# YEAR IN REVIEW

Leveraging the Railroad's diverse franchise and executing the Yield Strategy enabled Union Pacific to profitably grow the top line in 2003. Despite a challenging economy during the first half of the year, operating revenue grew 4% to $11.6 billion, the highest level in the Company's history. All six business teams experienced revenue growth during the year, with five of the six teams recording best-ever yearly revenue performance. Volume was up 1% as carloads surpassed 9.2 million units and gross ton-miles (GTMs) exceeded 1 trillion for the first time ever. In addition, average revenue per car was up over 2% driven by price gains from value-added service offerings, favorable business mix and fuel surcharges.

Although records were set in 2003, the year could have been even better as a shortage of train crews impacted the Railroad's network performance during the last half of the year. In addition, the nation's economy gained momentum during the fourth quarter driving carloadings up 4%, further straining already tight resources.

The Railroad was also challenged by continued high energy prices during the year as the average fuel price increased to $0.92 per gallon, a 26% increase versus 2002. The rise in fuel costs added $255 million in operating expense and also negatively impacted many of UP's customers, especially in the Chemicals industry. However, efforts to improve and expand the Company's fuel surcharge program resulted in approximately 44% of these incremental costs being offset.

In November of 2003, Union Pacific again became a "pure" railroad with the sale of its trucking segment, Overnite, through an IPO. A $211 million gain on the transaction, including an income tax benefit of $126 million, was reported in the fourth quarter of 2003. The sale also generated $620 million in cash that was used primarily to retire $500 million of the $1.5 billion Convertible Preferred Securities Term Income Deferrable Equity Securities (TIDES).

Cash from operations in 2003 increased 10% to $2.4 billion, while the Railroad's investment in infrastructure

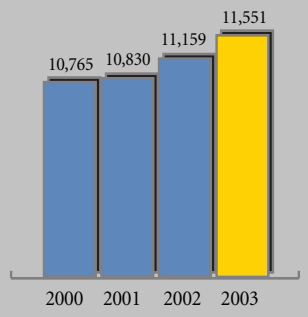
## FINANCIAL HIGHLIGHTS *(millions of dollars, unless otherwise indicated)*

| | 2003 | 2002 | 2001 |
|---|---|---|---|
| Operating Revenues | **$11,551** | $11,159 | $10,830 |
| Operating Income | **2,133** | 2,253 | 2,018 |
| Income from Continuing Operations | **1,056** | 1,265 | 934 |
| Income from Discontinued Operations *(a)* | **255** | 76 | 32 |
| Cumulative Effect of Accounting Change, Net of Taxes | **274** | - | - |
| Net Income | **1,585** | 1,341 | 966 |
| Dividends per Share | **0.99** | 0.83 | 0.80 |
| Capital Expenditures *(b)* | **1,940** | 1,820 | 1,696 |
| Operating Cash Flow | **2,422** | 2,199 | 1,865 |
| Net Free Cash Flow *(c)* | **524** | 536 | 241 |
| **Financial Statistics and Ratios** | | | |
| Revenue Carloads *(thousands)* | **9,239** | 9,131 | 8,916 |
| Average Employees | **46,371** | 47,298 | 48,632 |
| Fuel Consumed *(millions of gallons)* | **1,330** | 1,315 | 1,287 |
| Average Price per Gallon | **$0.92** | $0.73 | $0.88 |
| Operating Margin *(%)* | **18.5** | 20.2 | 18.6 |
| Lease Adjusted Debt to Capital *(%) (d)* | **44.8** | 51.7 | 55.0 |

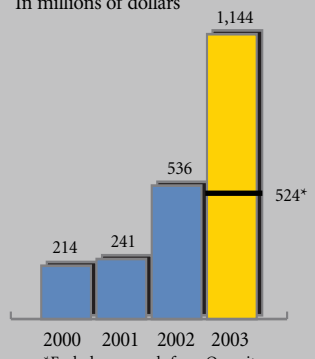
(a) The Corporation's trucking segment, Overnite, is presented as discontinued operations. 2003 results include a $211 million gain on sale, including an income tax benefit of $126 million.
(b) Capital expenditures include non-cash financings of $188 million, $126 million and $124 million in 2003, 2002 and 2001, respectively.
(c) Free cash flow is computed as follows: cash from operations less cash from investing less dividends paid less non-cash lease financings plus non-cash acquisitions. 2003 results exclude proceeds from Overnite IPO of $620 million.
(d) Lease adjusted debt to capital is computed as follows: total debt plus convertible preferred securities plus net present value of leases divided by total debt plus equity plus convertible preferred securities plus net present value of leases.

# YEAR IN REVIEW

## OPERATING REVENUES
In millions of dollars

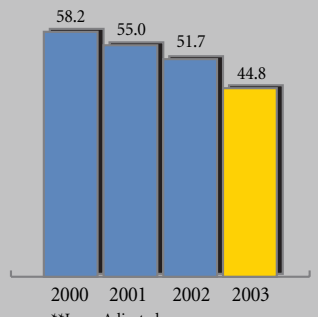



## FREE CASH FLOW
In millions of dollars




*Excludes proceeds from Overnite IPO of $620 million.

## DEBT TO CAPITAL**
Percentage




**Lease Adjusted

and equipment resulted in a capital expenditure program of $1.9 billion. Union Pacific's commitment to return value to its shareholders continued as the fourth quarter dividend was increased by 30% to $0.30 per share, following a 15% increase in 2002. In addition, UP generated $524 million in free cash flow after dividends (excluding proceeds from the Overnite sale). The Company also redeemed another $500 million of TIDES, with the remaining $500 million being refinanced with new unsecured debt at a favorable interest rate. The generation of significant cash flow, from both operations and the IPO, improved Union Pacific's financial flexibility, driving the lease adjusted debt to capital ratio to 44.8%, the lowest level since before the acquisition of Overnite. Moody's recognized this commitment to balance sheet strength during 2003 with a ratings upgrade to Baa2.

In January 2004, Ike Evans was elected Vice Chairman and Jim Young succeeded Ike as the President and Chief Operating Officer of the Railroad. Both Ike and Jim will join Dick Davidson, Chairman and Chief Executive Officer, in a newly created "Office of the Chairman". Rob Knight succeeded Jim as Executive Vice President and Chief Financial Officer. This new organizational structure, focused on improving quality processes and attaining operational excellence, continues the Company's commitment to be a railroad where customers want to do business, employees are proud to work and shareholder value is created.

### Looking Forward

The surge in demand that was experienced during the fourth quarter of last year has continued, with first quarter 2004 carloads up over 4%. The strong demand and tight train crew supply have increased the need for other critical resources such as locomotives and terminal capacity. These capacity constraints have decreased the company's operating efficiency which has negatively affected operating income. Efforts to impact velocity and service levels include training 3,700 trainmen for the 2004 peak season, bringing on additional locomotives including 270 new units and 350 peak-power units, as well as metering business volumes in key areas across the Railroad.

**Union Pacific is committed to be a company where:**

Customers want to do business,

Employees are proud to work and

Shareholder value is created.