

New York, 21st. November, 1895.

JAMES J. HILL, ESQ.,

St. Paul, Minnesota.

Dear Mr. Hill:-

I send you herewith a series of articles that have appeared in the evening "Commercial Advertiser" under the title of "The Case against Consolidation". Possibly a more accurate title would have been "The Secret of Great Northern's Success".

Sincerely yours,

*Edward D. Adams.*

(Enc-4)

# WALL STREET TO-DAY

## Latest News From All the Money Markets of the World.

### THE CASE AGAINST CONSOLIDATION

#### I.

The issue of the Great Northern annual report, 1894-5, and the presence of Mr. James J. Hill, president of the road, in this city, together with the recent decision of the court, at St. Paul, in the case of the State of Minnesota asking for an injunction against consolidation of Great Northern and Northern Pacific, make the present time extremely suitable for a presentation of the case against consolidation.

Up to the present time the case has been argued only in a legal way, and from the point of view of a Great Northern stockholder and the State of Minnesota. A good deal has been heard of the importance of the matter to the Northwest incidentally. An effort will now be made to present the case of the Northern Pacific itself. It is submitted, firstly, that the original scheme of consolidation, based on the "London Agreement," was one-sided, and would have given great advantages to the Great Northern without corresponding advantages to Northern Pacific, and, secondly, that the need for consolidation does not exist.

This is a matter on which all Northern Pacific security holders, and especially the Consolidated bondholders, and security holders of junior issues, are vitally interested, and, indeed, it may be said that the interests of all are alike in the matter. Most of all, however, does it concern the stockholders, on whom falls the burden of providing new money to pay the debts of the road, if they wish to preserve for themselves any equity in the road's future earnings.

Firstly, as to Great Northern. It may be admitted that it is in all respects a success. That is to say, it is a corporation that has always paid its obligations promptly on the day of maturity, and it has distributed regular dividends on its stock. The record of its operations shows, as will be seen hereafter, steadily increasing efficiency on the part of the machine, and its finances appear to be sufficiently sound. Mr. Hill has the reputation of being, in many respects, perhaps, the foremost railroad man in this country. No one can say, after reviewing the operations of his company, that this reputation may not be deserved. So much may freely be admitted. It is not intended to allege that Great Northern would be unable to make good the proposed guarantee. For the purpose of this argument, the solvency of Great Northern and the extreme ability of Mr. James J. Hill are assumed as proven.

The proposition is, therefore: Is it wise for Northern Pacific security holders to invite the Great Northern to guarantee annually \$6,200,000 per annum of net earnings, the consideration for the guarantee being 51 per cent. of the new capital stock of Northern Pacific, and a majority of the board of directors? To which our answer is: It is not wise, and it certainly is not necessary.

The reorganization of Northern Pacific, as of every corporation in bankruptcy, is designed to bring fixed charges and earnings to equilibrium, at least. We may leave out of calculations the details of the sacrifices demanded from security holders, remembering only that important sacrifices are asked from the bondholders below the seconds, and very serious sacrifices are demanded from the stockholders. We may also leave out of our calculations the purely financial side of the reorganization, remembering only that fixed charges in the past were so heavy as to render the company at once insolvent when the depression came. It is enough for our purpose to note that the deficit is extremely large.



The following table shows Northern Pacific mileage, and gross earnings, total and per mile of road, for the last five years. The figures are taken from the report of the Comptroller for the year ending June 30 last. This report will be used in all cases where possible, so as to avoid confusion:

	Miles.	Gross.	Gross per mile.
1890-1.....	4,222	\$25,151,544	\$5,941
1891-2.....	4,412	24,661,457	5,589
1892-3.....	4,443	23,920,108	5,384
1893-4.....	4,468	16,547,209	3,703
1894-5.....	4,469	17,434,980	3,901

This is evidence of extreme depression, hardly explainable even by a combination of panic and crop failure. Gross revenue is the item of all others in a railroad's operations least susceptible of control by good or bad management. Indeed, it may be said to be entirely beyond control.

