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Rail mergers stranding users on the tracks

By DIANE DUFF

For the past several years, the Alliance for Rail Competition, its members and allies have been petitioning the U.S. Congress to wake up and smell the coffee when it comes to rail policies. We believe its time for a change. Consolidations of the last 20 years have made the rail industry into regional monopolies and the Canadian National Railway Burlington Northern Sante Fe Railroad merger announcement proves that we are merely a few steps away from having two North American rail monopolies.

Let's put aside the specifics of a CN-BNSF merger for a moment, and look at what we already experience under today's regional monopolies. Approximately 30 percent of rail customers are held captive to their railroad, paying exorbitant rates for poor and continually deteriorating service while shouldering more and more of the costs associated with this form of transportation. Those captive customers are less able to compete in an increasingly global marketplace, yet the nature of their business forces them to rely on this underperforming, underachieving and generally unresponsive railroad system.

If you question this assessment of rail performance, consider that those rail customers who have the flexibility to choose another mode of transportation largely have done so. As one rail customer put it: If I could figure out a way to conduct our business without using railroads, I would absolutely without any hesitation stop doing business with them. Is it any wonder that more than 80 percent of all freight in the United States moves by truck? Despite all their claims to the contrary, the railroad industry's own data confirms that rail volumes are at essentially the same level as they were in the 1940s.

So what impact would a CN-BNSF merger have on this already unsavory situation? Let's consider the real facts:

- A CN-BNSF merger would be a side-by-side merger, not an end-to-end merger as the two companies claim. An end-to-end merger combines two rail systems that don't serve the same territory, whereas side-by-side mergers involve rail systems operating parallel to each other. Side-by-side mergers are duplicative, tend to eliminate rail-to-rail competition and create captive rail customers.

- This proposed merger effectively isolates three other railroad systems -- Union Pacific, Kansas City Southern and Canadian Pacific -- and calls the financial prospects for expansion of a fourth Dakota, Minnesota & Eastern into question. Analysts are already saying that these isolated railroads will have difficulty competing against a giant railway that will be able to generate large amounts of cash, make sizeable investments in its gathering networks and dominate traffic routings. As a result, these railroads will all either be forced into defensive mergers of their own or out of business. Either way, a clear path to the two monopoly system emerges.

- The sheer size of the proposed system would make a merger difficult to achieve without service disruptions. This is by far the largest merger to be considered. Each of the participants in the mega mergers of the recent past have assured us that their merger would cause no interruptions and would improve efficiencies through single-line service, etc., etc. Rail customers in Texas know all about the costs of merger-related rail service problems and the promises of improved service and increased efficiencies have yet to be realized.

Top rail analysts on Wall Street have been saying for some time now that the dwindling number of railroads will soon force an end to the earnings-through-mergers strategy. And for more than two years now, these same analysts have been calling for earnings growth through improved customer service, something that has not been a byproduct of mergers. According to an essay written by rail analyst Jim Valentine of Morgan Stanley Dean Witter in 1997, if railroad management really wants to get Wall Street's attention, it needs to develop a revenue growth strategy. He continues in saying that when the railroads stop

being distracted by who has the biggest network or locomotive fleet and begin to really focus on the customer, especially the small to medium customers, including their short-line feeders, we may see market share gains from trucks for the first time ever. Railroads can appease their shareholders with revenue growth by putting the customer first.

Could the railroads put the customer first today? Sure they could, but without the forces of competition applying to a large chunk of their customer base, they won't because they don't have to. No monopoly industry has ever embraced increased competition with open arms. But once those monopoly industries have been deregulated and are operating in a competitive environment, revenues increased, the number of new jobs grew and customers benefited in the form of improved services and competitive rates. The only reason railroads will change their approach is if there is more intra-rail competition, and that is what ARC is petitioning Congress to do.

Regardless of the outcome of this proposed merger, the die is cast. It is clear that the rail industry is on a path that will leave rail customers with a two major rail monopoly system in North America. So the questions rail customers must begin asking themselves are: What kind of service and rate performance can I expect from a two monopoly rail system in North America? What policy changes would make such a system provide the kind of service and rate performance that I need? Congress will play a role in this and the outcome is largely up to you -- the rail customer.

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