

Hearing Before the Surface Transportation Board**Docket No. Ep 775****Growth in the Freight Rail Industry****September 16 and 17, 2024**ENTERED
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Public Record**Summary of Testimony for
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Oliver Wyman**

Introduction

I am Adriene Brooks Bailey, a Partner with Oliver Wyman, a leading general management consulting firm. Before joining Oliver Wyman, I held senior executive positions at Southern Pacific Railroad, CSX, Pacer International, and Yusen Logistics. I led the service design function at both Class I railroads and was involved in all aspects of intermodal operations at Pacer International and Yusen Logistics. At Oliver Wyman, I currently lead the North American Rail Practice. I have more than 30 years of experience as a railroad executive, railroad customer, and consultant to railroads.

In my testimony, I will share my and Oliver Wyman's view of the importance of growth to North American freight rail, and what the collective stakeholders in this critically important industry must do to reverse the market share erosion that we have seen in the past 10-15 years.

Why is growth in the rail industry important?

To start, it is important to note that rail is a highly energy efficient, sustainable, safe, and low-cost mode for transporting freight. North America has the largest self-sustaining rail freight network in the world.

As the Board pointed out in its hearing notice, it is concerning that Class I rail volumes have not materially grown over the past decade. Indeed, rail is the only freight transportation mode that has lost overall net tons since 2017. In addition, the US Department of Transportation currently projects that rail will have the slowest growth among freight transportation modes through 2050

– which means that railroads are predicted to lose share to other freight modes over that timeframe.

Implications of share loss

To put context around what a continued loss of rail market share could mean for our society as well as rail stakeholders, I will summarize an analysis that Oliver Wyman performed in 2022, in which we looked at the implications of several scenarios for rail market share through 2050.

The Federal Highway Administration (FHWA) provided a baseline forecast that anticipates that rail market share will drop four percentage points by 2050. It is important to note that the FHWA forecast does not reflect the critical trend of flexible freight (which is freight with a choice between truck and rail) migrating to truck.

We created three alternative scenarios to project the potential for rail to gain, hold, or lose additional market share. In every one of these scenarios, the volume of rail freight grows. But there are far-reaching implications of rail losing share versus gaining share relative to truck. For example:

- **Safety:** Rail has far fewer incidents each year than trucking that cause injury or a loss of life. On a ton-mile basis, rail is about 28 times safer for the public and workforce than trucking.
- **Road investment:** More trucks on highways would require billions more in federal and state dollars to be spent on maintaining and expanding road infrastructure. We estimate that by 2050, the US would need to spend an additional \$332 billion on roads if railroads fail to take share back from trucks.
- **Energy efficiency:** In 2022, trucking moved one and a half times as much freight as rail, but generated 11.5 times more greenhouse gas emissions. Even if in the future both truck and rail achieve net-zero emissions, rail's vastly lower energy consumption will be increasingly valuable – since no matter what future energy sources we use, they are unlikely to be unlimited or free.
- **Shareholder returns:** Losing additional market share would eliminate billions in revenue and operating income, which is needed to ensure railroads can adequately raise capital, continue to invest in infrastructure and assets, and employ a growing workforce – all of which benefits US businesses and the economy as a whole.

What is causing the market share erosion that has plagued the industry for a decade?

Next, I will briefly review what is causing current rail market share erosion. Since the Staggers Act deregulated rail in 1980, the railroads have delivered tremendous improvements in productivity – much of which has been delivered back to shippers and consumers in the form of rate reductions.

Starting around 2015, however, productivity gains began to flatten out and rates began to move up again, while volumes began to stagnate; the industry has since been ceding share to truck year over year. It is tempting to attribute this market share loss exclusively to the decline of coal, but other major non-coal sectors of rail freight (with the exception of intermodal) also have not been growing.