The table immediately following shows the operating expenses, in gross and per mile, and the net earnings in gross and per mile of road.

	Op. Exp.	Ratio.	Net earnings.	Do. per mile.
1890-1 ...	\$14,940,402	59.40	\$10,211,141	\$2,418
1891-2 ...	14,176,364	57.48	10,485,092	2,376
1892-3 ...	14,471,771	60.50	9,448,337	2,126
1893-4 ...	11,816,120	71.40	4,731,089	1,058
1894-5 ...	11,319,682	64.92	6,115,298	1,368

This table is the corollary of the preceding. A decline of about 55 per cent. in net earnings in two years would break any road, no matter how carefully it were capitalized. It is to be noticed, moreover, that this decline in net earnings has been the result of the fact that, while gross earnings fell off over \$8,600,000, operating expenses were reduced by only about \$3,100,000.

Summarizing, we find—

Gross decrease 1890-1 to 1893-4 about 34 per cent.; net decrease, nearly 54 per cent.

# THE CASE AGAINST CONSOLIDATION

## II.

We have seen Northern Pacific's record for five years. It shows a decline in gross earnings per mile of from \$5,941 to \$3,073, and in net earnings per mile from \$2,418 to \$1,058. Let us look at Great Northern's results in the same five years.

	Miles.	Gross earnings.	Do. per mile.
1890-1 .....	2,796	\$10,281,714	\$3,676
1891-2 .....	2,865	12,604,128	4,398
1892-3 .....	3,351	13,522,581	4,034
1893-4 .....	3,765	11,345,356	3,013
1894-5 .....	3,766	13,109,939	3,481

Here we have, in two years, a decline of about \$1,260,000 in gross earnings, and a decline of \$1,385 in gross earnings per mile. Net results, and operating expenses, as follows:

	Op. ex.	Ratio.	Net earnings.	Do. per m.
1890-1 .....	\$5,163,954	50.22	\$5,117,760	\$1,830
1891-2 .....	7,133,298	56.59	5,470,830	1,909
1892-3 .....	7,335,417	54.24	6,187,164	1,846
1893-4 .....	6,488,779	57.19	4,856,577	1,289
1894-5 .....	7,146,462	54.51	5,963,477	1,583

Summarizing, we find, gross decrease per mile of road 1891-2 to 1893-4 about 31 per cent.; net decrease per mile about 32 per cent. Increased mileage obviates comparison of total figures. We compare thus with Northern Pacific:

	Gross per mile decrease.	Net per mile.
Great Northern .....	31 p. c.	32 p. c.
Northern Pacific.....	37 p. c.	56 p. c.

which at once gives us the vital point of difference between the two roads. Both have experienced much the same vicissitudes, and both have lost gross earnings, Northern Pacific more than Great Northern, but Great Northern has been able to decrease operating expenses, and thus reduce the net loss. How is it that Northern Pacific has not done so? The answer to that question contains the key to the Northern Pacific problem. Let us see, therefore, how the answer can be arrived at.

The table below shows the freight tonnage and density in the case of both roads, in each of the five years:

### FREIGHT TONNAGE.

	Northern Pacific.	Rate. Cents.	Great Northern.	Rate. Cents.
1890-1.....	3,497,234	1.40	2,280,382	1.23
1891-2.....	3,913,671	1.40	2,926,706	1.23
1892-3.....	3,514,404	1.23	3,103,647	1.23
1893-4.....	3,286,422	1.11	2,593,749	1.09
1894-5.....	3,781,316	1.11	2,946,920	1.01

### FREIGHT DENSITY.

	Northern Pacific.	Great Northern.
1890-1.....	282,345	220,417
1891-2.....	286,014	275,002
1892-3.....	307,176	254,886
1893-4.....	229,889	212,299
1894-5.....	263,405	271,421

Here we may notice that Great Northern has steadily gained on Northern Pacific in the matter of freight density. Last year, for the first time in its history, it surpassed Northern Pacific in this respect. Summarizing the changes, we find, comparing the highest years with the lowest:

	North. Pacific.	Great North.
Freight rate decrease...	20 p. c.	18 p. c.
Freight density decr'se.	25 p. c.	22 p. c.

