the WIDENING WAY to BETTER RAILROADS

An Address by
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A LITTLE more than a year ago, I spoke for the first time before your Society. I appeared then, as I appear now, as the representative of a troubled industry. But I am happy to say that today's troubles of the railroads—on the surface, at least—are less painful than in those recession-darkened days of early 1958.

A great deal has happened since that previous appearance. Freight traffic and revenues, at low ebb throughout 1958, have begun to move upward with what appears to be mounting vigor. One indication of the change in economic climate is the latest forecast of the 13 Regional Shippers Advisory Boards. These biggest users of transportation have estimated that freight carloadings in this second quarter of 1959 will show a 12 per cent gain over year-ago figures. Significantly, the biggest increases have been forecast for the hard-hit eastern railroads. Yet even a 12 per cent rise over year-ago levels would still be 11 per cent under 1957 loadings.

So we hope we have bid farewell to the worst of the economic recession that has plagued us. However, in all candor, I find it difficult to show complete optimism over the outlook, either short or long range. The reason is simply that there still remain too many awesome barriers in the way of railroads producing the best service they know how.

Economic recovery may, in fact, magnify these obstacles. I think one of the greatest dangers the industry faces is that this modest pickup will be interpreted as a sign that all is well with transportation and that nothing further need be done to correct the grave imbalances within the industry. The multitude of transportation policy inequities would then go uncorrected and would continue their work of undermining the railroads and short-changing the public.

Are effective moves now being taken against these underlying problems? Frankly, the answer is **no.** Washington gears up for a study here, and we hear rumors of a study there. But the further legislation all the experts recognize as essential is so far nowhere in sight.

Since my talk of a year ago, we have witnessed two important legislative events on the Washington scene. First was passage of the Transportation Act of 1958 and the second was repeal of the 3 per cent

excise tax on the for-hire transportation of freight. I feel these actions constituted a needed start toward achieving equality of competitive opportunity for the several different forms of transportation. But not even by the longest stretch of imagination could they be viewed as ending the discrimination existing in taxation, regulation and promotion policies. Common sense is still pitifully lacking in the nation's over-all approach to transportation.

America's railroads exist in two worlds. They work in the tough competitive world of the present but they are saddled with laws and regulations and work practices that belong to the world of half a century ago. The twin devils of ancient government policies and antiquated work practices continue to hound and harass these carriers whose services are so indispensable to the nation.

I don't think I need spell out to this informed audience the details of what we are up against in the area of public policy inequities. You know as well as we railroadmen that the lines are regulated much more stringently than other carriers.

You also know that railroad facilities, being private property, are loaded with tremendous burdens of taxes not faced by competitors using tax-built and tax-free facilities. And railroads are handicapped and victimized by all-out government development of water, air and road transportation.

Now I said I would not detail these glaring inequities that, from where we railroadmen sit, appear to be doing a most effective job of preventing us from giving the best in rail services. In fact, sometimes, as in time of recession, these inequities seem to be aimed at preventing us from surviving at all. **I wonder sometimes if through such policies, we are building up transportation giants with feet of clay. Is government so impeding and penalizing the nation's great basic carrier—the railroads—and so promoting and subsidizing other forms of transportation that it is creating more transportation problems than it is solving?**

You might find an answer in the worsening transportation problems of our great cities. Certainly, New York City offers lessons in point. Rapid outward expansion of built-up areas and the additions of new millions to metropolitan centers should long ago have compelled our city fathers to offer every encouragement to the development of adequate rapid transit facilities. But until recent months at least, cities continued to march off in every other direction. **With highways and parking lots the favored weapons, they have been fighting a hopeless, losing battle against traffic stagnation and urban decay. We dare hope that the greatest weapon in the transportation arsenal—the safest, most efficient carrier yet devised—will one day be given a real chance to prove its effectiveness.**

What is happening in our big cities holds true in varying degrees throughout the country. This 1959 fiscal year, the federal government, capping off years of

steadily rising expenditures for air, water and highway development, is pouring out a total of $3.7 billion on behalf of these other forms of transportation.

The growth curve of such federal spending can only prove anew that nothing is so easy to spend as public money. There is always that comforting illusion that public money is someone else's money. But let's not deceive ourselves as to whose pocket is being picked.

