	$38,831
Intangible drilling costs	20,363	22,233
Surrender of offshore Florida leases	29,514	—
Incentive per diem[a]	(13,005)	2,120
Investment tax credit[b]	—	20,084
Other	3,314	5,003
	$87,235	$88,271

(a) Results from revenues previously deferred for tax purposes.

(b) Represents amount used in 1977 tax return but recognized for financial statement purposes as a reduction of the deferred income tax provision in 1976.

A reconciliation between the statutory and effective tax rates follows:

	1978	1977
Statutory tax rate	48.0%	48.0%
Investment tax credit	(11.6)	(11.1)
Depletion of natural resources	(1.3)	(1.1)
Other	(1.5)	(1.5)
Effective tax rate	33.6%	34.3%

Federal income tax returns have been examined by the Internal Revenue Service through 1972 for all companies. In 1978, a settlement of the years 1943 through 1945 was approved by the Congressional Joint Committee on Taxation and a refund was received. However, the Corporation is asserting that additional refunds are due and this may require litigation. Joint Committee approval of a settlement for the years 1946 through 1961 is expected shortly. Settlements which have been negotiated with the Appellate Division of the IRS for the years 1962 through 1967 are subject to review by the Joint Committee. The settlements reserve, or will reserve, to the Corporation the right to file refund claims on certain issues and litigation is anticipated to pursue such claims. For the years 1968 through 1972, negotiations with Appellate are taking place.

It is the opinion of management, after consultation with independent tax counsel with respect to the years 1943 through 1973, that the Corporation is adequately accrued for Federal income taxes through December 31, 1978.

6. Debt

Long-term debt as of December 31 is summarized below:

Thousands of Dollars	1978	1977
Equipment Obligations, 5⅜% to 9⅞%, due through 1993	$516,087	$515,836
Debentures, 8.4%, due 1987 to 2001	150,000	150,000
Notes, 8.6%, due 1983	100,000	100,000
Refunding Mortgage Bonds, Series C, 2½%, due 1991	43,279	43,279
Commercial Paper	—	20,000
Pollution Control Revenue Bonds, Series A, 7⅜%, due 2005	18,900	18,900
Convertible Debentures, 4¾%, due 1999	14,853	16,920
	$843,119	$864,935

Certain railway equipment secures the outstanding equipment obligations. Approximately 3,300 miles of Railroad main and branch line track, certain other railway equipment, supplies and other facilities are subject to the lien of the mortgage securing the refunding mortgage bonds.

The 4¾% debentures are redeemable at the option of the Corporation at 101.59% of the principal amount until April 1, 1979 and at reduced percentages thereafter. The 4¾% debentures are convertible into common stock through April 1, 1999 at $28.57 per share (subject to adjustment under certain conditions). During 1978 and 1977, $2,067,000 and $8,257,000, respectively, of debentures were converted into shares of common stock.

Maturities of long-term debt for each of the five years 1979 through 1983 are $47,278,000, $55,235,000, $54,672,000, $50,294,000 and $148,035,000, respectively.

The Corporation has a $100,000,000 long-term credit agreement with thirty-one banks available through September 30, 1982. Loans under this agreement will bear interest at Citibank, N.A.'s base rate for 90-day loans and there is provision for an annual commitment fee of ½% on the unused portion. In addition to the credit agreement, there are individual short-term lines of credit totaling $100,000,000 with eight banks. The credit agreement and lines of credit were not used during 1978 or 1977.

An informal agreement to maintain compensating balances in amounts deemed appropriate by the Corporation exists under these credit arrangements. Any compensating balances are unrestricted as to use at any time. During 1978 and 1977, average compensating balances were $15,500,000 and $15,685,000, respectively.

