The Basics of Railroad Competition

A. Railroad competition in the 19th Century was structured by three basic facts:

1. **Railroads owned the highway *and* all the vehicles on the highway**

2. **Railroads had High Fixed Costs**

3. **Railroads, for political and *economic* reasons, were not allowed to be Liquidated**

B. The Railroad's Pricing Problem – The decisions of railroad managers in setting or administering their prices reflected two basic conditions:

1. **The pressure of high fixed costs. Costs that did not vary with traffic volume were about *two-thirds of the cost of running the railroad*!**

   a. **Interest on invested capital, salaries, insurance, and taxes were all pure fixed costs.**

   b. **Movement expenses were pure variable costs.**

   c. **Repair and maintenance of roadbed, buildings, bridges, etc., and station expenses were partly fixed and partly variable.**

2. **The existence of unused capacity.**

C. *These high fixed costs created an inexorable pressure to attract traffic*.

D. The typical railroad often had *no competition for local, short-haul freight*. However, almost all large cities were served by several railroads.

E. The consequence of points B) and C) was that railroads had considerable flexibility in setting their rates. Unlike most other economic actors, the *railroads tended to set prices in relation to cost rather than demand*.

F. ***This inexorably led the railroads into setting rates that discriminated against persons, places, and types of traffic*****.**