What is behind this shift? In 2020, Oliver Wyman surveyed large rail shippers and found that 100 percent believed truck to be superior to rail on key attributes of customer experience. At the same time, shippers consistently told us that they wanted to do more with rail because of its advantages, but that the product and experience simply are not meeting their supply chain needs.

When I began my career in the industry, the most important thing to a shipper was the pure transportation cost on the invoice. Today's shippers are increasingly focused on the total cost of doing business with a carrier or transport mode. Freight rates are still important of course, but shippers now factor many other considerations into their choice of a freight carrier or mode.

Based on our interviews with shippers, Oliver Wyman identified three important factors that are causing shippers to shift more freight to trucking:

- Railroads must become more integrated with their customers to understand how they can best fulfill shippers' more complex needs. They also need to ensure shippers are not making decisions that could lock them out of future rail access (such as converting rail sidings and unloading doors to other uses).
- Rail must improve overall service performance. Shippers we surveyed expressed disappointment in rail's on-time performance, shipment visibility, and ETA accuracy. It is important to note here that shippers are not expecting "fast" service nor even the same degree

of reliability as trucking. But they do expect more transit time consistency and a more responsive approach to problem resolution if they are going to consider rail.

- Railroads must deliver a better overall customer-centric experience. It is no secret that trucking is considered the gold standard for ease of doing business. Rail shippers we talked to expressed concerns over response times, transaction processes, and rail-related service failures. This may be the most difficult challenge to overcome, however, as it requires significant cultural and organizational transformation.

Can the volume decline trend be reversed?

If railroads can deliver consistent, reliable transit times and a customer experience that is much closer to trucking, we believe that rail market share erosion could be reversed. In addition, we identified several specific volume and market share growth opportunities that the Class I railroads could begin to pursue, and which I will briefly discuss:

- **Intermodal:** While railroads have a 65 percent market share for single-railroad intermodal in lanes over 1,500 miles, they only account for 11 percent in lanes under 750 miles. We estimate that rail intermodal could serve as many as 27 million out of the 41 million total truckloads in these lanes, using the current terminal and railroad network.
- **Industrial:** Rail could capture more freight growth from the manufacturing upturn now occurring in North America. Railroads are developing large flagship transloading and industrial parks in locations they can efficiently serve. But we believe a more comprehensive view is needed to ensure shippers are considering rail when selecting sites and to prevent the erosion of access at existing rail-served sites. There is a need for a renewed focus on building rail access to shippers – including new lanes, connections, service offerings, and transload facilities.
- **Short lines:** With a strong customer-first culture, many short line railroads have realized impressive volume gains in recent years by leveraging infrastructure, ancillary services, and industrial development that is not directly available to the Class I's. Oliver Wyman recently interviewed senior executives representing some 300 of these short line railroads. Many believe there is more volume to be captured if Class I railroads would help their short line connections better leverage their strengths and complement their efforts to deliver growth. There are several steps that Class I's could take here, including; 1) ensuring C-suite line of

sight and support for growth-oriented shortline strategies; 2) increasing active collaboration with short lines to attract more shippers to rail; and 3) Class I's working to improve their processes and timelines for responding to short line requests for new business support, as well as interchange performance with their short line connections.

In general, railroads face a challenge that truckers do not, which is that they must work with connecting railroads for well over half of their shipments. Is it harder? Yes. Does that mean it is impossible to design joint processes that are simple, fast, and easy for customers, or to deliver consistent transit times door-to-door? At Oliver Wyman, we think the answer is no.

I do believe that as a group, the Class I's are now more strategically focused on growth. I am hearing CEO's articulate that earning more of shippers' share of wallet and bringing more volume to the railroads is going to be the next opportunity to create substantive earnings growth. Ultimately, I am confident that successful railroad growth strategies will prove that increasing market share also yields higher investor returns.

If railroads can deliver a customer-centric experience and more reliable on-time performance, they will take trucks off of our highways. And we will all enjoy the benefits of a US transportation system that is safer, less costly, more energy efficient, and more sustainable.

Citations

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