



THE TRAINS INTERVIEW

Larry Gross

Analyst considers intermodal after the pandemic

▲ A trio of BNSF C44-9Ws in "Heritage 2" paint leads a west-bound stack train past the since-removed Santa Fe searchlight signal at Verona, Ill., on June 20, 2017. John Crisanti

ANALYST LARRY GROSS,

president of Gross Transportation Consulting, publishes the monthly "Intermodal in Depth" report that analyzes international and domestic intermodal volume trends. He is a frequent speaker at transportation conferences. Prior to starting his consulting practice, Gross had a long career in intermodal equipment development and sales, most notably the Road-Railer intermodal system. TRAINS chatted with Gross about the future of intermodal.

Q Intermodal has been the rail industry's growth engine for a long time. But growth had slowed and then stopped even



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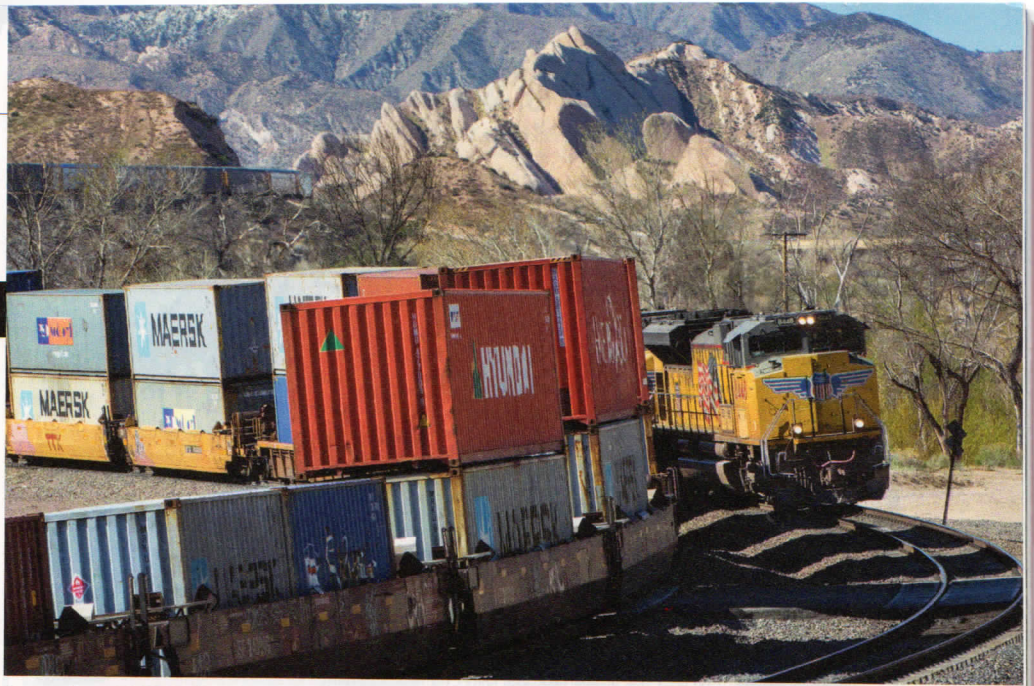
before the pandemic hit. Why?

A We have to keep in mind that intermodal is really two separate markets. There is international (i.e., import/export) and domestic — and they are driven by different economic factors. The first decade of the 2000s was all about international, as imports from China grew quickly, driving rapid growth in inland-point intermodal movement of ISO containers. Then there were labor problems at West Coast ports, and shippers adopted a "four corners" strategy and began using ports on the East Coast, Gulf Coast, and Canadian West Coast. And that began

a decline in international intermodal volume that then accelerated during the Great Recession.

In the meantime, domestic intermodal didn't do much between 2000 and the Great Recession. Sometimes it grew faster than truck, sometimes it didn't. But after the Great Recession, it came out faster than truck, ushering in the golden era of domestic intermodal growth. International intermodal grew out of the Great Recession, too. The industry went through an era of adding services, adding secondary terminals and new routes and corridors. There really was a growth orientation and volume responded. Intermodal grew faster than truck right up until 2016.

