RAILROAD WEEK IN REVIEW

February 18, 2022

"We think UNP could be best positioned from a volume standpoint relative to our expectations. In part this reflects recent coal and intermodal contract wins. Based on these contract wins, we now expect the best volume growth from UNP among the U.S. rails over the next two years." — Scott Group, Wolfe Research, February 13

"International Paper reported mixed fourth quarter results with strong revenue growth but lackluster earnings. The industrial packaging segment reported a decrease in both fourth-quarter and four-year volume but an increase in revenue for board. Volume was constrained in the quarter by operational supply charges." — Morningstar analyst note January 28

"The Proposed Rule is a regulatory mandate that railroads do things they would not do in a free market. Switching required by STB order is a form of forced sharing, where a railroad is compelled to operate its facilities and equipment for the advantage of someone else." — AAR to STB on reciprocal switching

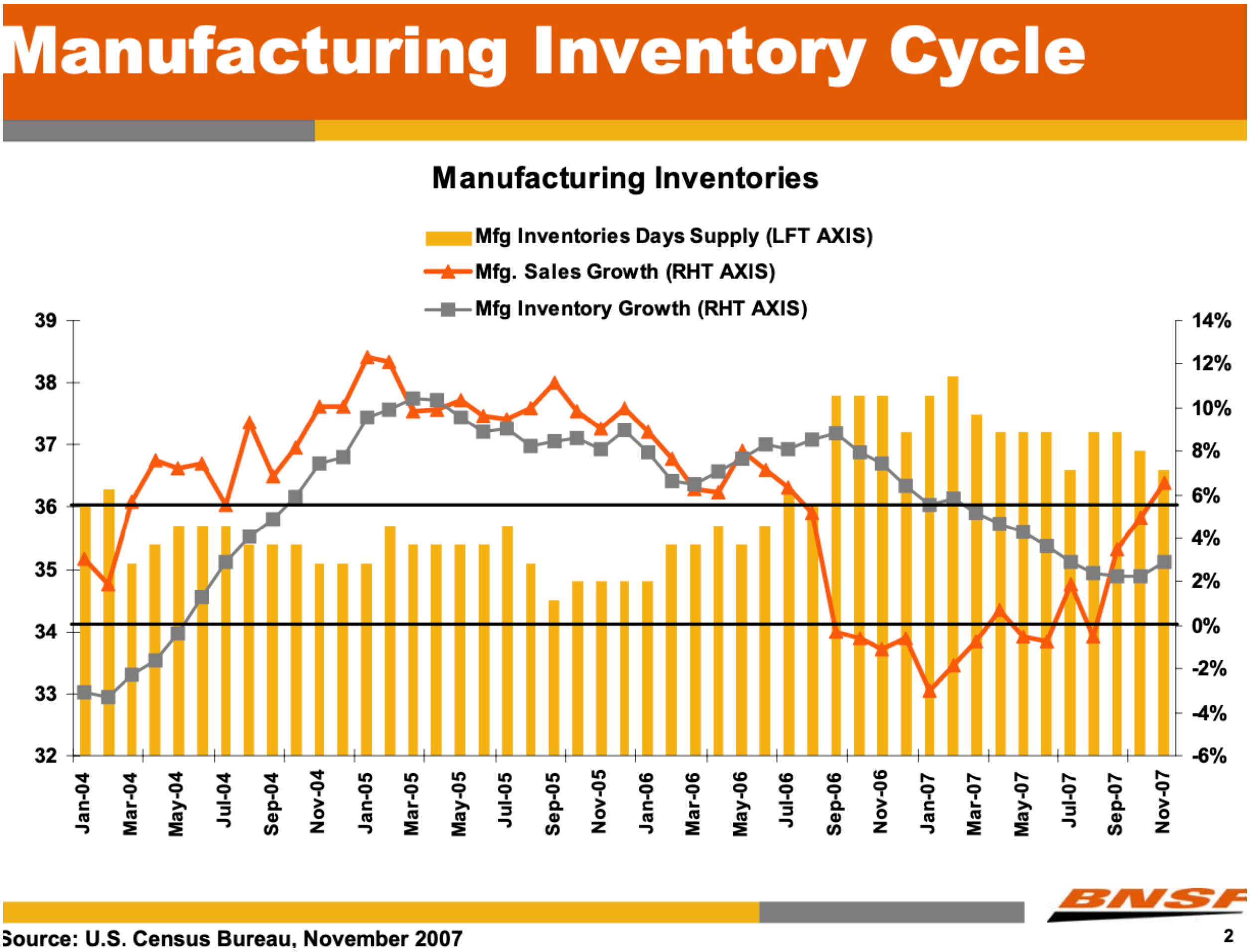
A question has arisen about the use of research to help railroads gain market share from the trucks. Jason Miller, PhD, Associate Professor of Logistics, Department of Supply Chain Management, Eli Broad College of Business at Michigan State weighs in:

