

**DEFENSE
AND THE
RAILROAD
PROBLEM**

J. M. SYMES

**VICE PRESIDENT—OPERATION
THE PENNSYLVANIA RAILROAD COMPANY**



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Defense and the Railroad Problem

By J. M. SYMES

Vice President—Operation
The Pennsylvania Railroad Company

THE industrial might of America—upon which we place our chief reliance to win a war if need be—or preferably, to secure a peace which may be maintained by the caution or fear of our enemies, is based on our capacity to produce and deliver the terrible instruments of modern war to the doorsteps of an enemy in quantities unmatched by any other nation.

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Other nations have more men. Other nations know how to make atomic bombs, jet planes, homing rockets and modern warfare weapons of that sort. But we can manufacture and transport these weapons in unmatched volume, and we can bring them to bear in concentrations that far exceed the ability of the slave-labor countries.

Upon that fact we place our hope for continued existence in a world which has seen many countries fall under dictatorship, where the power of war or peace has been placed in the hands of a few men.

Power, concentrated in the hands of a few men, is always threatening. Power, in the hands of the people, can be trusted in the long run to work for the good of the greatest number.

The Source of America's Strength

This industrial might of which we are justly proud is like a protective tent over our civilization, supported by the staunch tent poles of private enterprise. Privately owned and managed farms, mines, factories, power plants, and railroads, and other transportation agencies, each represent the accumulated and treasured savings of many individuals.

The owners and managers of these private enterprises daily demonstrate a continually improving efficiency. That is

because thousands of inventive minds in many fields are spurred to extra effort by the rivalries of competition and the incentive rewards for individual success.

Others have warned of the dangers we face if the termites of Socialism are allowed to eat away the tent poles that uphold our industrial civilization. I shall not dwell on that long-range point now. I do wish to call your attention to an immediate danger confronting one important segment of our economy and threatening the success of our defense program.

How Railroads Serve

First, a few figures, which will not be too burdensome; allow us to review the place of railroads in our overall economy.

The Class I railroads in the United States, of which there are 131, employ a million and a quarter men and women. They operate 225,000 miles of railroad and 397,000 miles of track; enough to circle the globe sixteen times. They operate 40,500 locomotives, about 2 million freight cars, and 37,000 passenger cars. This equipment, standing end to end, would extend across the continent and two-thirds of the way back again.

Last year the railroads handled 589 billion-ton-miles of freight at an average cost to shippers of one and a third cents

per ton mile. They provided passengers with the nation's safest, most comfortable and dependable type of transportation at an average cost to the passenger of two and a half cents per mile of travel.

For these services in 1950, the railroads received—in round figures—a total revenue from all operations, of nine and a half billion dollars. Railroad operating expenses last year were seven billion dollars. They paid one billion, two hundred million dollars in taxes. They had a net income of 784 million dollars. The net income in dollars seems large but, when you consider the 25 billion dollar net property investment of these carriers, they actually earned last year less than a 4% return on investment.

Railroad Improvement

Capital expenditures for road and equipment last year amounted to one billion 65 million dollars. This kind of improvement has been a continuing program every year since the end of World War II and should continue at an even larger rate. The capital expenditures of the railroads last year amounted to 134 per cent of their gross net income without any provisions for dividends. Of course, there was some depreciation money available for improvements, but that was entirely inadequate considering that the price of replacements is more

than double—and in many instances more than triple—the original cost of the facilities being replaced.

I am sure nearly everyone will agree that the figures cited are somewhat staggering. They certainly indicate that the railroads are one of our Nation's most important assets.

There is ample traffic available to move at rates which will allow the railroads to earn the income they must have if they are to continue to improve their efficiency and service. This efficiency has already been improved more than is generally realized.

Demonstrated Efficiency

If we compare railroad efficiency with other forms of transportation we find some challenging and startling figures: To equal one railroad-man working one day moving freight with railroad equipment, it takes 28 men to move the *same* amount of freight the *same* distance in trucks. On fuel efficiency, trucks use three times as much fuel per ton mile of pay-load as railroads—airplanes use thirty times as much.

The *real* efficiency of the rail method of transportation is so great that its competitive advantages are certain to increase as America's standard of living goes up and the value of an hour's work increases. Contrary to the belief of many,

the railroads are not losing their "place in the sun" as the nation's principal transportation agency. A count of the traffic now being handled—both freight and passenger—on a unit or on a dollar basis, shows that the railroads did more business in 1950 than they did in the boom year of 1929.

The figures I have used have been for the purpose of indicating what the railroads are—what they do—why healthy railroads are important to our overall economy in time of peace and why they are essential to our national defense or war protection. These facts will remain true whether railroads are allowed to continue under the free enterprise system which we all cherish so much, or are operated by the Government through taxation.

Obstacles to Progress

The biggest problem confronting the railroad industry during the past several years—and still unsolved—is the failure of those regulating the pricing of the industry to recognize that, when inflation moves in on the costs of conducting business, as it has since World War II, it must also move in on the pricing of the product sold. We sell only one product—transportation—moving people and goods to where they want to go. Why we are denied the right to increase charges, in keeping with increased costs, is dif-

ficult to understand.

