ASSOCIATION OF AMERICAN RAILROADS | POLICY & ECONOMICS

Rail Industry Overview

October 2024

Economic Turbulence Strikes Amid Waning Recession Concerns

Since the Federal Reserve's decision to cut interest rates in September, the U.S. economy has been navigating a series of disruptions, ranging from labor strikes and hurricane recovery efforts to rising oil prices driven by an escalating conflict in the Middle East. One key challenge — the port strike along the East and Gulf Coasts — has been resolved, with an agreement between the International Longshoremen's Association and the U.S. Maritime Alliance ensuring wage parity with West Coast workers. However, as operations resume, the lingering impact on supply chains, which handle 25% of U.S. imports and exports, could affect sectors like automotive, aerospace, and consumer goods, especially as the holiday season approaches.

Compounding these challenges, escalating conflict in the Middle East has driven global oil prices higher, placing additional pressure on transportation and manufacturing sectors. If tensions intensify, a dramatic surge in fuel costs could further strain energy-dependent industries.

Simultaneously, Hurricane Helene has left significant economic damage in its wake, with losses estimated between $145 billion and $160 billion, particularly impacting Florida and Georgia. Consumer spending in these regions is declining, and job losses and furloughs are expected in critical sectors such as retail and agriculture. Despite these challenges, economists remain optimistic that the U.S. economy's job growth trajectory, sustained over the past four years, will continue.

Key Takeaways

- **Port Strike Averted, But Delays Loom.** A tentative agreement has ended the three-day port strike that threatened to derail critical supply chains. Although the strike was short-lived, the freight industry is bracing for delays as the backlogs clear.

- **Hurricane Helene and the Middle East Conflict Compound Economic Strain.** Damage from Hurricane Helene and rising fuel prices due to tensions in the Middle East are adding pressure on supply chains, increasing consumer costs, and complicating economic recovery.

- **Mixed Rail Performance in September.** Strong consumer spending has bolstered intermodal rail volumes, driven by a resilient labor market. However, continued stagnation in the manufacturing sector, rising costs and potential supply chain disruptions pose challenges to rail traffic.

- **FRI Signals Growth Amid Uncertainty.** The Freight Rail Index (FRI) rose by 0.4% in September compared to August and 7.3% year-over-year, indicating steady growth in rail activity. However, the full impact of recent port strikes and hurricane recovery efforts remains unclear, creating uncertainty about sustained growth.

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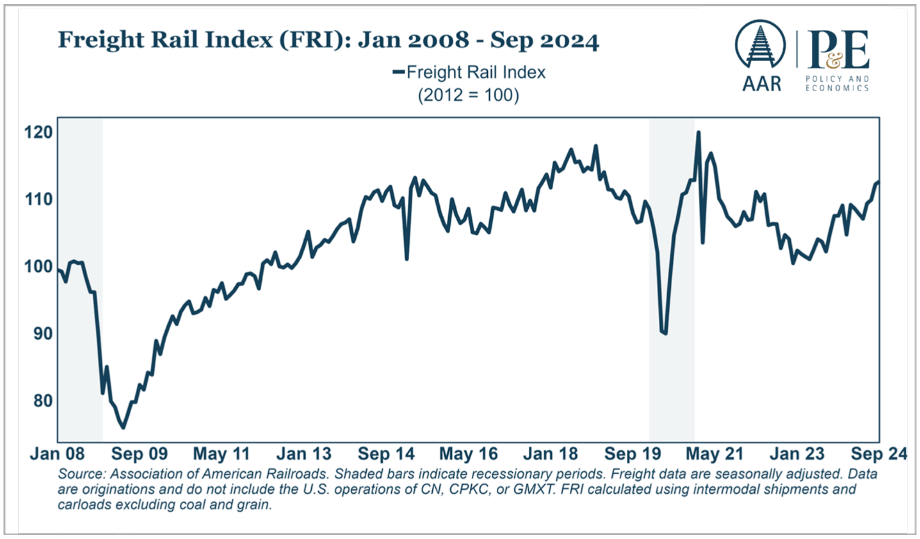
Resilience remains a cornerstone of the freight rail sector as it navigates the aftermath of Hurricane Helene. Operating across a vast outdoor network, railroads are accustomed to and regularly plan for severe weather challenges. Recovery efforts are well underway, with CSX and Norfolk Southern — two major railroads most impacted by the hurricane — making significant progress in clearing debris and repairing infrastructure. However, certain routes remain out of service, and delays are expected. Shortline railroads have also played a key role in restoring network fluidity, highlighting the industry's ability to recover swiftly from disruptions. With the potential for further weather challenges, sustained efforts will be critical in maintaining service continuity.

