The Surface Transportation Board

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The Surface Transportation Board

- Created by ICC Termination Act of 1995
- Successor agency to the ICC—child of deregulation
- Residual economic regulation of the railroads
- Reduced scope of regulatory activity
- No direct role in infrastructure investment, but Board's decisions can affect it

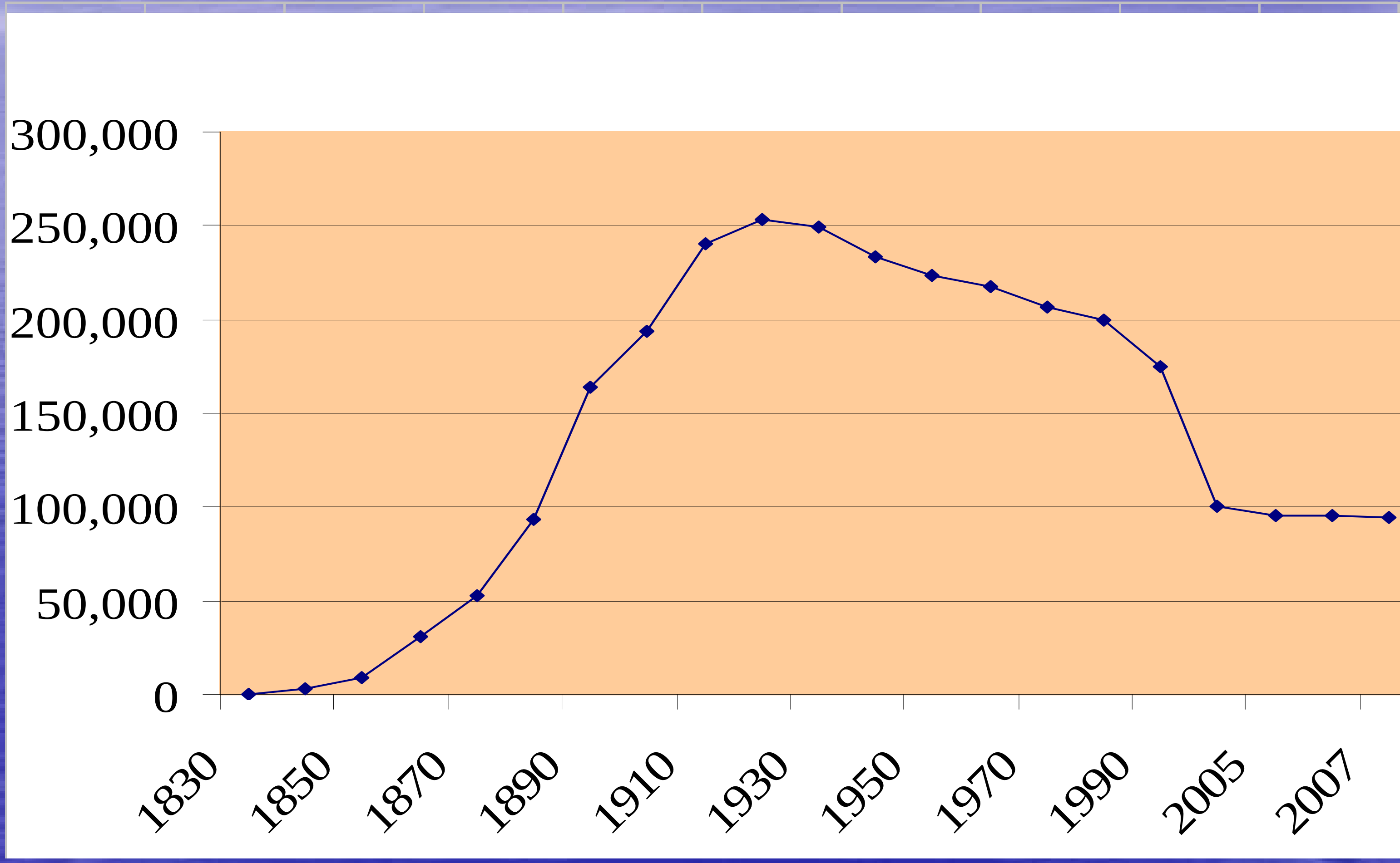
Trends in Railroad Capacity

- Too much railroad track was built in the 19^{th} Century
- Traffic losses in 20^{th} Century, especially to truck, led to serious excess capacity
- Railroads tended to lower rates to cover marginal costs, not fixed costs
- Restrictive regulation made network rationalization difficult

