CSX NORTH AMERICA

A marriage under scrutiny

In his first six months as President & CEO of CSX, E Hunter Harrison has moved swiftly to implement his Precision Scheduled Railroading concept, generating mixed reactions. David Lustig investigates.

CSX has been in the news a lot lately. Mostly, it has been about new President & CEO E Hunter Harrison taking the helm and changing the course of the railroad using his concept of efficient and profitable railroading. As he had done previously as CEO of Illinois Central, Canadian National and Canadian Pacific, he is making waves. Lots of them.

Nominated by activist investor shareholders and confirmed in post on March 6 (RG 4.17 p62), Harrison immediately began implementing the Precision Scheduled Railroading concept which he had developed and applied on the other railroads he led. His aim is to transform CSX into a leaner operation, running fewer, longer and reorganised freight trains, offering a new style of ‘co-ordinated service’, with an eye solidly fixed on the bottom line.

Already, many of CSX’s hump yards have been closed or converted to flat shunting, thousands of jobs have been eliminated, and hundreds of diesel locomotives have been taken out of service. Thousands of freight wagons are also now considered surplus to requirements.

Announcing its second quarter results on July 18, CSX reported net earnings of $510m and an operating ratio of 67·4. Revenue was up 8% compared to the same period last year, with growth across nearly all markets, ‘primarily driven by coal-related gains, strength in core pricing and volume across the other markets’. Efficiency savings of $90m had been achieved, offset by a restructuring charge of $122m.

STB intervenes

But many customers are not pleased by the changes, and some are just plain angry. So are the unions. Faced with a growing raft of concerns raised by different parties, the Surface Transportation Board entered the debate with a letter to Harrison dated July 27.

In its letter, STB ‘expressed growing concerns about the service problems resulting from ongoing operating changes underway at CSX Transportation Inc’. The board pointed out that it had received a number of complaints from shippers, expressing a range of concerns including a marked deterioration of service. It cited unpredictable transit times, freight wagons sitting in yards for days, switching services becoming inconsistent and unreliable, and ‘circuitous and inefficient’ car routings. In addition, STB felt that CSX customer service personnel had been unable to provide meaningful assistance.

Another customer concern was that CSX had been initiating changes to its operating plan without sufficient lead time and co-ordination efforts that would have allowed them to adjust their individual production schedules and supply chain operations to the revised service pattern.

STB followed up with a second letter on August 14, responding to a telephone conversation between Harrison and Acting Chairman Ann Begeman. Pointing out that ‘it is not apparent to the Board and interested stakeholders that service is improving’, STB instructed CSX to submit weekly performance data. CSX was also asked to provide a detailed schedule for the remaining implementation of its new operating plan, setting out ‘key action items and milestones’ for the rest of this year.

Photo: Scott Hartley
Precision Scheduled Railroading

While PSR may be new to CSX and its customers, it is not an untried concept, and its previous implementations have certainly driven improved financial results for the railroads that have adopted it.

According to CSX, PSR consists of a combination of service excellence, controlling costs, optimising asset utilisation, operating safely and valuing and developing employees. This has been translated to mean balancing traffic flows, running fewer longer trains to improve crew and locomotive productivity, and reducing the number of times a vehicle is shunted en route, helping to minimise vehicle dwell time in yards. More freight is moved in so-called ‘general purpose trains’, rather than dedicated flows in order to help balance flows, running fewer longer trains to improve crew and locomotive productivity, and reducing the number of times a vehicle is shunted en route, helping to drive down the operating ratio dramatically.

What’s going on?

First, a few facts. Annual revenue at CSX had been declining before Harrison arrived, with little forecast of a dramatic upswing. Its leadership team of previously very competent managers had been struggling to turn the railroad around. Despite all the statistics in the financial statements and annual reports, coal had been the major staple of CSX’s freight operations and had always kept the railroad profitable. But US coal demand has been falling rapidly in recent years (RG 8.16 p33), and while there has been a slight recovery in recent months there is a high probability that coal traffic will never return to the levels seen in recent decades.

Lost in the uproar about what is going on, nobody at CSX, including Harrison’s own leadership team, has suggested that the implementation of PSR was going to be without challenges. Perhaps the collective memories of initial disruption at IC, CN, and CP mellowed as the new operating patterns settled in. Perhaps it wasn’t as bad. Or maybe it was and the market just got used to it.