In 1978 and 1977, the Corporation had short-term borrowings in the form of commercial paper. The following table summarizes commercial paper activity for the years ended December 31:

Thousands of Dollars	1978	1977
Maximum month-end outstanding	$51,100	$96,559
Average daily balance	14,827	41,167
Average interest rate	6.8%	5.3%
Average interest rate on year-end balance	—	6.7%

At December 31, 1978, all commercial paper has been paid. In addition, during 1978 the Corporation utilized an informal short-term credit facility. The maximum amount available under this facility is $50,000,000. The average daily balance outstanding and interest costs during the year were nominal.

The bank credit agreement and certain indentures contain restrictions relating to the payment of cash dividends. The amount of retained earnings available for cash dividends, under the most restrictive of the covenants, was $421,518,000 at December 31, 1978.

7. Pension Plans
The Corporation and its subsidiaries have funded pension plans covering substantially all salaried employees.

At December 31, 1977, the date of the latest actuarial valuation, unfunded actuarial liabilities amounted to $94,092,000 and the value of vested benefits exceeded pension plan assets valued at market by $10,844,000. Charges to operations for the plans amounted to $19,222,000 in 1978 and $18,112,000 in 1977. Such charges included prior service costs which are being amortized over thirty years.

The Corporation and its subsidiaries also have unfunded pension plans for officers and supervisors and for retirees under a predecessor plan. At December 31, 1977 the actuarial liability and vested benefits amounted to $42,200,000 and $34,900,000, respectively. Charges to operations for the unfunded plans are based upon actual payments to retirees and amounted to $4,157,000 in 1978 and $4,163,000 in 1977, which approximate normal costs plus amortization of prior service costs.

8. Capital Stock and Stock Option Plans
The outstanding preferred stock provides for cumulative cash dividends at an annual rate of $0.475 per share; redemption at the option of the Corporation at $10.60 per share through May 31, 1979 and at reduced amounts thereafter; and convertibility into common shares at the rate of 0.35 of a share of common stock for each preferred share. Total dividends declared on preferred stock were $125,000 in 1978 and $150,000 in 1977.

The Corporation has two stock option plans (a 1976 Plan and a 1969 Plan). At December 31, 1978 and 1977, there were 893,400 and 1,060,300 shares, respectively, available for grant to officers and key employees. Outstanding options under the 1969 Plan may be qualified or non-qualified and are exercisable for a period of five and ten years, respectively, at 100% of market value at the date of grant. Options under the 1976 Plan are non-qualified and are exercisable for a period of ten years at 100% of market value at the date of grant. All options become exercisable one year after date of grant. Changes in common stock options outstanding during 1978 and 1977 are summarized as follows:

1978	Shares Under Option	Price Range Per Share
Balance		
Jan. 1	**711,500**	**$21.07 to $53.82**
Granted	**171,600**	**43.94 to 54.44**
Exercised	**(26,479)**	**30.07 to 44.57**
Expired	**(6,121)**	**44.57 to 51.25**
Balance Dec. 31	**850,500**	**$21.07 to $54.44**
Exercisable Dec. 31	**678,900**	**$21.07 to $53.82**

1977	Shares Under Option	Price Range Per Share
Balance		
Jan. 1	724,900	$21.07 to $46.07
Granted	154,300	45.94 to 53.82
Exercised	(110,200)	27.07 to 44.57
Expired	(57,500)	44.57
Balance Dec. 31	711,500	$21.07 to $53.82
Exercisable Dec. 31	557,200	$21.07 to $46.07

The 1976 Stock Option Plan also provides for granting stock appreciation rights to holders of options, which permit them to surrender the related exercisable options, or any portion thereof, in exchange for cash or stock in an amount equal to the excess of the market price of the common stock on the date the right is exercised over the option price. During 1978 and 1977, options for 73,500 and 65,200 shares with stock appreciation rights were granted under the 1976 Plan at option prices ranging in 1978 from $47.82 to $54.44. In 1978, $458,000 was charged to income and, in 1977, $306,000 was credited to income with respect to such rights. Charges (or credits) to income relating to such rights result from changes in the market value of the stock. Credits to income are limited to amounts previously provided for market value increases. At December 31, 1978 and 1977, there were 243,300 and 171,300 shares subject to outstanding stock appreciation rights, respectively.

