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Are We Entering a New Railroad Golden Era?

Across the Globe, Money is Pouring into Rail Infrastructure—but is it Enough in US? 80% More Miles on a Gallon of Diesel than 30 Years Ago

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It's staple of many college business textbooks – how in the early 1900s the railroads didn't perceive how the car would revolutionize travel, or refused to adapt even if they did, leading to a century of decline as cars and trucks took over the movement of people and goods across the US.

But is it possible we are entering a new "Golden Era" for railroads?

In North America, the fortunes of the seven major rail freight carriers (Union Pacific, CSX, Norfolk Southern, Burlington Northern, Kansas City Southern, Canadian National and Canadian Pacific) began to rise in the 1990s with the surge in imports. Import volumes grew at double digits annually, with many importers using rail carriers to move containers from east or west coast ports further inland.

Soaring fuel prices and fuel surcharges also moved in the rail carriers' favor. Shippers were more likely to put up with the longer transit times and more inconsistent service from the rail lines as costs for truck movement soared. Children's apparel maker Carter's, for example said earlier this year it planned to move 15% of its current trucking volume to rail or intermodal transport in 2008.

The net result is expected steady growth in rail volumes for years to come – and even resurgent interest in rail for passenger traffic. China and Europe are investing billions in rail infrastructure for moving freight and people, and investors such as legendary Berkshire Hathaway CEO Warren Buffet are betting rail carriers will provide outsized returns based on the fundamentals.

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Will Trucking Dominance Finally Decline?

Despite growing imports since the 1990s, trucking's share of the freight market continued to grow through at least 2004, as the need for speed and flexibility in increasingly Lean supply chains trumped the lower cost of the rails. Trucking accounted for 82% of the U.S.'s truck-and-rail intercity-freight spending in 2004, up from 78% in 1990, according to Eno Transportation Foundation, a research organization in Washington, D.C.

However, several trends look bright for rail growth:

- Despite a recent slow down, most economists expect strong growth in import volumes to continue over time.
- Many policy experts are looking at increased use of rail as a partial answer to congestion issues on US highways. The recent National Surface Transportation and Revenue Study Commission report specifically called for a broad multi-modal strategy to increasing logistics ca-

Are We Entering a New Railroad Golden Era? (Con't)

pacity, and noted the advantages of moving more freight by rail (and waterways). (See **The National Surface Transportation and Revenue Study Commission report**.)

- Rail will also provide environmental advantages, an increasingly important factor. Environmental concerns may lead some shippers to use rail to reduce their own carbon footprints, and politicians may take action to favor rail movement for similar reasons.
- Though rail carriage is also impacted by rising fuel costs, the effect is less for rail than for trucking.

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General investors are noticing the same bright prospects for rail carriers. While most of the rest of the US stock market is down sharply in 2008, Burlington Northern is up 26% since the start of this year; Union Pacific, the No. 1 freight line, is up 32%, even as volumes are flat in the face of a slow economy. **John Larkin**, a transport analyst with Stifel Nicolaus, sees some freight stocks climbing 10% to 15% more over the next year -- and much higher over the long haul.

Meanwhile, private and public investments in passenger and freight rail infrastructure are simply staggering. Europe is pouring billions into new train tracks and further billions to rationalize the confusing mix of track widths in different nations that now cause huge delays in the transfer of freight loads at national borders. Having completed the record-breaking high-altitude rail link between Qinghai and Tibet, the Chinese government is quadrupling its spending on its railroads to $160 billion over the next three years. Plans call for 10,000 miles of new track, on top of the existing 56,000-mile net-

work, to be laid by 2010, half of it dedicated to high-speed passenger trains that would zip between cities at 200 miles an hour.

"All the evidence is there that the train is returning to a degree once never expected [and that] an economic and cultural tsunami is about to transform the United States," says Harvard professor **John Stilgoe**, author of the recently published book ***Train Time***. "Change is everywhere along the railroads....Track is being expanded, modernized and relaid, and once-abandoned rail right-of-ways are being reclaimed. And what you are seeing now is only the beginning. The best is yet to come."

There is already some evidence that more commuters in large US cities are already moving to trains for workday commutes, with up to 15% making the switch in the past year in some metro areas. If that trend were to continue in the face of rising gas prices and traffic delays, it might actually benefit freight movement into cities by relieving some of the huge congestion problems.

One possible fly in the ointment – lack of rail infrastructure. A report from 2007 sponsored by the Association of American Railroads says $148 billion will be required between now and 2035 to add enough capacity in both long haul and short haul

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lines to keep service at approximately today's levels. (See **Rail Infrastructure Improvements – Searching for $148 Billion**.)

Rail congestion is starting to develop and stands to get much worse. If significant new track isn't laid, Burlington Northern CEO **Matthew Rose** predicts a possible "rail meltdown" and "rail traffic gridlock" by 2035. Adds Paul Bingham, a transportation expert at research firm Global Insight: "It's not rocket science to see we have a calamity coming down the road."