> I continue to believe the most powerful documents available for those in the rail industry to understand market share possibilities are the Commodity Flow Surveys from Census Bureau. The data coverage is better than any single industry source has access to given the stratified random sample used by the Census Bureau and Bureau of Transportation Statistics. Folks can slice and dice the data up to find those long-haul trucking lanes that provide the highest likelihood of conversion back to rail.

Miller says a great example of rail-truck price spreads can be seen by comparing the 2019 price changes for rail freight intermodal versus general freight, long-distance, truckload. One can see how trucking prices started to decline in 2019 yet the railroads didn't lower intermodal prices. "And they wonder why they lost a lot of intermodal traffic in 2019 to truck? Sad thing is the spread between TL and intermodal rates have never been higher, but intermodal loadings are still well below 2018 levels."

The question being asked in my small circle of railroad observers is simply this: How can rail grow market share without such competitive market intelligence? To me, it appears that the freight railroads have stopped tracking economic trends and that they have never really tracked truck pricing, especially by commodity and lane. That's where market share gains start.

Time was when, for example, BNSF had an in-house economist, Sam Kyei by name, who tracked national economic trends and how BNSF could use them to increase revenue units. Here's a slide from Kyei's 2008 MWARS presentation. You can see how he sets the economic scene and relates to potential BNSF carload volumes.



I remain of the opinion that today's RR market managers are setting prices according to what they see on their screen after entering the particulars of the move— there's nothing to do with what price the market will bear. Nor is there any consideration of the commodity trends or how the shipper's business is performing.

For example, if you're working the STCC 26 paper desk you can look at an industry report like the Morningstar note excerpted in the quotes section above. You can drill down into older reports and find the parallels with Kyei's manufacturing trends chart to see how paper inventory supply days track sales and industry growth and then you can ask your paper customers what *they're* seeing.

As for truck trends, I think the customer is better served if one compares truck vs rail pricing using the *total cos*t of the move to the customer. A useful spreadsheet starts with the rate offered and then one enters inventory value, shipment size, transit days, any safety stock provisions, distance, adjustments for congestion etc., and estimated truck rate per mile.

Then you can tell a customer what the all-in costs of truck vs. rail really are. I'm afraid today the quoted rate and ease of doing business captures all, but if you compare *total* delivered costs rail may start to gain an edge. *That's* the kind of market intelligence we need to fill the cars and trains.

The Railway Industry Agreement I mentioned last week in the context of reciprocal switching is a document whose longevity I've long doubted. Like so many of these kinds of initiatives, they look great for a few months but then are consigned to the dustbin of history as the next new initiative comes along.

Turns out I'm not alone in my doubts. A dear friend upon whom I depended at the time to sanity check the document as to actual feasibility and use writes,

> I noted in last week's you referenced the Rail Industry Agreement, and I feel you're spot-on in your assessment. But based on my current industry dealings/involvement, I have to wonder who in today's Class I world, and for that matter who at the STB, has even bothered to read the document much less be governed by it?!?
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> I know there are some short line managers (senior and otherwise) that have no idea of its existence much less what it was intended to accomplish. When Messrs. Warchot and Borman [advocates of the RIA] retired from their roles with AAR and ASLRRA respectively, one had to wonder who from the industry trade associations are making sure the signatories are trying to uphold the rules?

And so I ask: who among WIR readers even remembers the RIA, let alone was able to make use of it?