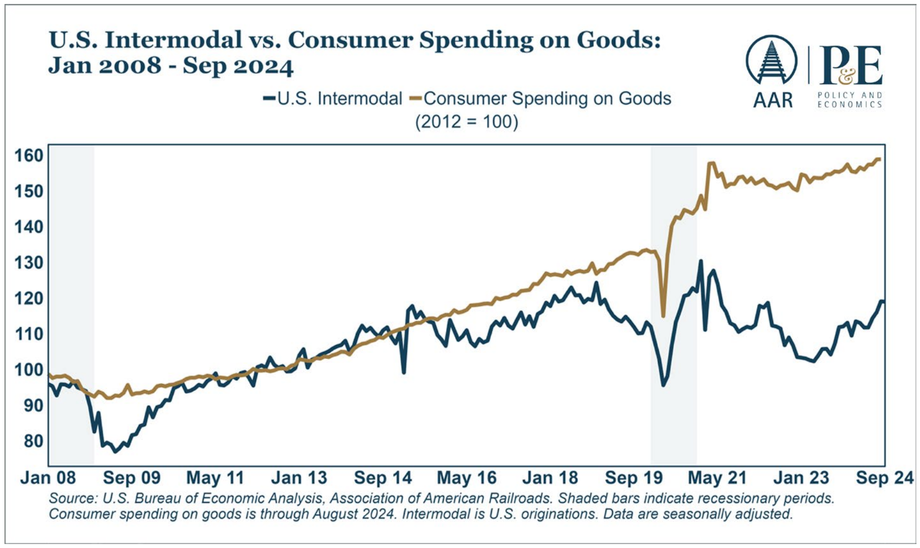
As the economy moves forward, uncertainty remains. While inflationary pressures had been easing, these recent disruptions are reigniting concerns over supply chain bottlenecks and rising costs. Despite these challenges, early indicators show some resilience.



AAR's Freight Rail Index (FRI) for September posted a seasonally adjusted 0.4% increase over August, and a 7.3% rise compared to September 2023. However, the full extent of the impacts from the port strike and hurricane recovery efforts has yet to be fully realized. The coming months will be critical for gauging the broader economic trajectory.

Rail Traffic Trends: Economic Resilience Amid Labor Market Strength and Supply Chain Disruptions

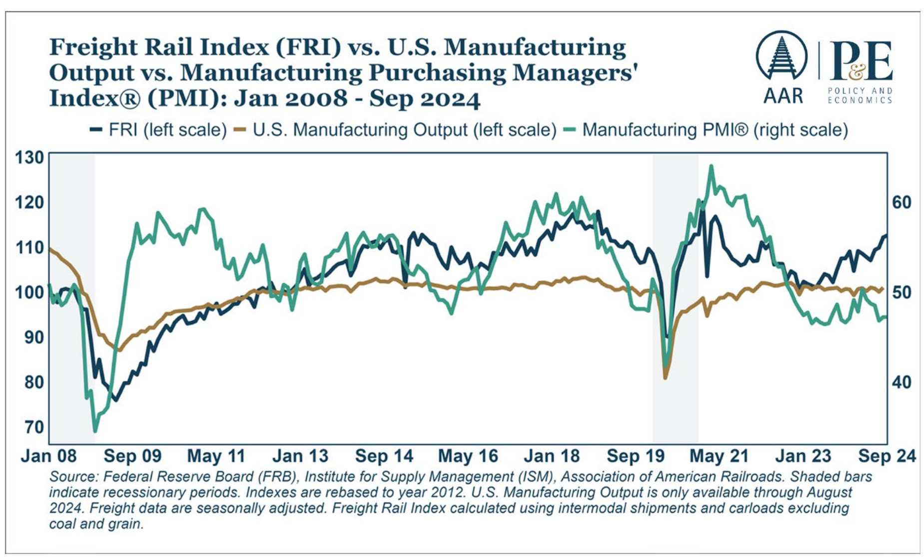
In September 2024, the U.S. economy continued to demonstrate stability, largely supported by a robust labor market. With a preliminary 254,000 jobs added in September and the unemployment rate falling to 4.1% from 4.2%, this strong employment growth should bolster consumer spending. Consumer spending accounts for over two-thirds of U.S. economic activity and remains a vital driver of demand for transportation services, including freight rail. As average real wage gains remain positive, consumers have maintained their spending patterns, with services rising by 0.2% in August. However, spending on goods remained practically flat for the month after adjusting for inflation.



Intermodal rail, which is closely tied to the movement of consumer goods like electronics, household items, and motor vehicles, has benefited from this economic resilience. In September 2024, U.S. railroads originated 1,117,166 intermodal containers and trailers, a 10.7% increase over September 2023.