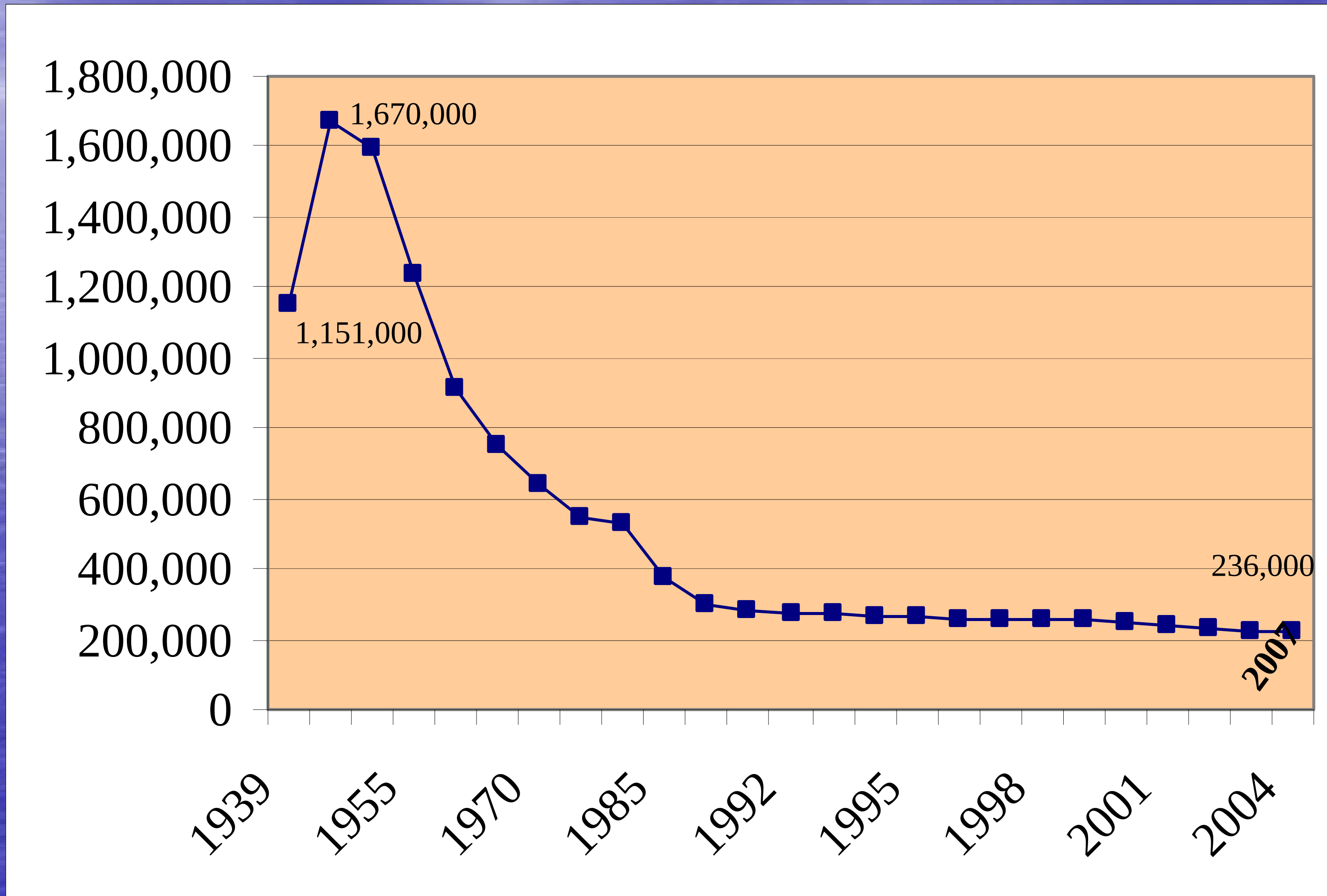
Trends in Railroad Capacity

- Staggers Act of 1980 gave railroads more freedom to shed excess capacity
- Class I rail network reduced to 1880's track mile levels
- Hundreds of shortline railroads created
- Staggers successful in improving the profitability of US railroads

