

ISSUE ANALYSIS:

Impacts of Increased Competition on Rail Labor

Which side of the debate should rail labor support in order to best protect the interests of union members? The introduction of modest pro-competitive changes, such as those included in S. 621, H.R. 2784 and H.R. 3446 would unquestionably change the way railroads approach their business, force them to adopt real growth strategies, and in turn, rail labor and the customers they serve will benefit. Consider:

1. The downsizing that typically accompanies deregulation has already taken place. The ranks of transportation and maintenance employees have been cut from 331,707 in 1980 to 147,808 in 1998, a decline of about 55%; the number of professional and clerical employees also have been reduced from 88,198 in 1980 to 19,214 in 1998, a decline of about 78%. Although there may be some typical reductions that result from attrition, our economic analysts do not see any significant ability of the railroad industry to further reduce the ranks. This opinion is supported by a recent Morgan Stanley Dean Witter analysis dated December 15, 1999 entitled, "Railroads: Troubles Don't End in 2000." In this report, Jim Valentine asserts, "we do not expect any further wave of headcount reduction, as we saw in the early 1990s, because there doesn't appear to be that much fat left."

2. The future of railroading will be determined based upon the industry's ability to grow. In order to grow, railroads need to focus on their customers. Yet according to many rail customers, railroads are arrogant and unresponsive. According to one shipper quoted in an October 4, 1999 Traffic World editorial, "There isn't one [railroad] today that is easy or convenient or just competent enough to warrant doing business with." Another rail customer was quoted in the same editorial as stating, "If I could figure out a way to conduct our business without using railroads, I would absolutely without any hesitation stop doing business with them." These are not isolated viewpoints. I have personally heard similar comments from rail customers in just about every industry that uses railroads—including IMCs. Without some significant changes to the way railroads run their business, there will be little or no growth, and in turn, little or no opportunity for rail labor to either grow in numbers or increase wages. Competition is the only thing that is likely to change the way railroads view their business responsibilities.

Railroad representatives often snicker at the assertion that competition will change railroad behavior. They claim that if railroad management could address these issues, they would be doing so because Wall Street gives them the incentive. In reality however, Wall Street has consistently accepted the railroad practice of achieving stock earnings through the cost cutting associated with mergers, although the latest BNSF-CN announcement may mark the beginning of change in that trend. Top rail analysts on Wall Street have recognized for some time now that the dwindling number of railroads will soon force this business strategy out of existence. And for at least two years now, these same analysts have been calling for earnings growth through improved customer service. According to an essay written by Jim Valentine in 1997, "If railroad management really wants to get Wall Street's attention, it needs to develop a revenue growth strategy." He continues, "When the railroads stop being distracted by who has the biggest network or locomotive fleet and begin to really focus on the customer—especially the small-to-medium customers—including their short-line feeders, we may see market share gains from trucks for the first time ever... railroads can appease their shareholders with revenue growth by putting the customer first." Could the railroads put the customer first today? Sure they could, but without the forces of competition for a large chunk of their customer base, they won't because they don't have to. No monopoly industry has ever embraced increased competition with open arms. But once those monopoly industries have been deregulated and are operating in a competitive environment, revenues have increased, the number of new jobs has grown and customers have benefited in the form of improved services and competitive rates.

The financial projections for what would happen to the railroad industry if competition such as that which is outlined in pending legislation were adopted is summarized in a separate analysis, but in short, year 2005 rail industry annual profits will be \$500 million higher if pro-competitive policies are adopted.

The Alliance for Rail Competition then commissioned L.E. Peabody & Associates, Inc. to conduct a follow-up study projecting the impact on rail labor. Similar to the financial impact analysis, L. E. Peabody & Associates looked at a "status quo" scenario versus a "competitive service" scenario. Under the "status quo" scenario, they assumed that current rail performance problems stabilize this year and that no changes are made to rail policy; their resulting projections show that modest growth will occur. The additional employees required to handle that growth is projected to be a modest 4,342 by the year 2005, or an increase of 3.1%.

However, under the "competitive service" scenario, our economists assumed that competitive policies, consistent with the provisions included in S. 621 and H.R. 2784, were adopted, and the results clearly show rail labor would be much better off. With pro-competitive policies in place, rail labor jobs would be projected to increase by 11,870 by the year 2005, or by 8.5%. Further, total compensation would increase by \$652 million under a competitive environment, as compared to only \$236 million if rail managements continue to follow the operational policies in place today.

At best, maintaining the status quo offers little in the form of job growth, and at worst, rail labor could be looking at a stagnating industry with dwindling resources in a relatively short period of time—certainly within the next decade. On the other hand, rail labor stands to gain far more job growth and compensation as a result of the adoption of competitive rail policies.