Throw all the brickbats you might want to at Harrison, his decades-long career has seen consistent success in terms of restructuring operations, cutting out any fat, and slimming down the railroad, helping to drive down the operating ratio dramatically.

LETTER

‘We value your business’

July 31 2017

To our valued customer,

Over the past four months, CSX has been undergoing a tremendous amount of change, including an operational transformation that will ultimately result in better service to our customers. We’re not at the finish line yet, but I’m personally writing you today to reaffirm our commitment to working with you individually to ensure you receive the support you require to meet your business needs.

I think we can agree that more-reliable service and improved asset utilisation is a win-win for your business and ours. It is with these intentions that we have focused our efforts — moving our customers’ freight consistently, reliably and cost efficiently.

The pace of change at CSX has been extremely rapid, and while most people at the company have embraced the new plan, unfortunately, a few have pushed back and continue to do so. This resistance to change has resulted in some service disruptions. To those customers that have experienced such issues, we sincerely apologise. As we move forward, we will continue to address these internal personnel matters and our teams have recommitted themselves to reaching out to those affected to work through any service issues and resolve them as quickly as possible.

Throughout our transformation, one thing that has remained constant is our dedication to our customers and the great effort we put forth to deliver the service you expect from CSX. Our operating and sales and marketing teams are collaborating closely to better ensure you are prepared for and work through any planned changes that may occur. I will remain engaged in overseeing our customer service and communications efforts, and appreciate your partnership and willingness to also remain engaged.

We value your business and thank you for the opportunity to be your transportation provider.

Sincerely,

Hunter
A railroad fixer

Ewing Hunter Harrison began his railroad career in 1964, while a student at Memphis State University in Tennessee. Finding work as a carman for the St Louis - San Francisco Railway, he steadily moved up the ranks. After SLSF was absorbed by Burlington Northern, Harrison eventually reached the post of Vice-President for Transportation & Service Design.

In 1989 he moved to Illinois Central, initially as Vice-President & Chief Operating Officer. He became CEO from 1993. Following IC’s acquisition by Canadian National in 1998, he became President & CEO of the combined railroad until retiring in 2009.

Two years later, Harrison teamed up with investor Bill Ackman of Pershing Square Capital Management during a proxy battle with the directors of Canadian Pacific. The challenge was successful and in 2012 Harrison was appointed President & CEO of CPR. After handing the reins over to his protégé Keith Creel, Harrison had been due to retire again in mid-2017. But at the beginning of this year he resigned early from CPR, foregoing a generous benefits package to join ex-Pershing investor Paul Hilal and his Mantle Ridge fund seeking to take control of CSX.

Given his reputation as a ‘railroad fixer’, many investors have expressed confidence in Harrison’s ability to do the same with CSX. The company’s share price rose sharply on suggestions of his involvement, even before he formally took over in March.

CSX isn’t the same

Critics, however, suggest that CSX is not the same as IC, CN or CP, being much more of a ‘network’ and less of a ‘linear’ operation. Its traffic flows are complex, and the railroad has a lot of legacy infrastructure in the eastern coalfields, although it has been steadily developing its intermodal corridors.

To combat complaints, management began blaming some of the early problems on resistance to change within the company. But that explanation seems to have mostly fallen on deaf ears. With complaints increasing, and some customers threatening to move traffic to rival Norfolk Southern where possible, Harrison responded to the STB intervention on July 31, with a letter of apology to all CSX customers (panel). This can be seen as an attempt to quell the unrest and buy more time to achieve his goal of smoothing out and improving CSX service.

Radical change is not unique to rail, of course. It is a fact of life for all industries, not least the energy and chemical sectors. In the transport market, many North American airlines have been through some huge restructurings in recent decades, and while some have prospered, other famous names have vanished. CSX itself is the product of the huge wave of railroad mergers during the 1970s and 1980s, culminating with its acquisition of 42% of Conrail in 1999.

Whether the steps that Harrison is taking to implement PSR at CSX will work remains up in the air, at least in the short term. Investors are split, with many reportedly confident that their CEO is on the right track and just needs more time.

But a number of customers and employees remain unconvinced. They not only expect and demand improved service from CSX, they need it to stay in business. The threat to move to Norfolk Southern only works in some geographic areas, but switching traffic to road is another alternative. If customers opt for that route, there must be concerns that the traffic will never return to rail, no matter how good service becomes.

The answer to whether PSR is the right model to address the challenges that CSX had been facing is far from clear. Only time will tell if this will be Harrison’s finest hour or his ultimate blunder.