There is close correspondence in these items, except that, as we have seen, Great Northern has shown much greater recuperative power, in the year ending June 30 last.



The foregoing figures, however, show very clearly that both roads have had to face times of great depression, and that the circumstances affecting business have been much the same in both cases. It is necessary to bear this in mind in order to see the force of what follows.

It is not necessary to examine the passenger statistics very closely, because they are not very important in affecting final results. We may safely confine our examination to freight statistics for the present, although it is impossible to separate freight and passenger statistics in looking at the total results from certain standpoints. As a matter of fact, both roads have lost heavily in passenger business, and it is probably safe to say that on neither of them has there been much profit in this business of late.

The following table shows the gross revenue per train mile, and the operating expenses per train mile on each road for the five years. The figures cover all revenue train mileage, as it is practically impossible to make an exact apportionment of expenses between freight and passenger train mileage:

	Northern Pacific.		Great Northern.	
	Gross per T.M.	Op. ex. per T.M.	Gross per T.M.	Op. ex. per T.M.
1890-1.....	\$1.86	\$1.11	\$2.09½	\$1.05
1891-2.....	1.91	1.10	2.26	1.28
1892-3.....	1.80	1.09	2.41¼	1.30¾
1893-4.....	1.51	1.09	2.03½	1.16½
1894-5.....	1.68	1.10	2.02	1.10

From which it is seen that, for every train mile run, the Great Northern habitually earns a great deal more money than does Northern Pacific, and also spends considerably more.

## III.

The Great Northern's low ratio of operating expenses, in connection with its comparatively small freight density, and gross earnings per mile, has always been a source of wonder to railroad men, who have not examined the operations of the company closely. Yet, we see from foregoing tables, that for every train mile run (and no better "co-efficient" of operating expenses is obtainable than this), Great Northern has spent more than Northern Pacific, with its larger freight density, and gross earnings per mile.

We may compare the operating expenses per train mile on the two roads for two years back in detail as follows, classifying the items.

	North. Pacific.		Great North.	
	1893-4.	1894-5.	1893-4.	1894-5.
Cond'g t'rs-				
p'tation .	59.4c.	57.7c.	57.8c.	54.8c.
M'nt'n'ce of				
way .....	28.4c.	26.5c.	31.7c.	29.4c.
M'nt'n'ce of				
eq'pm't ..	14.5c.	15.4c.	15.3c.	14.6c.
G'n'ral ex-				
penses ...	6.6c.	10.3c.	11.6c.	11.2c.

Total ....	\$1.08.9c.	\$1.09.9c.	\$1.16.4c.	\$1.10.0c.
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Notice that Great Northern's "maintenance" items in 1893-4 were 47 cents per train mile, against 42.9 cents in the case of Northern Pacific, and in 1894-5 they were 44 cents, against 41.9 cents on Northern Pacific. Clearly, therefore, we cannot accuse Northern Pacific of undue extravagance any more than we can accuse Great Northern of undue economy.

In point of fact, the figures given above show clearly that Northern Pacific is not in trouble, because it is spending more money on its road in the running of a train mile than Great Northern is spending. On the contrary, if anything, the figures go to prove that Northern Pacific is spending rather less on its road, in proportion to the work done by the machine, than is Great Northern. Evidently, there is no saving to be effected in this way, and we must look elsewhere for leakage. We cannot for a moment suppose that Great Northern is spending any more money on the running of a train mile than it can possibly help.

We must, therefore, examine somewhat the items that bear directly on the gross revenue resulting from the running of a train mile. Clearly there are two, and two only, viz., the amount of freight or passengers hauled and the amount received for each ton of freight or each passenger.