Freight rates represent a far lower proportion of the cost of commodities today than they did during the years prior to World War II. Despite this, the Interstate Commerce Commission has reduced, or delayed inordinately, practically every request the railroads have made during the last twenty years for a general adjustment of freight rates. The recent decision of the Commission to cut the rate application of the railroads in half means that the railroads are utterly unable to meet increased costs. Yet, the ability of the railroads to meet increased costs is absolutely necessary to place the railroad industry in position to give our country the improved equipment and service called for by the men in charge of defense mobilization of the nation.

Millions of Dollars Lost

Here is what we are up against. Take the Pennsylvania Railroad for example. The Interstate Commerce Commission authorized freight rates that will increase our gross revenues in the calendar year 1951 by 27 million dollars. The increased cost of wages and materials during this same year will amount to 85 million dollars. This means we are 58 million dollars short this year from obtaining relief on rates to offset increased costs.

Extending this situation to a full year—increased rates would amount to 59 million dollars, and increased wages and materials to 96 million dollars—still 37 million dollars short in offsetting increased costs.

The railroads are told overnight, or even to a retroactive date, by government agencies, that our wage rates have been increased. We are told overnight that our costs of materials have gone up because equipment manufacturers must protect their businesses against inflation by putting escalator clauses in the purchase contracts we make. But the railroads are told by the Interstate Commerce Commission—many months after *our* costs have gone up—that we can't have what we are seeking in the way of increased pricing—because, as nearly as I can understand the reasoning, "We just won't authorize it."

Too Little Too Late

Let me offer an example of what the lag in procedure for rate relief means: In the years following World War II there have been a number of applications for increased rates, partially to offset inflationary costs. But on the average, a year elapsed from the time the applications were filed until relief was actually granted.

During those lags, those waiting periods, we were deprived of nearly 400 million dollars in revenue on the Pennsylvania Railroad alone; revenue so sorely needed to improve, maintain and expand our plant to meet the challenge of the future.

It is only natural, from what I have said, that two questions will be asked: Why is the industry being shackled in the manner I have described? And what can be done about it?

I should like to declare tonight that the nation's defense effort and the economic soundness of all types of business will be endangered unless the Interstate Commerce Commission changes the "too little and too late" practice it has followed in regulating railroad rates and fares. If the Commission does not change such practices of its own accord, Congress should amend the Interstate Commerce Act.

Sixty-four years ago when the Interstate Commerce Act was first written, it was a good law for our country, that then, except for steel rails, was ankle deep in mud. At that time the railroads were more or less of a monopoly in the transportation field. Today the railroads compete for every ton of freight and every passenger they carry, yet they are regulated under a statute that has not been

adequately amended to meet modern conditions.

Railroad Act Out of Date

The railroads required regulation in the public interest when the Act was written sixty-four years ago. And as then administered it no doubt served the needed purpose of the time. However, during the past fifty years there has been a complete change in the transportation facilities of this country.

We now find the nation laced with super-highways, checker-boarded with airports, dredged for thousands of miles of inland waterways, and criss-crossed by 150,000 miles of pipelines. The railroads no longer need regulation over rates insofar as "ceilings" are concerned. Competition now takes care of that.

Unfortunately, however, it is apparent that regulatory authorities give much weight in their decisions as to whether increased rates might drive rail traffic to competitive forms of transportation and thus adversely affect net income to a greater extent than increased rates might improve net income. I say that should not now be a consideration of regulatory authorities.

If the railroads require additional net income—and the records, not even disputed by regulatory authorities, clearly indicate that they do—they should be

permitted to bring it about in a business-like way. If railroad management does not know how to price its product in a competitive market, such as we now have in the transportation field, then there should be new management. But we should not now delegate that very important function of management to those not held directly responsible for their actions.

Regulation vs. Over-Regulation

Please don't misunderstand me—I am not advocating that the railroads be released from all regulation—but I am suggesting that they be relieved from the shackles of over-regulation, now taking place under procedures of a Commerce Act written two generations ago and, as stated, not adequately amended since.

Certainly I would want regulation to see that the industry is fully protected with respect to area and other established differentials—essential to protect the free flow of commerce in our country. I would want regulation for abandonments of line, consolidations of properties, certain financial transactions, and things of that sort, designed to maintain a well-run system of railroads for the nation and to protect the public interest fully.

I advocate regulation designed to protect the public interest under transportation conditions as they now exist. It

may be that the Interstate Commerce Act actually does not require too much change—maybe it only needs proper interpretation through administration designed to meet present-day conditions, which after all was its original intent.

The Subsidy Evil

The next biggest problem facing the industry is that of subsidy. The inherent economic advantage of rail transportation is being submerged by the subsidy of other forms of transportation, particularly the highways and airways.

Without question, all modern transportation agencies have a proper field in the economy of our country, and each and every one has certain inherent advantages over the others. However, these inherent advantages should not be pushed aside by subsidy. When such subsidy enables one transportation agency to take traffic from another that is not subsidized, you destroy the healthy and natural competition in transportation which alone can determine which service best suits the needs of every community for every commodity.