And then things changed.



An eastbound BNSF intermodal train meets a westbound Union Pacific train led by SD70ACE No. 8448 at Cajon, Calif., on Feb. 11, 2020. Precision Scheduled Railroading has seen railroads sacrifice volume to maintain operating ratio, analyst Larry Gross says. Two photos, Elrond Lawrence

Starting in 2016, growth leveled off. Why did this happen? The railroad focus changed from growth to profitability. This is all part of the Precision Scheduled Railroading mantra. PSR looks for simplification, streamlined operations, and profit margins. Trucking rates are pretty volatile with supply and demand. The railroads are not willing to follow trucking rates to any great extent because it will affect their operating ratio, and the operating ratio is important in today's scheme of things. The railroads appear to be more than willing to sacrifice volume in order to maintain margin. And as a result, the stuff that doesn't fit has been going back to highway, and the share numbers show that. The strategy has been highly successful from a financial perspective. It's just not a growth strategy.

Q How is intermodal volume likely to rebound as the economy recovers from pandemic-related challenges?

A It's impossible to predict what the recovery is going to look like. I don't see any reason why intermodal won't follow what's going on with freight in general. Intermodal is the tail of the dog. Trucking is the main story, and intermodal follows along and goes up or down faster or slower depending on whether railroads are inclined to grow share or not. I'm not forecasting an increase in share, which is different from what happened after the Great Recession. When you have a recession, intermodal is well positioned to gain share because it's a more value-oriented method of moving freight. But it's all about price. People don't ship intermodal unless it's cheaper because it's not better. It's not as flexible, not as fast, not as responsive as truck. That's the domestic piece. The international piece is

determined by import container volume. I think the era of international intermodal growing faster than the overall economy is over, and that's a fundamental change. The other piece of the puzzle not working in the railroads' favor is international containers moving away from the West Coast toward the East Coast. When stuff lands on the East Coast, it's not moving as far inland, so it's not as intermodal friendly. A higher percentage moves by highway.

Q What can railroads do to profitably grow their intermodal volumes and take market share from the highway?

A It all depends on what your definition of profitable is. There are many things that could be done. Today, only the most intermodal-friendly freight will make it to the rails, because it has to be ideally situated to generate the kind of margins the railroads are looking for. What could they do to grow? They need a robust system of connecting secondary locations that goes beyond a point-to-point, high-volume system, which is how I would describe the intermodal network today. Running large

trains to large locations with few work events in between runs counter to the ongoing dispersal of port traffic and the dispersal of domestic traffic related to e-commerce. To grow, railroads will need to get containers as close to their origins and destinations as possible. Drayage, the local truck movement to and from the terminal, is expensive. They need more terminals and a network to connect them that provides a highly reliable level of service. More frequent service would help, too.

Q Would a transcontinental merger of U.S. systems help intermodal?

A It would. The reason it would help is if you look at intermodal markets by mileage, the biggest is the 2,000 to 2,500 length of haul, which is the West Coast to the Midwest. The second biggest, 750-1,000 miles, is the East Coast to the Midwest. There is a big old donut hole in the middle. There's no reason from an economic standpoint that share is lower in the 1,000-2,000 range than it is from 750-1,000 miles. The reason is because of the interchange. Most of those medium-range hauls stretch beyond one railroad and involve two railroads. Think Minneapolis to Atlanta, for example. When you get to the interchange, say Chicago, but anywhere up and down the Mississippi, often one side or the other of the move is too short for a railroad to be interested. And a crosstown rubber-tire move in Chicago is expensive. If you had a coast-to-coast railroad, that would blow up the artificial barrier, and then there's a giant opportunity. But to be clear, although there would be intermodal benefits, I'm not advocating a merger. It would open a regulatory door and you don't know what's on the other side. — Bill Stephens



A Citirail lease unit is on the point as an eastbound BNSF Railway stack train hurries through Bagdad, Calif., in November 2016. The West Coast-Midwest haul is the longest rail intermodal move, but railroads don't compete well in the 1,000-to-2,000-mile range.