Of the unissued common stock, 2,346,339 shares (2,463,152 in 1977) are reserved for issuance upon conversion of the convertible debentures and convertible preferred stock, and exercise of stock options.

9. Contingent Liabilities, Commitments and Litigation
At December 31, 1978 the Corporation was contingently liable for $94,000,000 which includes, except for the ethylene plant discussed below, indebtedness of affiliated companies, principal, interest and rental payments of various companies and additional premiums relating to a service interruption policy carried jointly with other railroads.

Champlin holds a 37½% interest in a $630,000,000 joint venture for the construction and operation of an ethylene plant at Corpus Christi, Texas. At December 31, 1978, the venture had incurred indebtedness of approximately $264,000,000, of which the Corporation and Champlin have guaranteed approximately $99,000,000. It is expected that the venture will incur approximately $178,000,000 of additional debt, of which the Corporation and Champlin will guarantee approximately $67,000,000.

Champlin's operations in the United States are subject to Department of Energy (DOE) regulations which include price and allocation controls. The DOE and certain private parties have challenged Champlin's interpretation of certain provisions of these regulations. Management believes Champlin has complied with the regulations and that the final amount of price adjustments or rollbacks as finally determined, if any, will not have a material adverse effect on the consolidated financial position of the Corporation.

Certain subsidiaries of the Corporation, including Champlin, are parties to three lawsuits in Utah and two in Wyoming in which such subsidiaries' ownership of oil and gas and other mineral rights have been challenged in about 48,000 acres of land in Utah and 5,700 acres in Wyoming. Independent counsel has advised the Corporation that the mineral reservations involved in the lawsuits are valid and legally effective and include all right, title and interest to all minerals, including oil and gas, and they should be so construed by the courts. In November, 1978 the United States Federal District Court for Wyoming held in one of the cases pending in that State that such subsidiaries have complete title to all the minerals underlying the tract in question, including, but not limited to, ownership of any oil and gas. The mineral reservations involved in these lawsuits are similar or identical to mineral reservations covering many thousands of sections of land grant lands sold by the Union Pacific Railroad and its predecessor companies in Wyoming, Utah and Colorado chiefly in the late 19th and early 20th centuries. If any of these challenges should be successful, it is possible, depending upon the effect of such court decision as a precedent in other cases, that such subsidiaries' mineral interests in such other lands could be affected.

The Railroad is defendant to an action brought by the City of Los Angeles in which the City claims ownership of, and seeks an accounting with respect to, 206 acres of alleged tidelands and submerged lands located in the Wilmington oil field, a long-term oil producing property. In the opinion of independent counsel, the Railroad has substantial defenses which, in their view, should be sustained by the court.

There are several other lawsuits pending against the Corporation and certain of its subsidiaries not described herein. It is the opinion of management, after consulting with legal counsel, that such litigation will not have a material adverse effect on the consolidated financial position of the Corporation.

10. Quarterly Results of Operations (Unaudited)
The unaudited quarterly results of operations (in thousands of dollars, except per share amounts) for the two years ended December 31 are as follows:

1978	Mar 31	Jun 30	Sep 30	Dec 31
Revenues	**$686,148**	**$738,823**	**$730,259**	**$834,198**
Income before Federal income taxes	**82,681**	**93,063**	**98,859**	**122,976**
Net income	**56,100**	**63,489**	**64,944**	**79,577**
Per common share	**$1.18**	**$1.34**	**$1.36**	**$1.67**
1977				
Revenues	$602,665	$617,679	$641,278	$692,673
Income before Federal income taxes	67,345	79,405	83,896	107,343
Net income	47,572	54,682	55,876	63,779
Per common share	$1.01	$1.15	$1.18	$1.34

Responsibilities for Financial Statements

The accompanying financial statements, which consolidate the accounts of Union Pacific Corporation and its subsidiaries, have been prepared in conformity with generally accepted accounting principles appropriate in the circumstances.