When we speak of "low air fares" and "cheap water transportation," let's face up to the facts behind these fine phrases. As a user of such services, you get a relative price break only because someone else—some taxpayer—pays the balance of the costs. Every time a man flies from New York to Washington, some poor taxpayer in Tallahassee, Chicago or Seattle puts up a little more of his hard-earned money to help buy the ticket. I might add that the taxpaying railroads themselves are also plucked to help out.

What these inane policies boil down to is the virtual elimination from transportation of true economic competition. Certainly, prices offered by all contenders in the field do not now reflect full costs of providing the services people buy. The scales have been tilted, knocking the railroads' share of intercity freight traffic down from 67 per cent in 1945 to about 45 per cent today. The rail share of commercial intercity passenger traffic has nose-dived from 73 per cent to a current 30 per cent.

And what about rail competitors? The

share of intercity freight traffic handled by motor trucks has trebled in the post-war period, to a current 21 per cent. And inland waterway traffic, not including the Great Lakes, also almost trebled.

On the passenger side, the share of commercial intercity traffic moving by motor bus rose nearly 50 per cent to about one-third of the total at present. And the airlines' share literally skyrocketed, multiplying 12 times to 36 per cent of all traffic.

Now, gentlemen, such changes have made many wonder if there were something fundamentally wrong with the rail method of hauling goods and people—if, indeed, these other carriers did not somehow have a superior claim to customer patronage. Let me nail that one right on the head. You may recall that in discussing railroads in the transportation future when I was here last March a year ago, I cited the important ways in which, all costs considered, railroads produce transportation service with unbeatable efficiency and economy.

When it comes to employing fuel, materials and men to produce a service, nothing can match the efficiency of trains of steel wheels running on steel rails or concentrate so much capacity in a limited space. These attributes should be first considerations when we weigh alternative means of hauling goods and people. But political favoritism has brushed them aside. Only in time of grave emergency when every man, every ton of steel and every gallon of fuel counts in the balance of victory do railroad assets get full leeway.

Every military leader will recall that railroads in World War II, using their same basic plant, doubled their freight traffic load over that of preceding peacetime years—and their passenger volume quadrupled. At the height of the emergency, railroads handled 3 out of every 4 units of traffic moving between our cities.

Could they do it again? I wish I could answer "yes" to that question. But I cannot. Under the impact of artificial and uneconomic diversion of business, rail passenger car ownership has so declined that it is now less than two-thirds of the fleet which turned in such a fantastic job in World War II. The Office of Civil and Defense Mobilization recently reported to Congress that a "disproportionate burden" would fall on rail carriers in event of war, and that it feared early shortages of freight and passenger cars. Expansion of normal economic activity could also run into the bottleneck of equipment shortages in the not-too-distant future.

Must we simply sit back and wait for these blows to fall, or is there forthright action that might be taken to head them off? Fortunately, there are many steps that can be taken to solve our transportation problems. But these things will have to be done, not simply studied and talked about. Let's examine the more urgent of them. And since you analysts have more than a casual interest in investment and earnings factors, I will emphasize action affecting these key areas.

When we consider the relative success of the different carriers, as I have indicated, we look at trends in the traffic volume each handles. Yet this is only the end-product of business rivalry. Success in competing might just as readily be expressed in terms of success in attracting investment capital. For here, in acquiring the means to expand and modernize, to promote operating economy and improve services, lie the real origins of the final standings.

In competing for investment capital, railroads, of course, come up against not only all other carriers but also against all other businesses. And in this day of accelerating emphasis on new product development, on automation and plant expansion, competition in the investment marketplace has never been so fierce. Now what happens in this situation to the industry whose average postwar rate of return on net investment is little more than 3 per cent? You experts know the answer to that one.

So the railroads, in competing in the area that means everything to their future, are squarely behind an 8-ball. Other carriers can count on tremendous public investment in at least their roadway and other basic facilities. They generally need worry only about raising capital for motive power and other equipment and servicing facilities.

But the railroads must scrape up capital funds and build from the ground up. For example, of the $14 billion invested in new railroad plant since the end of World War II, about one dollar in three went for roadway and structures. And while railroads in these years were investing this private money in modernization and better service, the federal government alone was spending a whopping $17 billion on behalf of competitive transportation.

