PLG CONSULTING

STRATEGIC ANALYSIS

THE APPLAUSE FOR PSR WAS DEAFENING

How investor praise reinforced efficiency, narrowed resilience, and left shippers asking whether a bigger railroad will really serve them better.

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C-SUITE BRIEFING	RAIL STRATEGY	UP-NS MERGER CONTEXT

Executive summary

Precision Scheduled Railroading did not simply improve railroad efficiency. It reshaped the industry's incentives. As investors rewarded leaner operations and stronger financial performance, railroads were incentivized to prioritize efficiency over resilience, latent capacity, and long-term growth capability.

For many shippers, the result was palpable. They experienced reduced elasticity, tighter service options, higher rates justified by the value of scarce rail capacity, and increased pressure to commit freight under longer-term arrangements. In normal conditions, an optimized network can perform well. Under stress, a network with less cushion can become difficult to recover.

Against that backdrop, Union Pacific and Norfolk Southern is couching their proposed merger as a new growth platform. The strategic promise is clear: longer single-line routes, fewer interchanges, more density, truck conversion, and a broader national franchise. Those benefits may prove real. But for upper management who rely on rail, the more important question is whether the rail industry has truly learned from the tradeoffs of the PSR era, or whether larger scale is again being asked to stand in for better service.

C-SUITE THESIS

The UP-NS merger should be evaluated not only as a transaction, but as the next phase of an industry strategy that prioritized optimization over resilience, and is now touting the efficiency of growth through scale. The issue is not whether PSR worked. It did. The issue is whether the industry can grow in a post-PSR era without becoming more fragile.

What executives should take away

1	PSR solved a profitability and productivity problem, and investors rewarded the result.
2	The same program reduced operational cushions that help railroads absorb disruption and growth.
3	Investor praise created a feedback loop: efficiency produced earnings, earnings produced approval, approval produced more optimization.
4	Short lines became an important counterweight by preserving customer intimacy and local service flexibility.
5	The merger is best understood as the next strategic chapter: optimization of geography after optimization of operations.

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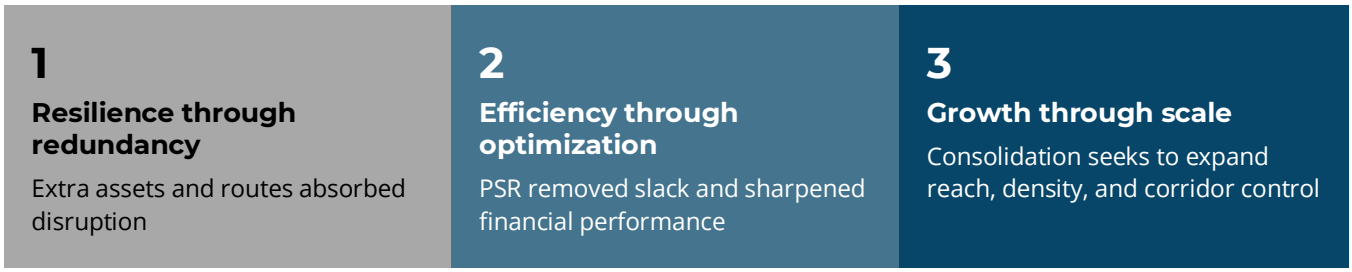
CONTEXT

The merger debate is only part of the story

For many shippers, the immediate question is simple: why should they believe this time will be different? The proposed merger between Union Pacific and Norfolk Southern has sparked one of the most consequential rail debates in decades. Supporters see a growth platform. Opponents see deeper concentration. Regulators are weighing competition, service, labor implications, and the long-term shape of the national freight network.

Yet much of the public discussion remains fixed on the transaction itself rather than the strategic path that made a merger like this plausible. The UP-NS merger did not emerge in a vacuum. It is the latest expression of a journey that began decades ago and steadily reshaped how railroads operate, how shippers engage carriers, and how freight moves across North America.

EXHIBIT 1 — RAIL STRATEGY HAS MOVED THROUGH THREE ERAS



The merger is therefore not just a regulatory event. It is a strategic signal. If PSR optimized the railroad operating model, the next phase may optimize the freight map itself — longer corridors, more internalized handoffs, greater density, and fewer points where customers can use independent alternatives as leverage.

Before PSR, railroads were built for redundancy

For much of the twentieth century, railroads were built around a practical operating assumption: when problems arose, capacity solved them. Railroads kept extra locomotives, extra crews, extra yard capacity, and multiple routing options. Networks were designed with redundancy because disruption was expected. If weather struck, traffic surged, or equipment failed, there was usually another way to move the freight. That system was resilient, but that resiliency came at a cost.

Following deregulation under the Staggers Act and decades of consolidation, railroads became healthier financially, but investors continued pressing for more. By the time Hunter Harrison emerged as the industry's most influential operating leader, the question was no longer how to save railroads. It was how to make them perform better, look sharper to the market, and deliver the financial results investors would continue to reward.

