

January 7, 2000

Mr. Clayton Boyce, Editor  
Traffic World  
1230 National Press Bldg.  
Washington, DC 20045

Dear Mr. Boyce:

I was troubled to read your January 3, 2000 editorial, "Most Curious" where you stated that the CN-BNSF merger, "viewed objectively, is much more deserving of Surface Transportation Board approval than the Conrail carve-up or the Union Pacific-Southern Pacific merger."

Maybe the CN-BNSF proposal could be considered "deserving" if it were viewed in a vacuum. But we are far beyond the point where we have the luxury of looking at any proposed rail merger based on anything other than the big picture. Thus, I feel compelled challenge your reasoning for why the CN-BNSF merger should be approved:

1. The CN-BNSF merger is anything but an end-to-end merger. A cursory review of the map that Traffic World printed in the same issue shows clearly that this is a side-by-side transaction. 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.

2. Promoting intra-rail competition is still a major tenet of U.S. rail policy, yet this merger will only limit customer choice. A CN-BNSF merger would eliminate many of the competitive options that currently exist for rail customers down the entire length of the Mississippi River, negatively affecting the states of Illinois, Iowa, Arkansas, Mississippi and Louisiana. For example, corn movements, which tend to move by barge, still rely on railroads to get to the river. Contrary to popular belief, rail rates are a major component in river movements of corn, so corn growers will soon be entering the world of rail captivity, courtesy of a CN-BNSF merger. Similarly negative consequences will be felt in Kansas, Nebraska and South Dakota. Competition that exists today from Chicago to Sioux City—gone. Industries that will see the most immediate negative impacts will include corn, wheat, fertilizer, and chemicals.

While the CN-BNSF merger may be largely a stock transaction that "won't create a burden of debt" that rail customers will later be expected to repay, if approved, this merger will inevitably result in a North American duopoly. Why? Canadian Pacific, Union Pacific and Kansas City Southern will all become isolated rail systems that will be forced either to acquire, be acquired or simply go out of business.

In the case of the CP, its network of lines will be surrounded by CN to the north and BNSF to the south. Analysts are already saying that the CP will have difficulty competing against a giant railway that will be able to generate large amounts of cash, make sizeable investments in its grain gathering network and dominate traffic routings away from CP. If one carrier has a dominant presence facing only a weak competitor, the weak competitor will either go out of business, or it'll be forced to join up with another major U.S. carrier. The potential loss of the CP is especially troubling for industries including forest products, grain, potash and fertilizer and the outcome strengthens the railroads' monopoly stranglehold over the states of Minnesota, North Dakota, Montana, Idaho and Washington. CP is the only rail carrier providing, albeit limited, rail competition to the some of the northern U.S. states.

The Union Pacific has already been identified as being susceptible to the some of the most serious traffic diversions that would result from this merger. Still in recovery from the worst service crisis in history, which was brought about as a result of a similar defensive merger, one must consider whether we could be facing an instant replay—only this time on an even grander scale—and such a result would impact everyone in the West.

The Kansas City Southern has had a long-term marketing agreement with the CN/IC, but this merger calls its future into question. With this combination, CN/IC doesn't need to sustain this agreement, effectively shutting KCS off from the "NAFTA railroad" network the marketing agreement offered.

3. To assert that a CN-BNSF merger would go off without a hitch simply because the CN-IC merger had no problems is an unreasonable leap of faith given the precedents. The merger of the much smaller IC with the CN was truly an end-to-end merger, and did not result in anything close to the "largest North American railroad network," as the CN-BNSF merger is being billed.

4. An increase in the single-line efficiencies resulting directly from a CN-BNSF merger are questionable at best, and could probably be achieved without a merger. During the past year, CN-IC has claimed significant improvements in traffic handling through its marketing alliance with KCS. If this is true, apparently a merger is not critical to achieving such efficiency improvements. Further, none of the mega-mergers of the last few years has demonstrated consistent service improvements compared to pre-merger data. The reality is that the huge railroad mergers of the 1990s have yet to produce the low prices and/or better service that they promised. In fact, rail customers have experienced a lowering of performance standards—as well as a lowering of expectations. And mergers also have not produced lasting returns for stockholders.

The future of railroading does not depend on further consolidation that will inevitably lead to a North American duopoly. Rather, it depends on growing the railroad industry's traffic base. Mergers have not yet produced a railroad business organization that is interested in developing or instituting a true growth strategy. Instead, mergers have relied on achieving earnings growth through cost cutting, and the CN-BNSF proposal is no different. Wall Street has been telling us for some time that there is very little earnings potential left in the earnings-through-mergers strategy. A true growth strategy would require focusing in on how the railroad in question could innovatively and efficiently meet the growing and changing needs of its current and prospective customers.

How many times will rail regulators—and rail customers, for that matter—be lulled into accepting the false hope that further consolidation generally, or this merger specifically, will produce anything different?

Sincerely,

Terry C. Whiteside  
Chairman, Alliance for Rail Competition