

## **A Switch on the Tracks: Railroads Roar Ahead Global Trade, Fuel Costs Add Up To Expansion for Once-Dying Industry**

By Frank Ahrens  
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RADFORD, Va. -- When Bob Billingsley hired on with Norfolk Southern railway 31 years ago, he was a rookie on work crews that were closing unused lines as the nation's economy turned its back on the railroads.

Now he's in charge of raising the roof of a Norfolk Southern tunnel in southwestern Virginia to clear headroom for the double-stacked container cars that have become the symbol of the industry's sudden surge thanks to a confluence of powerful global factors.

"For years, we were looking for ways to cut costs to increase profits," said Billingsley, as a train rumbled by. "Now, we're building business to increase profits."

The freight railway industry is enjoying its biggest building boom in nearly a century, a turnaround as abrupt as it is ambitious. It is largely fueled by growing global trade and rising fuel costs for 18-wheelers. In 2002, the major railroads laid off 4,700 workers; in 2006, they hired more than 5,000. Profit has doubled industry-wide since 2003, and stock prices have soared. The value of the largest railroad, the Union Pacific, has tripled since 2001.

This year alone, the railroads will spend nearly \$10 billion to add track, build switchyards and terminals, and open tunnels to handle the coming flood of traffic. Freight rail tonnage will rise nearly 90 percent by 2035, according to the Transportation Department.

In the 1970s, tight federal regulation, cheap truck fuel and a wide-open interstate highway system conspired to cripple the railroad industry, driving many lines into bankruptcy. The nation's 300,000 miles of rails became a web of slow-moving, poorly maintained lines, so dilapidated in spots that tracks would give way under standing trains.

The Staggers Rail Act of 1980 largely deregulated the industry, leading to a wave of consolidation. More than 40 major lines condensed into the seven that remain, running on 162,000 miles of track.

But the changing global market has fueled prosperity -- and the need to add track for the first time in 80 years. Soaring diesel prices and a driver shortage have pushed freight from 18-wheelers back onto the rails. At the same time, China's unquenchable appetite for coal and the escalating U.S. demand for Chinese goods, means more U.S. rail traffic is heading to ports in the Northwest, on its way to and from the Far East.

Coal still accounts for the most tonnage hauled by U.S. railroads, but it is the ocean-crossing shipping container -- carrying autos, toys, furniture and nearly every product a consumer will buy -- that has lit a rocket under the railroad industry. Passenger rail traffic is also increasing; 2007 was Amtrak's fifth consecutive year of increased ridership, up 6 percent from 2006.

The zeitgeist has even dropped a "green" gift in the industry's lap. A train can haul a ton of freight 423 miles on one gallon of diesel fuel, about a 3-to-1 fuel efficiency advantage over 18-wheelers, and the railroad industry is increasingly touting itself as an eco-friendly alternative. Trucking firms also use the rail lines; UPS is the railroad industry's biggest customer.

Rail traffic, revenue and profit began to soar in 2002-03 and seem largely immune to the economic downturn. Last Tuesday, for instance, CSX reported a record first-quarter profit. On Friday, the stock price of Western rail giant Burlington Northern Santa Fe (BNSF) hit an all-time high. At the industry's nadir in the 1970s, the average annual rate of return on investment for a railroad company was 1.2 percent. By 2006, that number was 10.2 percent.

And even though the economic slump has reduced key traffic about 4 percent this year compared with last, it has not slowed the railroads' urgent tracklaying. Capital expenditures this year are up, as the railroads think the downturn is temporary, said the industry's trade group, the Association of American Railroads.

Seven railways control nearly all of the freight shipped in the United States. In the West, they are, from largest to smallest by track mileage, Union Pacific, BNSF, Canadian Pacific/Soo Line and Kansas City Southern. In the East, they are Norfolk Southern, CSX and the Canadian National/Grand Trunk lines. Most of them have extensive expansions planned or underway.

The companies are attracting the attention of big-money investors, such as Berkshire Hathaway Chairman Warren E. Buffett, who sees a future in the Industrial Age behemoths. Buffett, a Washington Post Co. director, began loading up on shares of BNSF last year and is now its largest shareholder, with more than 18 percent of its outstanding stock.

The industry estimates it will take \$148 billion in expansion to carry the amount of traffic anticipated by 2035. Of that, the railroad companies will contribute \$96 billion, said the industry's trade group. The rest would have to come from the federal government and the states.

The railroads argue that more trains mean fewer trucks on the road and less air pollution, public benefits that the public should help pay for. Further, the railroads could not achieve the profits they say Wall Street demands without government subsidies. The railroads seek a tax credit, backed by Sen. Kent Conrad (D-N.D.), that would help them expand further.

Meanwhile, the railroad industry's long-standing antitrust exemption has attracted the attention of lawmakers. They seek to eliminate the exemption and closely examine the rates railroads charge to haul freight, which the industry says would cripple its expansion at a critical time.

The railroads' rate structure has also drawn the ire of some of their customers: Nearly 30 antitrust lawsuits have been filed against major railroads in recent months, including one by agri-giant Archer Daniels Midland last month, alleging collusion and price-fixing.

For some lawmakers and advocacy groups, today's rail industry recalls that of the late 1800s, when the only ceiling on rates was the limit of a rail baron's avarice. The railroads say today's rates are reasonable and reflect something the industry has not had in decades: pricing power.

"Customers had gotten used to rates going down all those years, and all of the sudden, they're not anymore," Norfolk Southern vice president James A. Hixon said in an interview. "They don't like it."

Sen. John D. Rockefeller IV (D-W.Va.), whose state depends on trains carrying coal, introduced a bill last year that the railroad industry derides as the "Reregulation Act."

The legislation, which has not been scheduled for a floor vote, would allow shippers to easily challenge railroad rates at the Surface Transportation Board, which regulates the rail industry. Now, some shippers say, they have almost no recourse if they think the railroads are gouging them.

"It's a byzantine system, and it's rigged against the shippers," said Robert Szabo, executive director of Consumers United for Rail Equity, a coalition of shippers who say that the railroads' monopoly pricing structure raises the cost of consumer goods.

The railroads "have been in a seller's market since 2004," said Szabo, whose group backs Rockefeller's legislation.

Sen. Herb Kohl (D-Wis.) introduced a bill last year that would remove the railroads' antitrust exemption. Unlike other industries, the Department of Justice cannot block a merger between rail companies, and the STB has been criticized for siding too often with the industry.

"Competition has virtually gone away," Kohl said in an interview. His bill has not been scheduled for a floor vote. "They have carved up the country, and each [railroad] controls its vast area."

Sen. Byron L. Dorgan (D-N.D.), a co-sponsor of both bills, cites an example: The railroads charge four times as much to ship a carload of grain from Bismarck, N.D., to

Minneapolis as they do to ship it from Minneapolis to Chicago, although the distances are about equal. The reason: Shippers have only one choice of railroad out of Bismarck.

The railroad industry calls it "differential pricing," and "it occurs every day in the airline industry," said Edward R. Hamberger, president of the railroad trade group.