We have seen, already, that Northern Pacific receives rather a larger rate per ton per mile than does Great Northern. The difference is not extremely important, but it is in Northern Pacific's favor. The following table, however, sheds a flood of light on the problem, and really contains the key to the solution. It shows the average number of tons of freight hauled per "freight train mile" in the case of both roads:

	Northern Pacific.	Great Northern.
1890-1.....	137	196
1891-2.....	147	202
1892-3.....	152	235
1893-4.....	144	227
1894-5.....	163	237

Here is the secret of Great Northern's success, in face of adverse conditions which brought down the Northern Pacific. Looking at it in another way, we show the gross revenue per freight train mile as follows:

	Northern Pacific.	Great Northern.
1890-1.....	\$2.02	\$2.43
1891-2.....	2.10	2.49
1892-3.....	1.90	2.89
1893-4.....	1.64	2.54
1894-5.....	1.84	2.45



Thus, while Northern Pacific lost between 1891-2 and 1893-4 no less than 46 cents per freight train mile, Great Northern gained 5 cents for every freight train mile run. There is no reason why it should cost more to run a freight train one mile now than it did five years ago. Most of the items of cost, indeed, should be smaller, if anything. Assuming, however, on the basis of last year that \$1.10 represents the present cost of running a train mile on both roads, we see from the foregoing that it costs Northern Pacific 0.675 cents to haul one ton of freight one mile, while it costs Great Northern 0.464 cents to do the same thing.

Clearly, therefore, although Northern Pacific has spent no more money in running one train mile than Great Northern, it has spent 0.211 cents, or 31 per cent., more for every ton hauled one mile. We may safely assume that Northern Pacific has been in this way 30 per cent. more extravagant than Great Northern. It is just this 30 per cent. that has broken Northern Pacific, and it is just this 30 per cent. that has to be saved, at least in part.

Can all or any part of it be saved? That is the question of all others that concerns Northern Pacific security holders. Suppose, for purpose of argument, that Northern Pacific had been operated last year as Great Northern was operated. Suppose that the 0.211 cents per ton had been saved—what would have been the result?

Operating expenses would have been reduced by no less than \$2,483,800, which would have increased net earnings by that amount and brought them up to almost \$8,600,000. This seems startling and almost impossible, yet it is absolutely correct, and follows logically from the figures which we have seen.

How much of this \$2,483,800 can be saved?

# THE CASE AGAINST CONSOLIDATION

## IV.

We have now arrived at the conclusion that Great Northern has been enabled to live and make progress, in the depression that ruined Northern Pacific, only because it economized, while Northern Pacific was wasteful. In short, it saved on train mileage, which Northern Pacific failed to do.

From what we have seen, moreover, it is clear that, although Northern Pacific has saved to some little extent, it has never been operated on so economical a basis in this respect as has Great Northern. Evidently, the main thing to be done with the property is to bend all energies and efforts in the direction of saving train mileage. How is this to be done?

There are three factors which enter into the question of increasing the average train load. These are:

- (1) Efficiency of road-bed and track.
- (2) Efficiency of equipment.
- (3) Good management.

A heavy train load requires a good track with heavy rails, strong bridges, good ballast and sound ties; a powerful locomotive with capacious freight cars, and such an adjustment of accommodations to shippers' requirements as shall give the largest possible amount of freight to a given train. The utmost tact and vigilance are required for this test, and, probably, good management is the most important factor in the problem at any and all times.

Taking first the matter of equipment, it can be said with some confidence that Northern Pacific is thoroughly well equipped. All railroad men who have ever ridden over the Northern Pacific know that at one time the equipment of the road was fine to the verge of extravagance, and there is no doubt that it is in good shape to-day. It cost a great deal more originally than did Great Northern's rolling stock, although, probably, the latter road has more modern locomotives as far as age goes. The following table illustrates the relative position of the two roads on a per mile basis and in proportion to the business done:

	Northern Pacific.	Great Northern.
Loc'm't'vs (per m'l of r'd)...	.141	.101
Pass cars (per mile of r'd)...	.095	.084
Fr'ght cars (p. m. of r'd)...	4.01	3.46
Freight density per car....	14.7 tons.	20.7 tons

From this it would seem that Northern Pacific is really better equipped, at all events as to numbers, than Great Northern. Evidently it cannot be lack of rolling stock that is responsible for the lower train load on Northern Pacific. It is not reasonable to suppose that all its locomotives are light or old-fashioned, and its freight cars of small capacity. The average carload, however, on Northern Pacific is over two tons less than on Great Northern.