Growth & Decline of Class I Railroad Mileage



Railroad Employment 1939-2007



Railroad Industry Cost of Capital and ROI 1996-2007

	Cost of Capital	BNSF	CSXT	NS	UP	KCS	SOO	GT
1996	11.9%	8.6%	8.9%	13.0%	9.3%	7.2%	23.5%	0.0%
1997	11.8%	8.4%	9.8%	13.1%	5.2%	3.6%	12.3%	5.2%
1998	10.7%	9.7%	8.1%	10.5%	2.9%	9.1%	4.9%	3.0%
1999	10.8%	9.5%	3.8%	5.2%	6.8%	6.4%	2.5%	25.4%
2000	11.0%	8.8%	3.6%	5.5%	6.9%	6.3%	5.6%	5.9%
2001	10.2%	7.1%	4.6%	8.3%	7.6%	7.0%	5.9%	4.9%
2002	9.8%	6.4%	5.2%	9.1%	8.6%	6.5%	5.7%	3.1%
2003	9.4%	6.2%	4.0%	9.1%	7.3%	3.7%	0.01%	4.5%
2004	10.1%	5.8%	4.4%	11.6%	4.5%	8.3%	3.3%	6.0%
2005	12.2%	10.3%	6.2%	13.2%	6.3%	5.9%	8.9%	8.1%
2006	9.9%	11.4%	8.2%	14.4%	8.2%	9.3%	11.6%	9.5%
2007	11.3%	10.0%	7.6%	13.6%	8.9%	9.4%	15.3%	10.1%

Capacity Issues

- After years of excess capacity, capacity shortages arose in the mid-2000's
- Economic growth and expanded trade with China spurred intermodal traffic
- Trucking capacity grew limited due to higher fuel prices, driver shortages, etc.
- Rail market share rose, congestion increased and rates rose

Rail Capacity Issues

- Widespread concern that nation's transportation infrastructure could not meet future demand
- DoT's Freight Analysis Forecast and Cambridge Systematics' study for AAR envisioned a serious rail infrastructure investment shortfall

Rail Capacity Issues

- Traffic down dramatically in past year: roughly one-half million railcars and thousands of locomotives parked
- Railroads reversed recent increase in hiring and have furloughed tens of thousands of employees
- Rail rates have, however, remained steady

Rail Capacity Needs

- Reassessment of rail infrastructure capacity needs
- STB commissioned a capacity study by Christensen Associates
- Report released April 2009
- Very different findings from prior DOT and Cambridge Systematics' results

Rail Capacity Needs

- Christensen took account of recent downturn and employed more conservative (realistic?) forecasts of economic growth
- Christensen also examined the principal components of rail traffic demand

Rail Capacity Needs

- Christensen study criticizes failure by DoT or Cambridge Systematics to offer range of forecasts
- E.g., OASDI forecasts of GDP growth for 2002-2035 are 80% for low rate of growth and 151% for high rate of growth—implies growth for rail of 61% to 116%
- Other factors will affect demand for freight rail service including fuel prices
- Christensen study still finds a rail capacity funding gap