The integrity and objectivity of data in these financial statements and accompanying notes, including estimates and judgments related to matters not concluded by year-end, are the responsibility of management as is all other information in this Annual Report unless otherwise indicated. Management devotes ongoing attention to review and appraisal of its system of internal controls to provide reasonable assurance at reasonable cost that the Corporation's assets are protected and that transactions and events are recorded properly. This system is augmented by a staff of corporate traveling auditors supplemented by internal auditors in the subsidiary operating companies; careful attention to selection and development of qualified financial personnel; programs to ensure timely communication and monitoring of policies, standards and delegated authorities; and evaluation by independent public accountants during their examination of the annual financial statements.

These financial statements have been examined by Deloitte Haskins & Sells, independent public accountants. Their report, which appears on this page, expresses their opinion on whether management's financial statements, considered in their entirety, present fairly the Corporation's financial condition and operating results in conformity with generally accepted accounting principles. Their examination is conducted in accordance with generally accepted auditing standards and includes a review of internal controls and sufficient tests to provide them with reasonable assurance that the financial statements are neither materially misleading nor contain material errors.

The Audit Committee of the Board of Directors, composed entirely of outside directors as identified on page 28, meets regularly with financial management, internal auditors and the independent public accountants to review the work of each and to ensure that each is properly discharging its responsibilities. The independent public accountants have free access to the Audit Committee, without management representatives present, to discuss the results of their examination and their opinions on the adequacy of internal controls and the quality of financial reporting.

James H. Evans
Chairman of the Board and
Chief Executive Officer

W. F. Surette
Senior Vice President
Finance

Auditors' Opinion

Union Pacific Corporation, its Directors and Stockholders:
We have examined the statements of consolidated financial position of Union Pacific Corporation and subsidiary companies as of December 31, 1978 and 1977 and the related statements of consolidated income, consolidated changes in stockholders' equity, and consolidated changes in financial position for the years then ended. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, such consolidated financial statements present fairly the financial position of Union Pacific Corporation and subsidiary companies at December 31, 1978 and 1977 and the results of their operations and the changes in their financial position for the years then ended, in conformity with generally accepted accounting principles applied on a consistent basis.

Deloitte Haskins & Sells

January 25, 1979

New York, NY

Ten-Year Financial Summary

Union Pacific Corporation and Subsidiary Companies	**1978**	1977	1976	1975	1974
Revenues	**$2,989.4**	$2,554.3	$2,065.0	$1,850.1[(b)]	$1,623.4
Costs and Expenses	**2,591.8**	2,216.3	1,817.8	1,662.5	1,442.8
Federal Income Taxes	**133.5**	116.1	59.5	39.0	55.4
Income Before Extraordinary Item	**264.1**	221.9	187.7[(c)]	148.6	125.2
Net Income	**$ 264.1**	$ 221.9	$ 195.2[(c)]	$ 148.6	$ 125.2
Earnings Per Common Share					
Before Extraordinary Item	**$5.55**	$4.68	$4.02[(c)]	$3.21	$2.73
Net Income	**5.55**	4.68	4.18[(c)]	3.21	2.73
Dividends Per Common Share	**$2.075**	$1.775	$1.475	$1.40	$1.30
At December 31					
Working Capital	**$ 184.5**	$ 130.6	$ 87.1	$ 118.2	$ 63.9
Total Assets	**4,437.1**	4,116.4	3,693.7	3,418.2	3,028.5
Debt Due After One Year	**843.1**	864.9	784.2	725.1	551.6
Stockholders' Equity	**2,286.0**	2,117.5	1,967.5	1,825.1	1,729.6
Per Common Share	**$ 47.98**	$ 44.54	$ 41.74	$ 39.19	$ 37.50
For the Year					
Capital Investments[(d)]	**$552.6**	$418.1	$393.3	$439.8	$404.0
Operating Cash Flow	**526.6**	449.5	369.1[(c)]	299.6	300.5
Total Salaries, Wages and Employee Benefits	**$816.9**	$698.1	$641.0	$559.5	$539.1
Average Number of Employees	**30,637**	28,787	28,386	28,191	30,169
Financial Ratios (percentages)					
Borrowings to Total Capital Employed	**24.7**	27.0	27.0	25.6	21.9
Return on Average Stockholders' Equity	**12.0**	10.9	9.9	8.4	7.4