As to "roadbed and track," which includes all that appertains thereto, viz., bridges, culverts, etc., the reports of Northern Pacific do not give a great deal of information. The first matter, however, is that of the grades, and the following tables give some figures bearing on the relative profiles of Great Northern and Northern Pacific:



# NORTHERN PACIFIC.

	Max.	Total	Total	
	Grade.*	Do.*	Ascent	Ascent
	Miles.	W.	E. (ft.)	W (ft.) E.
St. Paul—Glendive	666	53	53	5,459 4,093
G'nd'e—Livi'gst'n	341	26	26	2,668 250
L'v'gst'ne—Hel'na	123	116	116	1,714 2,269
Helena—Jocko ...	169	116	116	2,451 3,874
Jocko—Ellensb'g.	485	53	53	3,459 4,455
Ellen'b'g—Tac'ma	125	116	116	1,386 2,889
	<hr/> 1,909	<hr/> 116	<hr/> 116	<hr/> 17,137 17,830

\*In feet per mile.

## GREAT NORTHERN.

St. Paul—Minot..	530	32	32	2,064	1,204
Minot—Pac. Jn...	435	32	32	2,015	1,061
Pac.Jn.—Kalispell	261	53	105	4,457	4,028
Kalispell—Spok'n	251	79	79	2,340	3,417
Spokane—Everett	305	116	116	4,429	6,277
	1,782	116	116	15,305	15,987

## NORTHERN PACIFIC.

	Miles.	Average ft. per mile.	Average ft. per Mile
St. Paul—Glendive.....	666	8.2	6.1
Glendive—Livingstone.	341	7.8	0.7
Livingstone—Helena...	123	14.0	19.0
Helena—Jocko.....	169	14.6	22.9
Jocko—Ellensburg.....	485	7.1	9.1
Ellensburg—Tacoma...	125	11.0	23.1
Total .....	1,909	8.9	9.3

## GREAT NORTHERN.

St. Paul—Minot.....	530	3.9	2.2
Minot—Pac. Junc.....	435	4.6	2.4
Pac. Junc.—Kalispell...	261	17.0	15.4
Kalispell — Spokane...	251	7.3	13.3
Spokane — Everett....	305	14.5	20.5
Total .....	1,782	8.5	8.9

Clearly Northern Pacific has much the worst of the grades especially in the mountains and west of the Cascades. It is very difficult for any one not extremely familiar with the property to estimate, in dollars and cents, the amount of saving that can be obtained by a reduction in grades. As far back, however, as February, 1893, the report of the special committee, of which President Ives was chairman, states that the General Manager (then Mr. Mellen) and Chief Engineer Kendrick estimate that an expenditure of \$3,000,000 in reducing grades would bring them down all along the line (except in the mountains) to a maximum grade of 26 feet to the mile, and that this would result in an annual saving of \$750,000.

An opinion such as this is entitled to respect. There is an inherent probability about it, moreover. Take next the question of rails. The report of ex-Receiver Rouse made in December, 1893, contains an estimate by the General Manager that there are needed for the main track, to replace old 56-lb. rail, some 1,073 miles of 66-lb. rail and about 384 miles of 80-lb. rail for the mountain districts. Doubtless, money could be advantageously expended in this way, as also on ballast, of which the General Manager considers necessary about \$555,000 worth. It is questionable, however, if the light average train load can be charged against the rails or ballast to any important extent. Doubtless bridges have counted for more in this matter than rails, ties or ballast, and grade more than bridges, although all of them would count very much if not dealt with in time.

It seems as if the grades are the most important factor so far. If Northern Pacific is ever to haul a really large train load on an average, these must be reduced as soon as possible. One might say in regard to the rest that they can probably wait.