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Many merger proponents cite the history of the Staggers Act as evidence that continued consolidation and asset rationalization are good for the railroad industry. At the time Staggers passed in 1980, much of the railroad industry was financially broken. Railroads were burdened with excessive regulation, deteriorating infrastructure, redundant routes, weak capital investment, and pricing rules that created obstacles to responding to the marketplace. Staggers heralded a period of deregulation, line rationalization, and consolidation that was necessary to restore the rail industry's health. Nearly a half century later, the rail industry isn't populated by financial basket cases but by Wall Street darlings. The idea that simply continuing to apply — without question — the remedies of the Staggers Act to cure what ails modern railroads doesn't do justice to just how far railroads have come or where they still fall short in terms of being responsive to shippers' needs today.

OPERATING MODEL

PSR worked — but it optimized for a narrower definition of success

Hunter Harrison's answer became Precision Scheduled Railroading: a disciplined campaign to remove waste wherever it could be found. The concept is simple: keep assets moving, reduce dwell, eliminate unnecessary touches, and run fewer, longer, more productive trains.

The results were dramatic. Operating ratios improved. Asset utilization strengthened. Railroads became leaner, faster, more disciplined, and more profitable. Wall Street embraced the model, and PSR spread across the North American rail industry. The problem is not that PSR failed on its own terms. The problem is that the industry increasingly treated those terms as if they were the whole story.

As PSR delivered measurable efficiency gains, investor approval shaped its trajectory. Shareholders and large financial institutions applauded the railroads as operating ratios improved and financial discipline deepened. That applause was deafening. Like most institutions responding to strong external validation, railroads were encouraged to keep moving in the same direction.

EXHIBIT 2 — WHAT PSR OPTIMIZED — AND WHAT IT REDUCED

What PSR optimized	What PSR reduced
Asset utilization	Network flexibility
Operating ratios	Surge capacity
Schedule discipline	Routing options
Corridor density and velocity	Margin for disruption
Financial discipline and profitability	Latent capacity and elasticity
Locomotive and crew productivity	Terminal and yard throughput capacity

That tradeoff did not always matter under normal conditions. Optimized networks can perform exceptionally well when demand is steady and operations are stable. But efficiency and elasticity are not the same thing. Efficiency shows up in operating ratios and asset productivity. Elasticity is the network's ability to absorb a surge, a storm, a crew shortage, or a bad week — and recover without stranding freight.

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Not everyone was clapping for PSR. Many rail shippers felt that the railroad industry's success was coming at their expense. The tensions boiled over in an April 2022 STB hearing where Class I CEOs were skewered for service failures, poor customer service, and inadequate locomotive crews.

SERVICE UNDER STRESS

When efficiency meets the limits of resilience

The practical effect of PSR was the removal of many assets and operating cushions that once gave the network room to absorb disruption and growth. Sidings were taken out of service. Terminal capacity was reduced. Hump yards were converted to flatter, simpler operations. Locomotive fleets were trimmed. Crew bases were consolidated. Mechanical forces were reduced. Surge capacity was not merely allowed to fade. In many cases, it was intentionally rationalized away in the name of discipline.

The industry's service problems during parts of 2021 and 2022 brought that tension into public view. The Surface Transportation Board held emergency hearings as service deteriorated across parts of the network, and Union Pacific's use of embargoes became a particular focus of regulatory scrutiny. Whether or not one accepts every critique of PSR, the episode underscored a reality the industry can no longer sidestep: efficiency and resilience often exist in tension, and the more relentlessly one is prioritized, the more deliberately the other must be protected.

MANAGEMENT IMPLICATION

When the network tightens, the relevant question for shippers becomes very practical: which freight gets protected? A railroad working through congestion, weather, labor disruption, or merger-related turbulence will protect the traffic that keeps the system fluid and the franchise intact. From the railroad's perspective, that is rational. From the shipper's perspective, it introduces risk to its logistics function with little visibility and few opportunities to mitigate.

MARKET STRUCTURE

The short-line counterweight made the system more balanced than it appeared

As Class I railroads concentrated on density and core corridors, thousands of miles of track were transferred to short lines and regional railroads. At the time, the strategy seemed logical: large railroads would focus on high-density freight, while short lines would handle local service.

Yet many short lines did far more than survive. Freed from the economics of a large Class I system, they rebuilt customer relationships, developed new business, and often created a level of service flexibility that larger networks struggled to provide economically. In a sense, the industry became both more centralized and more decentralized at once: the Class I railroads concentrated on efficiency, while the short lines concentrated on customer intimacy.

EXHIBIT 3 — CLASS I AND SHORT-LINE ROLES BECAME COMPLEMENTARY

Class I emphasis	Short-line emphasis
Density	Customer intimacy
Asset productivity	Local service
Corridor optimization	Market development
Network efficiency	Commercial flexibility
Scale economics	Responsiveness

The PSR paradox

After decades of optimization, railroads faced a new question: what comes after efficiency? There are only so many times a locomotive can be cycled harder, so many yards that can be rationalized, and so many operating costs that can be removed before the gains begin to flatten. Every optimization strategy eventually must contend with the law of diminishing returns. When that happens, growth becomes the next frontier.