(a) Excludes the operating results of Champlin Petroleum Company which was purchased as of January 1, 1970.
(b) Includes a $59.9 million gain from sale of interests in British North Sea.
(c) Net income in 1971 reflects an extraordinary charge of $65.0 million ($1.45 per share) applicable to reserves for participation in Amtrak. Net income in 1976 reflects an extraordinary credit of $7.5 million ($.16 per share) due to a reduction in the Amtrak reserve. Operating cash flow excludes the extraordinary item.
(d) Includes advances to and capital expenditures of unconsolidated affiliated companies.

Dollar Amounts in Millions
Except Per Share Amounts

1973	1972	1971	1970	1969[a]
$1,243.4	$1,114.8	$1,000.5	$ 953.7	$ 709.8
1,046.3	954.6	861.2	837.7	586.3
70.0	55.7	49.2	34.6	39.1
127.1	104.5	90.1[c]	81.4	84.4
$ 127.1	$ 104.5	$ 25.1[c]	$ 81.4	$ 84.4
$2.81	$2.31	$2.00[c]	$1.82	$1.88
2.81	2.31	.55[c]	1.82	1.88
$1.12	$1.00	$1.00	$1.00	$1.00
$ 128.4	$ 62.3	$ 90.1	$ 100.4	$ 80.7
2,828.4	2,808.6	2,779.7	2,796.8	2.335.3
475.1	513.1	544.5	572.3	299.0
1,649.7	1,565.6	1,503.0	1,514.5	1,477.9
$ 36.18	$ 34.56	$ 33.29	$ 33.76	$ 32.94
$187.5	$150.0	$178.7	$224.6	$178.3
283.1	248.0	221.4[c]	218.4	173.0
$486.5	$431.3	$389.4	$370.0	$329.4
29,350	29,732	30,902	32,097	31,416
20.5	26.2	29.7	31.0	21.1
7.9	6.8	6.0	5.4	5.8

Executive Offices
345 Park Avenue
New York, New York 10022
212-826-8200

Operating Companies
Union Pacific Railroad Company
1416 Dodge Street
Omaha, Nebraska 68179

Champlin Petroleum Company
5301 Camp Bowie Boulevard
Fort Worth, Texas 76107

Rocky Mountain Energy Company
4704 Harlan Street
Denver, Colorado 80212

Upland Industries Corporation
Suite 1000, 110 N. Fourteenth Street
Omaha, Nebraska 68102
and
5480 Ferguson Drive
Los Angeles, California 90022

Transfer Agent and Registrar of Stock
Effective March 1, 1979, Union Pacific Corporation appointed Morgan Guaranty Trust Company of New York as stock transfer agent, registrar, and dividend disbursing agent for its common and preferred stocks. Correspondence concerning your account, dividend payments or address changes should be addressed to:
Morgan Guaranty Trust Company of New York
30 West Broadway
New York, New York 10015

Stock Listing
New York Stock Exchange
Ticker Symbol UNP

Annual Meeting of Stockholders
May 8, 1979, 12:00 Noon
Hotel Utah
Salt Lake City, Utah
The proxy statement and proxy form will be mailed in early April.

SEC Form 10-K
A copy of the Corporation's 1978 Annual Report on Form 10-K, to be filed with the Securities and Exchange Commission in late March, may be obtained after April 2, 1979, by writing to:
Secretary
Union Pacific Corporation
345 Park Avenue
New York, New York 10022

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