# WALL STREET TO-DAY

## Latest News From All the Money Markets of the World.

### THE CASE AGAINST CONSOLIDATION

(V.)

Before dealing with the third and perhaps most important of all factors in the question of "train loads," viz., good management, it is well to stop for a moment and consider the chief and only real important argument for consolidation that can for one moment be considered by the Northern Pacific as of any moment.

Northern Pacific has a desirable reputation among shippers and travelers in the Northwest. It is undoubtedly fair to say that it captures the largest share of strictly competitive business from Great Northern at points where the roads compete. Shippers prefer the road because they say that it gives better facilities than does Great Northern, and because it is more accommodating to their wants and wishes. This point would hardly be disputed by even the most zealous officers of Great Northern.

There is, however, only too great reason to suppose that the policy of golden spikes, extravagant rolling stock and other things of the same kind, which were so much affected by Mr. Villard's management in the old days, still finds expression in the form of overanxiety to please shippers, and consequently in wasteful train mileage. It is utterly impossible for any one not conversant with all the details of Northern Pacific business to estimate, even in the roughest possible way, how much business is captured from Great Northern, because Great Northern will not make the same terms as to time of delivery of freight, etc., as Northern Pacific will make. That some business is taken from Great Northern in this way there is hardly room for doubt. That a good deal is so taken is very probable.

Now, the Great Northern would like to consolidate the Northern Pacific with its own road, because the stress of competition being removed, it would naturally gain some business. It says also, with perfect truth, that Northern Pacific would gain considerably on other business, because it would be able to haul it most economically, and without being compelled to make unbusinesslike concessions in order to secure it. The basic idea of a traffic agreement would be some such division of business as would secure to each road its own share of competitive traffic, and it is quite safe to presume that the proposed "traffic agreement" was designed to cover this very point. Now, the answer to this is two-fold.

In the first place, the "London agreement" gives to the Great Northern a majority of the new capital stock of Northern Pacific, carrying complete control, in return for a guarantee that net earnings shall not fall below \$6,200,000. We have seen that Northern Pacific, operated last year as Great Northern was operated, would have earned \$8,600,000 net. In view of the paucity of the guarantee, and the magnitude of the consideration therefor, and in view of what we have seen in a general way as to conditions of business in the Northwest, it seems clear that it would be a very simple matter for Mr. Hill to conduct the two roads, so that Great Northern would benefit enormously, and Northern Pacific would benefit so far that the guarantee would never be needed. Further, does any one suppose that it would be long before Northern Pacific grades would be reduced, its rails renewed, its bridges replaced—all out of Northern Pacific earnings after the absolutely fixed charges under the reorganization?



No one can deny for one moment that consolidation would result in great economies on both roads. The essential point is that the fee to Great Northern is much too heavy, because Great Northern would be much the larger gainer.

We go further, and say that consolidation is not at all necessary for the physical regeneration of Northern Pacific and for economy in train mileage. Northern Pacific can do a great deal in this way of itself.

Suppose that it is in the habit of making concessions to secure business from Great Northern, at competitive points. Suppose that it secures two or three car loads by a promise that they shall be delivered in a certain time at a certain place, Great Northern refusing to take them on these terms, and that as a result the train pulls out with ten or a dozen cars, when a short delay would give five or six or eight cars more. Probably as a result of this sort of thing, freight agents at other points are in the habit of giving away concessions, just because the system prevails generally on the road.

It is most certain that Northern Pacific is even now giving away a great deal more than it need in this respect. What is needed is a general stiffening of backbones all along the line, and a system of the closest inspection and vigilance over trifles. The engineer that drops a car or two from his train and leaves them on a side track should be a marked man; the engineer who has the best average tons of train mile should be rewarded; the freight agents should be in constant touch with the yardmasters—there must be a hundred ways of bracing up the system. If the grades are reduced on Northern Pacific, the rails renewed and the bridges strengthened, there is no reason on earth that man can see why 200 tons should not be the average train load.

That would have given last year 37 to 40 cents more revenue for every train mile run, or, rather, would have reduced the train mileage by about 18 per cent.