All we ask—is equality of treatment—and from there on it is up to each transportation agency to demonstrate its ability to survive. A transportation agency that can produce the *demand*ed service of the shipper, at the lowest *full* costs, is the one that should move the traffic.

Rails Essential to Defense

All of this fits into my topic, "Defense and the Railroad Problem." The problem is immediate.

The railroads proved during World War II that they were the only transportation agency equipped to handle the war traffic. They are just as essential now to the defense program. They will be even more essential in another war.

Without adequate railroad transportation there could not be adequate defense, or war production in this country. That is a fact not disputed by anyone.

If the railroads are prevented from procuring adequate earnings to improve and expand their facilities, and outside capital is not obtainable, which it certainly will not be without proper earnings, where is the money coming from to do the things that need be done?

Without a continuous rail flow of raw materials to our industrial assembly lines and adequate rail transportation from one plant to the next, millions of workers would soon be idle and America's entire mobilization program would be snarled in hopeless confusion. If the railroad plant is allowed to deteriorate, and there is not sufficient equipment to move the traffic, it would be a most serious weakness in our defense.

The Defense Production Act

Over a year ago Congress passed the "Defense Production Act of 1950." The purpose of this Act was to strengthen this country militarily and economically in order to enable it to carry out its policy, as stated in the Act, "to oppose acts of aggression and to promote peace," and, for this purpose, "to develop and maintain whatever military and economic strength is found to be necessary to carry out this purpose."

To achieve this objective, the Act expressly states that there must be "expansion of productive facilities beyond the levels needed to meet the civilian demand." Expansion of productive facilities, in a free enterprise economy like ours, necessarily means increased investment by private capital in the creation of additional productive facilities. This in turn means that private capital must be allowed to earn enough to provide additional funds for such increased investment.

Expanding Railroad Facilities

With this policy of encouraging expansion of productive facilities in mind, many agencies of the Federal Government—the National Security Resources Board, the Defense Production Administration, the Defense Transport Administration, and the Interstate Commerce

Commission itself—have been calling upon the railroads of the country to acquire additional freight cars and locomotives, and otherwise build up the railroad plant. And the railroads, on their own initiative as well as in response to these calls, have undertaken to build up their plant by the addition of large quantities of equipment and other essential facilities.

But the acquisition of these and other additional facilities so vitally needed for the expanded transportation essential to the country's defense effort requires the investment by the railroads of large amounts of additional capital. This capital can come only from earnings—or from loans, which require earnings to carry them and pay them off.

One of the main objectives of the railroads in asking for the increase proposed in their recent general rate case, was to enable them to provide for the plant expansion and improvement called for by the Defense Production Act.

Surely, in these circumstances, it should be the duty of Government, which is charged with the administration of that Act and the achievement of its purposes, to aid the railroads in reaching a rate level which would permit sound financing of adequate plant expansion. But the fact is, that the efforts of many men in

many government agencies have been exerted in precisely the opposite direction. Several important Departments of Government actively and vigorously oppose the rate relief sought by the railroads. And the action of the Commission itself, which has held the railroads down to an inadequate rate level that does not produce a fair return on their investment, can only have the effect of preventing the railroads from achieving that degree of financial soundness which would permit plant expansion and improvement to the extent called for by the national welfare and contemplated in the Defense Production Act. Does all of this make sense? I don't think so.

Railroad Progress Depends on Earnings

Nearly every banker realizes where the railroads stand at the moment in financial circles—where our securities stand from an investment and speculative standpoint.

I have read recently a number of reports dealing with this situation, prepared by financial institutions and pertaining more specifically to the railroads in the East. These reports are not optimistic as to the future. In fact, many such reports recommend disposal of railroad securities for investment purposes—pointing out that in these boom times the securities of many other industries appear more favorable. But these should be

prosperous times for railroads too. We are operating at capacity or near-capacity with the equipment available. We should be earning the money needed to buy new trains instead of borrowing it. The situation, as you know, is not healthy even from the standpoint of borrowing money. The railroads need larger earnings now—need them to improve their properties and carry on a more efficient transportation service than ever before—so essential to the economy and defense of the country.

The Public Interest

It is not in the public interest to deprive the railroads of the right to adequate earnings on their investment—to earn enough to pay their owners an adequate return—to earn enough to pay for the improvement of the property—to earn enough to attract new outside capital. If we are not permitted to do this, and we are not, principally because of the conditions I have cited, then we cannot survive under the free enterprise system.

The railroad industry is a substantial part of the more than 100 billion dollars of private and government funds invested in transportation of all kinds in this country, representing one-fifth of the nation's productive capital assets. Whatever happens to these vast public services in the critical years ahead, will shape the

destiny of America for generations to come. Neither agriculture, industry nor finance can prosper for long within the framework of the enterprise system, if transportation is permitted to drift into Government ownership.

The great need today is for the railroads and industry, and finance and others, to coordinate their efforts to keep enterprise alive and healthy in all segments of our economy, and thereby to demonstrate that no socialistic bureaucracy can compete in benefits to the individual citizen with economic freedom which is the keystone of all liberty.

I solicit and appeal for the wholehearted support of everyone in furthering such a program.