This is the PSR paradox. The same industry that spent the better part of a decade optimizing around efficiency is now presenting a future centered on expansion. Both ideas can be true, but they are not governed by the same operating assumptions. A railroad organized around shedding capacity does not become a railroad organized around driving growth simply because a merger occurs.

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STRATEGIC INTERPRETATION

The UP-NS merger may be the next phase of the PSR era

The UP-NS merger is usually framed as a growth story. Single-line service, truck conversion, intermodal expansion, improved fluidity, and broader reach are the benefits supporters cite. Those benefits may prove real. But they are also exactly the kind of promises shippers have learned to examine more carefully than they once did.

There is another way to understand the transaction: the first phase of the modern rail strategy optimized operations; the vision of the second phase represented by the UP-NS merger will optimize geography. For decades, railroads focused on making networks run more efficiently. Today, they may be focused on making networks structurally stronger by controlling longer corridors, internalizing interchanges, concentrating freight density, and positioning themselves at the center of future freight flows.

EXHIBIT 4 — THE STRATEGIC QUESTION SHIFTS FROM COST REMOVAL TO GROWTH ABSORPTION

PSR-era logic	Growth-era requirement
Remove excess capacity	Add reliable capacity where growth appears
Reduce assets and touches	Absorb volume without service degradation
Optimize density	Preserve optionality and recovery paths
Defend operating ratio	Rebuild customer confidence and service resilience

Viewed through that lens, the merger becomes less about simply operating trains more efficiently and more about shaping the future freight map itself. The proposed transaction is not the structural change itself. It is the most visible symptom of a structural change already underway — and one likely to continue regardless of how this application is decided.

CORE DILIGENCE QUESTION

Can a system optimized to remove capacity transition into one optimized to absorb growth without rebuilding the very capabilities PSR reduced?

CUSTOMER ECONOMICS

Why this matters to shippers and upper management

The possibility that network structure now determines supply-chain resilience should matter to shippers because it changes the questions serious customers should ask. Not just whether the railroad will be bigger, but whether it will be better for freight-paying customers.

For most of the last generation, shippers treated the railroad primarily as a service relationship. The practical questions were rates, transit time, equipment supply, and on-time performance. The structure underneath that service felt like someone else's problem. That assumption is breaking down.

Today, network structure affects leverage. Gateway access affects options. Railroad priorities affect service recovery. Competition affects negotiating power. The shape of the network increasingly determines the resilience of the supply chain.

That is why the debate is not simply about efficiency. Many shippers value something a more consolidated network can reduce — optionality. Single-line service may lower handling costs, reduce interchange friction, and improve transit on some lanes. But it can also narrow alternative routings, alternative gateways, alternative carrier relationships, and alternative commercial leverage. Efficiency and optionality are both real goods. They do not always move in the same direction, and customers do not all value the tradeoff the same way.

EXECUTIVE LENS — WHAT CUSTOMERS ARE REALLY BUYING

Traditional rail buying lens	Emerging strategic lens
Rate	Total supply-chain resilience
Transit time	Reliability under stress
Equipment supply	Access to recoverable capacity
Route	Optionality and leverage
Service promise	Enforceable recovery capability

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DECISION IMPLICATIONS

What comes next

FINAL TAKEAWAY

The issue is not whether efficiency matters. It does. The issue is whether the next rail strategy can deliver growth while rebuilding the flexibility, resilience, and customer confidence that shippers now consider essential.

Whether the UP-NS merger is approved or denied, the forces that produced it are unlikely to disappear. The pursuit of density, the search for growth, the importance of corridor control, the economics of scale, and the need for capital concentration were all in motion long before this application was filed. They will likely continue long after the STB issues its decision.

The history of PSR helps explain why many customers now view the merger's promises with skepticism. It is difficult to ask shippers to endorse an even larger railroad on the assurance that it will better serve their needs when many believe the last major operating transformation delivered outsized financial rewards to carriers and investors at the expense of their service levels and resiliency.

Questions every CEO should ask before accepting the growth narrative

1	Has the industry truly learned from the tradeoffs of the PSR era — or will larger scale once again be asked to stand in for better service?
2	Will a bigger railroad be better in the ways that matter when freight actually has to move — rates, transit time, equipment supply, service recovery, and on-time performance?
3	Which freight gets priority when the network tightens — and will critical customer freight be on the protected list during congestion, weather, labor disruption, or merger-related turbulence?
4	Will efficiency gains from consolidation come at the cost of resilience, optionality, alternative routings, gateways, and commercial leverage?
5	If the promised growth and service improvements do not materialize, what comes next — investment in resilience, or another round of capacity reduction and asset trimming?

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The future of freight rail won't be determined by whether one merger — however important — succeeds or fails. It will be decided by whether the industry can balance efficiency with flexibility in the era that follows — and whether it can do so without sacrificing the service resilience shippers need.

And if the promised windfall does not materialize, shippers are right to ask what comes next. If the gains fall short, will the railroads simply return to the PSR playbook: reduce capacity, trim assets, and defend efficiency first?

Precision Scheduled Railroading transformed the railroad. The next phase of that evolution may transform the map. If it does, the consequences will extend far beyond the boardroom and every shipper will have a stake in the outcome.