milwaukee should remain as a viable railroad

Those who have been concerned about the financial problems of railroads, and their future in America, were in part cheered by Sam Reynolds' editorial of Jan. 4, which

local comment

supported the idea of maintaining the Milwaukee Road as an independent rail corporation.

Unfortunately, railroad bankruptcy is a twilight zone sort of affair, and what will actually happen to the Milwaukee in the months to come is anyone's guess. Over a year ago, I suggested on this page that financial reorganization was probably the only hope for the railroad.

Now that the railroad is finally in bankruptcy, there is the problem of a Department of Transportation (DOT) that feels a mandate to clean up what it perceives as "the railroad mess."

Without too much apparent thought, many government and private officials have come to the conclusion that there are simply too many railroads and that merging whole bunches of these corporate entities together will somehow make the rails themselves more profitable.

DOT Secretary Brock Adams has been making noises along those lines already, suggesting that the Milwaukee Road is a redundant railroad, and that it would be best to let it and others like it "disappear."

Especially in the case of the Milwaukee Road, that line of reasoning is misleading and superficial. The present bankruptcy of the Milwaukee Road is not by any means the inevitable result of excessive competition between too many railroads, and the basic causes are not even of recent origin.

Before 1905, the Milwaukee Road was, by all accounts, one of the most prosperous, well-run railroads in the world. Its board of directors had included such financial powers as August Belmont, James Stillman, Henry Rogers, and William Rockefeller. For many years, the railroad was known as the Standard Oil railroad, as that company was prominent in the ownership.

In the early 1900s, J.P. Morgan, always a rival to the Rockefeller interests, had teamed up with James Hill of the Great Northern Railway to create a truly transcontinental rail system linking the Atlantic Ocean at New York to the Pacific Ocean at Seattle. Morgan controlled lines to the east of Chicago, and Hill controlled the Great Northern and Northern Pacific to the west of St. Paul.

But between St. Paul and Chicago, the two controlled no railroads. To complete their system, Morgan wanted to purchase the Milwaukee, which had been carrying Hill's Chicago-bound traffic from St. Paul to Chicago. Hill, however, wanted to buy the Chicago, Burlington & Quincy Railroad (C.B. & Q.). Standard Oil refused to sell its interests in the Milwaukee, and Hill and Morgan turned to the C.B. & Q.

Interests representing the Milwaukee attempted to keep control of the Burlington line out of Morgan's hands in an awesome stock battle. The reasons were clear: the traffic that the Milwaukee carried from St. Paul to Chicago was a very important part of the company's business, and to lose it to the C.B. & Q. would be a large financial setback. However, Hill and Morgan eventually acquired the Burlington (although in a countermove, the Milwaukee interests just narrowly missed gaining control of the Northern Pacific).

So the Milwaukee found itself cut off from the G.N.-N.P. traffic and decided that to survive, it must generate its own trancontinental traffic by becoming a transcontinental railroad.

In 1908 the "eighth wonder of the world," the Milwaukee "Pacific extension," was completed from South Dakota to Tacoma, linking Chicago and the Pacific Ocean. The anticipated cost of the extension had been under $60 million. The actual cost was close to $300 million.

A large part of that horrendous, unexpected cost was due to the Great Northern and Northern Pacific interfering with land prices as the Milwaukee purchased right-of-way (the Milwaukee Road received no land grants).

To finance that incredible sum, the Milwaukee released bond issue after bond issue and stock issue after stock issue. In 1926, the railroad could no longer meet the crushing debt obligations of the Pacific extension, and declared bankruptcy. Its bankers, which the Interstate Commerce Commission concluded had put the railroad in the position that necessitated bankruptcy, purchased the railroad.

They lost control in another bankruptcy in 1935. That bankruptcy ended in 1945 with another bank prominently

'That's okay—I wasn't going anywhere much, anyway.'

represented in the ownership of the company.

The bankruptcy declared in December 1977 is, then, the third bankruptcy of the Milwaukee Road in this century.

Yet to suggest that this many bankruptcies is an indication of inherent weakness in the railroad is superficial. Part of the problem is with the process of bankruptcy itself. Bankruptcy does not imply that debt is cancelled, but only that payment is suspended for a period of time when it becomes apparent that a company no longer has the capability to meet its debt payments.

During that period, the various creditor groups meet to negotiate the outstanding debt of the company, either with regard to reducing it, or rescheduling payment. The final plan for reorganization of the debt structure, arrived at in this way, is then approved or modified by a board of trustees appointed by federal court.

It is the responsibility of the trustees to ensure that after bankruptcy, the company will have a debt structure sufficiently revised to both provide the previous creditors with as much return as possible, and to provide for a viable company in future operations.

The previous bankruptcies of the Milwaukee Road are considered to have been very conservative bankruptcies; the debt was not scaled down to a great degree. Hence, in a sense, the Milwaukee Road has been paying for that Pacific extension even until December 1977, and has been unable to finance any substantial improvements over the years because of the size of that original debt.