Those changes in shares of traffic handled by various carriers which I cited earlier are the result. **I will state flatly that the outsized gains registered by the competition would never have taken place without this massive intervention by government.**

I do not see how any private business can continue to match private capital against public capital. I don't believe the power of a depressed business to attract private investment can possibly match the power of tax authorities to raise and pour funds into competitive facilities.

Perhaps the day is past when we might have hoped to see such spending leveled off. But this does not mean that the people need countenance the promotion of commercial interests at public expense without demanding their paying back user fees commensurate with the costs. **Truly adequate user charges are long overdue. They alone can stop policies of robbing Peter to pay Paul. They alone can spike artificial and uneconomic expansion of certain carriers at the expense of the nation's great foundation carrier.**

Equally important, government must also take a new look at tax policies relating to capital investment. If railroads are more nearly to hold their own on the expansion and modernization front, they must have more realistic tax treatment. As you may know, the cost of new airplanes may be depreciated over a five-year period, while heavy trucks and intercity busses are written off in eight and seven years, respectively. Railroad depreciation schedules, on the other hand, reflect average lives of upwards of 40 years, with the result that we recover in depreciation accruals well under three per cent of investment funds a year.

Such unrealistic depreciation provides funds that are hopelessly inadequate for investment demands in an era of continuous inflation of prices. When we buy a freight car today to replace one that 20 years ago cost $2,500, for example, we find the price has gone up to about $8,500. And to obtain that difference from net income under today's corporate tax rates, a railroad must earn, before taxes, $12,500.

The realistic remedy is to allow railroads to recover capital costs in a much shorter period of time. We are urging Congress, therefore, to ascribe a 15-year maximum depreciable life to rolling stock and a 20-year maximum life to other property.

Another tax proposal that demands early attention is tailored not only to stimulate greater capital outlays but also to level out the peaks and valleys of railroad investment and to cushion the devastating impact of wide purchasing fluctuations on the railroad supply industry and its employees. We have called on Congress to allow railroads to set up construction reserve funds out of their own income. Taxes on these would be deferred if spent within five years for new facilities.

Had such a program been in effect prior to last year, I doubt if we would have witnessed the sharp fall—the cutting in half—of rail capital investment from the $1.4 billion spent in 1957. Mass unemployment might not have been experienced among railroad equipment manufacturers —and perhaps the economic recession would have been far less severe for the whole country.

I believe railroads should invest in new and modern plant and equipment at no less than the 1957 level for as far ahead as it is possible to see. This means that we should spend at least $14 billion in the next decade for the new plant that alone can give America the kind of rail service it deserves.

We frankly seek your help in shaping tax policies so as to encourage this greater railroad investment. Because of the railroads' extreme importance to national security and because of the discriminatory nature of over-all transportation policies which hit them so hard, special consideration of the railroads' problem would seem to be warranted in this respect.

Yet I am convinced that Washington must also revise tax policies to encourage greater investment throughout the economy. National economic policies have developed a bias toward consuming or using up goods and resources. However, the nation's future economic strength lies in channeling as much as possible of current effort into the creation of new resources and new productive plant.

We need no clearer indication of the necessity of this than to note how Russia is straining every muscle to do the same. Tax policies must stop treating the man who saves as the underdog of the economy. It is a simple truism that we cannot have our economic cake and eat it, too. If tax policies stimulating investment and expansion are not forthcoming and if we continue emphasizing spending and consumption, we may one day find little but crumbs remaining.

While laws and administrative practices are being geared up to these policy changes, we in the railroad industry will be doing our utmost to solve the major internal problem that plagues us. I refer particularly to featherbedding work practices that spring from antiquated work rules and which bleed the industry—and ultimately the public—of more than $500 million a year in unnecessary employment expenses. In the interest of brevity, I will not spell out this problem and its impact, though I invite any of you who are interested to request more information on this subject. I will see that you get it.