This makes September the second-highest month for intermodal movements in 2024, averaging 279,292 units per week (August was slightly higher.) The surge in intermodal traffic can be attributed to a combination of strong consumer demand and heightened port activity as industries rush to replenish inventories ahead of the holiday season. However, with the recent East Coast port strikes and the lingering effects of Hurricane Helene, October's rail volumes may face hurdles, potentially impacting the momentum built in September.

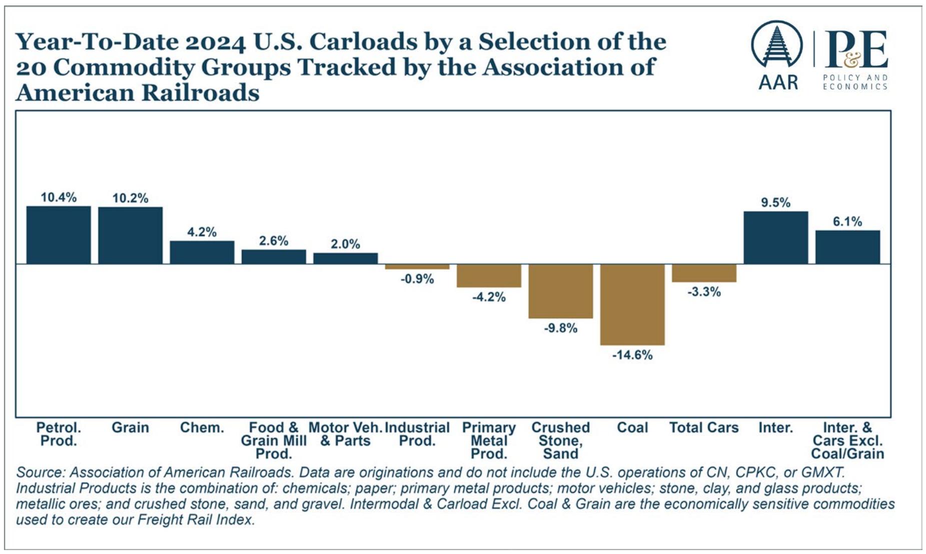
Looking ahead, consumer demand may be challenged by rising energy costs and supply chain disruptions, both of which threaten to increase transportation costs and squeeze household budgets. The uncertainty around consumer demand, especially as the holiday season approaches, could weigh on intermodal volumes, a critical part of the rail industry.



On the manufacturing front, the Manufacturing PMI® in September stood at 47.2%, its 22nd month signaling contraction in the past 23 months. Despite this, the broader U.S. economy remained in expansion, driven primarily by the services sector, which accounts for over 70% of U.S. jobs. However, the contraction in manufacturing, coupled with energy cost pressures and supply chain bottlenecks, poses a risk to sustained rail traffic volumes. Manufacturing, sensitive to disruptions in supply chains, could see further slowdowns if energy prices and logistical issues persist.

Despite the strength in intermodal traffic, total carloads — excluding intermodal — were down slightly in September. Total carloads reached 914,219, down 0.5% compared to the same period in 2023. The decline was mostly evident in commodities like coal, crushed stone and nonmetallic minerals. Coal carloads averaged 62,705 per week in September — the most for any month so far this year — but were still down 8.0% year-over-year, reflecting a longer-term downward trend in coal demand. Crushed stone, sand, and gravel saw a 7.3% decline in September, its 12th consecutive year-over-year decline. These declines were offset by gains in other commodities, such as grain, which saw a 19.6% year-over-year increase, reflecting a recovery from 2023's weaker grain export season. Chemicals and petroleum products also posted gains, increasing by 4.0% and 7.5%, respectively.

In total, combined carload and intermodal originations for September 2024 reached 2,031,385 units, up 5.4% over last year. While some sectors faced challenges, the rail industry posted overall growth, with intermodal volumes being the standout performer. However, as noted above, as we enter the final quarter of the year, the full extent of the port strikes and Hurricane Helene's impact on supply chains remains unclear, leaving the rail industry and the broader economy in a precarious position.



For the first nine months of 2024, total U.S. carloads totaled 8,472,040, a 3.3% decline from the same period in 2023, highlighting the mixed performance of various sectors. While grain and chemicals saw year-to-date increases — with year-to-date carloads of chemicals through September the highest on record — coal and crushed stone posted notable declines. As the U.S. economy navigates its challenges, rail volumes will be a critical indicator of broader economic health, particularly as we assess the impact of recent disruptions on consumer spending and manufacturing — both key drivers of rail traffic. The coming months will determine whether the rail sector can maintain its positive momentum in the face of these headwinds.