After reorganizing in 1945, the Milwaukee used its available financial bonding power to replace a good deal of equipment worn out by heavy war-time service, repair track, and, in the 1950s, replaced its steam locomotives with diesel locomotives, and modernized the electrification divisions.

But in the 1960s, when those facilities were in the best condition in years, and the Milwaukee should have been aggressive in its fight for shares of the transportation market, the railroad entered a series of merger negotiations with the Chicago & Northwestern Railroad. So certain was the board of directors of eventual merger, that they virtually abdicated a management role on the Milwaukee. They became in every sense, a "caretaker board" waiting for merger.

When the merger did not come off, the railroad had deteriorated significantly, markets had not been obtained to provide revenue, and the company's financial leverage was used up.

Since that time, the Milwaukee has been struggling to try and make do, to patch things up enough to keep going. On a railroad, makeshift management rarely works. If you derail trains you lose customers. When you lose customers, you lose revenue. When you lack revenue, you defer maintenance. When you defer maintenance, you increase derailments. December 1977 simply marked the point beyond which the downward spiral could not go.

Derailment costs on the Milwaukee Road have been averaging about $4 million a month. For a railroad, any railroad, costs of that magnitude are nothing less than a massive financial hemorrhage.

As a result, the Milwaukee has been encountering severe cash-flow problems for a number of years. To keep operating, the electrification was scrapped to get the scrap copper money. Timberlands have been sold off. Nearly 2,000 employees have been laid off (the roundhouse and service facilities at Deer Lodge, once performing the finest work on the system, have been virtually eliminated).

As far as long term management is concerned, those moves were disastrous. The maintenance and depreciation charges on the diesel locomotives that replaced the electrics make those diesels substantially more costly to operate than the electrics.

The timberlands have always been a steady flow of cash in sale of stumpage rights. And those employees maintained the track and made the sales. But for a desperate management, tomorrow would have to take care of itself; the managers could only worry about today. Sadly, for the Milwaukee, tomorrow came.

Brock Adams, secretary of the Department of Transportation, apparently believes that the problem lies not rooted in the Milwaukee's individual history, but in the presence of too many railroads in the Midwest, competing for too little traffic.

Yet, again, the history of the Milwaukee suggests that, at least in the particular case of the Milwaukee, Brock's assumptions are not true. Although it is in the Midwest where the Milwaukee has too much unprofitable track, the historical record suggests the opposite.

The Milwaukee has traditionally been operated as essentially two separate railroads: "Lines East," east of Mobridge, S.D., and "Lines West," west of Mobridge. Lines East, comprising that portion of Milwaukee trackage which duplicates with five other midwestern railroads, has been generally profitable for the railroad, earning revenues per track mile on par with any of the company's healthiest competitors.

Lines West has been a chronic money-loser for the railroad, earning about half as much as Lines East, per track mile, or about half of what Burlington Northern earns on its transcontinental trackage.

It is not, then, any weakness associated with over-competition that has hobbled the Milwaukee Road, but inability to generate return on that portion of its track which has the least competition from other railroads.

My own feeling has been that this situation has stemmed from a lack of aggressiveness and facilities in the western territories. The Interstate Commerce Commission, however, has remarked that the Milwaukee, in spite of superior grades and a shorter route "is hamstrung and shorthauled...continually losing effectiveness as a competitor," primarily because "of restrictive routings imposed by connecting lines," which means that the Milwaukee has not been given its share of traffic at connections with other railroads.

The ICC has long held that the Milwaukee Road should remain as an independent competitor to the Burlington Northern and the trucking industry. In fact, one of the major provisions allowing the Burlington Northern merger was the existence of a strengthened Milwaukee Road to provide competition, and that allowing the Milwaukee to merge or otherwise disappear would be a "subversion" of the court rulings that finally allowed the creation of the Burlington Northern.

The ICC attempted to impose conditions that would strengthen the Milwaukee, and although the conditions were helpful, they were not of the magnitude to overcome the railroad's longstanding financial weakness.

Competition is a concept of great controversy in the railroad industry. That it works is no illusion. Several months ago, the Milwaukee cut grain shipment rates by 15 percent, and the Burlington Northern almost literally cried bloody murder.

Another example, suggestive of the strong role that a healthy Milwaukee could play, can be taken from the Burlington Northern merger hearings in 1966. Merger advocates glowingly described how, after merger, the combined G.N.-N.P.-C.B.&Q. transcontinental train schedules could be reduced from 76 hours to 65 hours.

Even as they spoke, Milwaukee's "hotshot" freights, the "XL Special" and the "Thunderhawk," were accomplishing transcontinental runs in a shade over 55 hours.

The solutions to the Milwaukee's plight are not obvious. Massive infusions of federal aid to keep the company afloat would be unfair to the Milwaukee's competitors, who have operated on private funding. A liberal financial reorganization would have a hard time being approved by the bondholder's committees.

As objectionable as federal funding might be, the end of the Milwaukee Road would be far more objectionable. I hope enough people will write to Brock Adams at the Department of Transportation and urge him to preserve the Milwaukee Road as an independent transcontinental railroad. — Michael Sol, 4611 North Ave. W., Missoula.

the missoulian
Founded May 1, 1873