The major damage inflicted by the old work rules that concerns us today is their drag-effect on the railroads' ability to improve plant and streamline services. This takes two forms. First is the obvious blow struck at earnings and investment capabilities by practices that add so markedly to internal costs. And second are the formidable barriers erected by the old rules against introducing basic changes in plant and methods of operating. In fact, this problem of featherbedding may be viewed as a reluctance, if not refusal, by a key segment of the labor movement to accept technological change and improvement.

Yet the record shows clearly that labor's resistance to change and its stubborn defense of obsolete work standards react not only against the industry and the railroad-using public but against railroad workers themselves. The lines' lag in attracting traffic and the long-range reductions in our working forces bear mute testimony to the impact of make-work. **Featherbedding is truly a boomerang which unerringly strikes back at those who practice it.** This is why, with the moratorium on work rules changes expiring on October 31, we are urging rail labor leaders to cooperate in taking a new approach to the problem. Specifically we are asking them to join with us in seeking the appointment by the President of a non-partisan commission to study the impact of these rules on the general economy.

In their own self-interest as well as in the public interest, I feel labor leaders should join management in streamlining work rules and opening the way to lower unit operating costs, thereby making railroads more competitive in winning and expanding business, and creating new job opportunities. We still hope to see labor take this course.

Meanwhile, railroads are also going all-out to tailor freight rates to specific shipper needs in an effort to win traffic. One of the most important sections of the Transportation Act of 1958 was one establishing a new rate-making rule, which the Interstate Commerce Commission is to apply in competitive price situations. The railroads, backed by shipper groups, believe this new provision was intended to give them greater freedom to reduce freight rates, and was certainly intended to prevent the I.C.C. from barring reductions merely to protect the traffic of competing carriers.

I cannot overstress the importance that lies in such pricing freedom. Railroads must be allowed to make full use of their natural economic ability to move great quantities of freight at diminishing unit costs. Only thus can the public get the lowest service it is possible to give.

In recent months, railroads have proposed a wide range of rate adjustments in an effort to capture more business. Many of these new rates are volume or incentive prices and encourage heavier loading in cars or shipments in multiple car and trainload quantities.

Others are experiments with containerized rates, based on weight or bulk and distance moved rather than on the kind of lading inside. These "all freight" rates are a determined effort to recover less-than-carload or small shipments.

A number of freight rate adjustments

concern piggyback operations—an area of rail-truck cooperation that could hold enormous promise for the future.

Agreed charges are also being investigated. Already in effect in Canada, this approach would offer shippers a negotiated low rate in exchange for their agreement to move a certain share of their total traffic by rail.

Railroads have extensive studies underway and will propose still other significant rate changes and reductions, undoubtedly at an accelerating pace as our research discloses more about costs and marketing relationships. But the real key to how much we can do in this area, and to how much the public can benefit from such actions, lies in a fair interpretation of the new rate-making rule of the Transportation Act of 1958.

No effective substitute has yet been found to replace price competition in deciding what companies should get a customer's business. Certainly no concept of regulation by government can hope to allocate traffic among different carriers with equal efficiency or justice. As a matter of fact, the job faced by government regulators has never been so difficult. The great growth in recent years of private and unregulated transportation threatens the whole structure of public regulation. While practically all railroad freight is subject to economic or rate control, only about a third of intercity freight by motor carrier and less than a tenth of traffic on inland waterways is now so regulated.

This development of huge segments of "free" carriage directly competing with regulated segments may mean that government has lost control over transportation supply and pricing—that the only way out is greater freedom for those carriers now under the government's tight rein. Perhaps we should hark back in this respect to a basic premise of the Republic, which is simply that, like government itself, that regulation is best which regulates least.

I feel we are moving into an era of widening opportunities for railroads—of a widening way to a better future. How far we will go will necessarily depend heavily on people like you who understand the complex problems facing transportation and who can spearhead sound remedial action. Railroadmen know that real progress must also start at home, and I want to state emphatically that we are determined to win a better deal for this industry that means so much to America.

As I said in a speech in St. Louis three months ago, we are sick and tired of being the problem child of the American economy. **We are going to do everything in our power to break out of the trap of old laws and old work standards. The nation is moving into what could prove the most glorious golden age man has ever known. Railroads are going to fight as never before to be right in the vanguard of that movement.**

ASSOCIATION OF AMERICAN RAILROADS

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