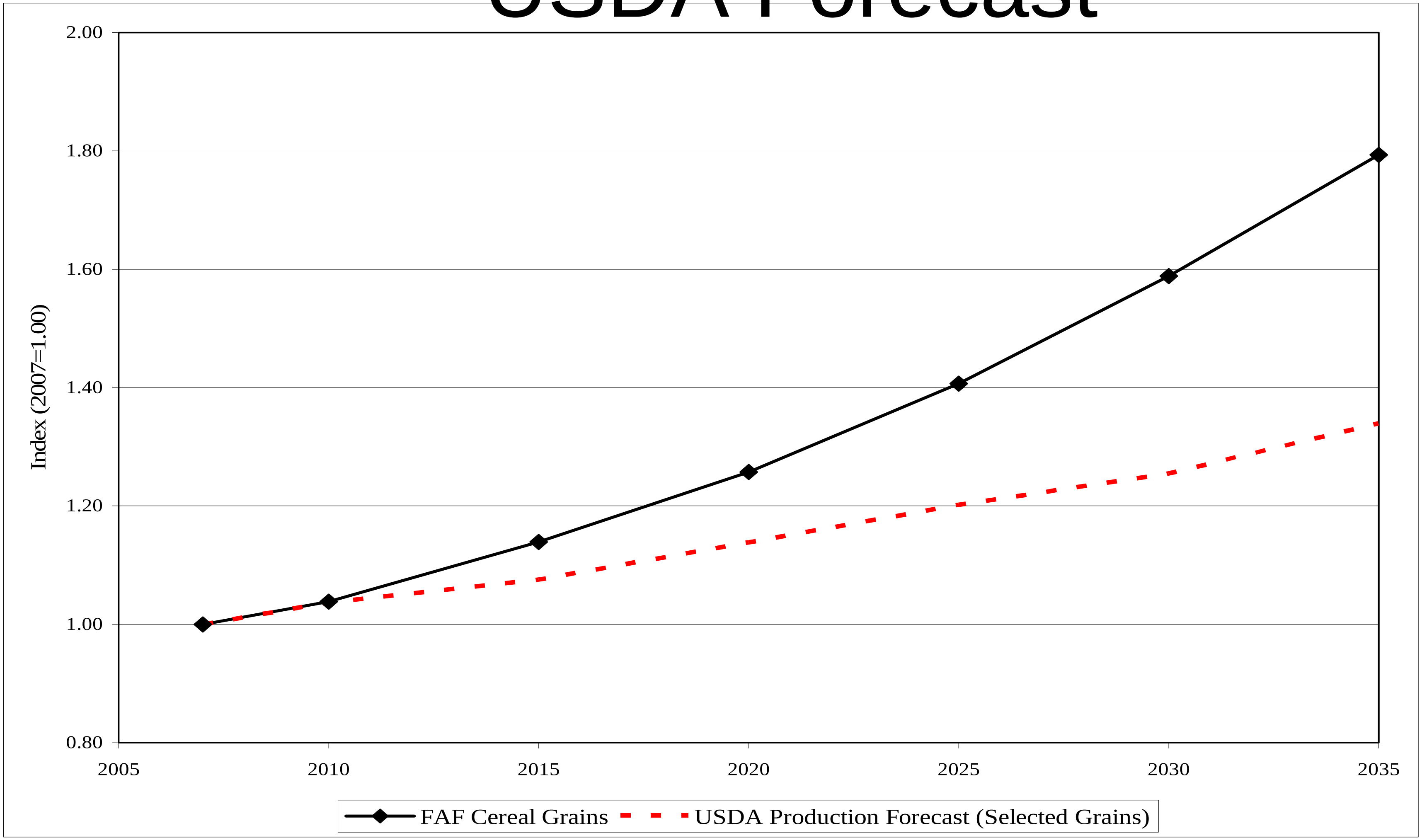
Rail Capacity Needs

- Christensen also examined components of freight rail demand, especially coal, grain and intermodal
- FAF projected 78% increase in rail coal tonnage between 2002 and 2030, but EIA's Annual Energy Outlook projects only a 24% increase, and that presumes: tax credits for solar and wind power will expire, and no increased restrictions on GHG emissions beyond required under 2009 law
- Clearly, prior coal traffic forecasts are likely overstated

Rail Capacity Needs

- Cereal grains category is second largest in DoT's FAF
- FAF forecasts near doubling of output between 2002 and 2035 to 150 million tons
- Rail tonnage is projected to grow 22% from 2010 to 2020 and 28% from 2020 t0 2030
- USDA forecasts are not as long range but suggest that cereal grains rail shipment growth rates in FAF model are excessive

FAF tonnage for Cereal Grains vs. USDA Forecast



Capacity Issues Long-term

- **Future demand for freight movement predicted to increase, but by how much?**
- **Challenge for private companies to meet that demand**
- **Constraints on rail capital investment**
  - **RRs inability to earn adequate revenue**
  - **Demands of investors**
  - **Undercapacity and overcapacity at the same time**
- **Demands of changing freight flows**

Potential for Public Investment in Rail Infrastructure

- Can railroads earn enough to maintain and expand the network and fund needed investments such as PTC
- Railroad Trust Fund concept – Class I opposition
- Public Private Partnerships (PPPs) –
  - CREATE
  - Alameda Corridor
- Short Lines and 286K ton car problem
- Investment tax credits—Railroads' Solution

STB/Rail Presentation

- Thank You. Any Questions