## FROM A PROFESSIONAL BOND APPRAISER.

WHEN the vice-president of a big New York trust company tells how he judges the value of railroad bonds, it is a good time for the investor to listen. The lecture given by Mr. George Garr Henry before the New York Y. M. C. A. West Side Branch is reprinted in the *Ticker Magazine* for last month.

No mystery is involved, says Mr. Henry. "Any man of experience in the business world can easily determine the degree of security which attaches to any particular railroad bond, provided he has two documents; viz., the mortgage and the trust deed which describes the property covered by the mortgage, and the last annual report which gives the financial condition of the property."

The mortgage is to show whether your principal is secure; the report of earnings to show whether your income is secure.

Security of principal follows three factors: (1) The dollars of bonds per mile of road as compared with the amount some one would have to spend to build a competing road; (2) the dollars of bonds whose claim comes before your claim, and (3) the dollars of bonds whose claim comes after yours.

The first point is thus illustrated by Mr. Henry, in a manner to show how closely finance is linked with common-sense:

Say a road is down South somewhere,—take the road that runs from Birmingham to Atlanta. You ask, "How much did the road cost?" The answer is, it is bonded for $25,000 per mile.

You say, "I do not want any of these bonds; the Atlantic Coast Line, which is a very profitable property, is only bonded for $20,000 per mile. If they build a road at $20,000 per mile, I do not believe I want the other bonds. I would rather have the Atlantic Coast Line's."

Another anecdote shows the workings of the second and third factors:

I was talking with a very successful bond buyer of one of the large insurance companies a while ago about the International & Great Northern Railroad, which went into the hands of a receiver.

I said, "Mr. So-and-So, haven't you some of those bonds?"

"Yes," he replied.

"Losing any sleep over it?"

"No, not a bit," he answered.

"Why, how is that? I thought you had the Thirds."

"No," he said, "I have the Seconds."

He was not losing sleep because the third-mortgage bondholders, in order to protect their interests, would have to "buy him in." He would get par for his bonds. It makes a great difference to bondholders whether there is anybody else behind them in a foreclosure.

When it comes to earnings, a lot of comparisons with other roads are needed. The important point is *net* income,—what is actually available to pay interest after the employees' wages and the bills for rails, ties, engines, and so forth have been paid. But if the road has not been patched and repaired sufficiently, the net earnings can be made to look larger than they ought, because that "maintenance" must be paid for some day.

A little scrutiny here will pay, because the net income, says Mr. Henry, "is what you have to consider. The average road is earning a little more than twice its interest charges. To put a bond in the first investment class it should earn anywhere from two to three times its interest charge."

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## THE NEWS ABOUT UNION PACIFIC.

THEY say Mr. Harriman never laughs. If anything does upset his savage concentration it ought to be the wordy wars engaged in by the newspaper writing and reading public whenever the name of the slight, stooping, hard-working president of the Union Pacific is prominently mentioned.

Many investors do not wish to question the personal conduct of Mr. Harriman, or of any one else, but still feel concerned. Shall they sell their Union Pacific stock? They don't want personalities, they want facts; but find it hard to get them.

No wonder. Last month the press fairly hummed with "U. P." news. On the 16th it was announced that $154,583,500 of different railroad stocks were held in Mr. Harriman's name. The meaning of this is perfectly plain to the youthful financial reporter who has just "seen Harriman," who writes under the impact of the mighty imagination that directs steel tracks by the thousand miles, dollars by the hundred millions. Clearly, the news merely hints at the genius of "our great constructionist" as a railroad general and a trustee for other people's money.

But on another page of the same newspaper one could read testimony from the Government's suit to split Mr. Harriman's vast structure at its very keystone,—the Union Pacific-Southern Pacific merger,—as in restraint of trade. Hence, something far different is "perfectly plain" to many serious and honest editorial writers and readers. And no one can doubt the sympathy on this point among those who travel and ship over the 24,637 miles of railroads directly managed under Mr. Harriman, and the 59,708 miles more dominated or largely influenced by him. No matter how good its service, a railroad is apt to fall under suspicion if its rates are fairly high.

To swing back to the other side: the two groups of railroads have 44,103 and 96,222 stockholders, respectively. Most of these more or less immediate partners of Mr. Harriman have been getting their dividend checks right along, and at rates above the average. They resent and ridicule the attacks made by editors of sensational papers.

But the latter, after all, are human and want to keep their jobs. They will hardly miss such a chance to dangle spooks like "blind pools," "stock gambling machines," "gigantic engines of speculation" before the startled reader's eye. So few public men can be called "freebooter," "spider," and even "incubus" who, like Harriman, will not answer back!

On the other hand, technical and responsible journals do not go far enough. For instance, the first *Railroad Age Gazette* of last month analyzes and admires the U. P.'s magnificent earnings as a railroad. But it feels the wisdom and righteousness of its grip on other railroad companies to be a question outside the field of the practical railway man.

This second problem is indeed discussed, both pro and con, by the London *Statist* and *Economist*. But they make no comment at all on a third point, not to be ignored, that although Mr. Harriman's companies show results satisfactory to their stockholders, the United States Government objects to some of their methods.

Can we not briefly get at the facts of record on these three questions, from original and coldblooded sources?

### (1) HARRIMAN AS A RAILROAD MAN.

The easiest thing Harriman admirers do is to point to the contrast between these different years' earnings *from operation* of the Union Pacific Railroad:

| Fiscal year. | Miles operated. | Operating revenue. |
|---|---|---|
| 1898 | 5,325 | $33,281,125 |
| 1908 | 5,781 | 76,039,225 |

The figures tell the story. An increase of less than 9 per cent. in mileage, but more than 128 per cent. in earnings! (And these earnings are independent of some $16,000,000 additional received in 1908 from "investments.")

To Mr. Harriman is conceded the plan and the achievement. His ideas were intensive. The Union Pacific has been made a *through* railroad. He concentrated on his main lines. In those eleven years he spent more than $123,000,000 in straightening and leveling the road, double-tracking it, buying it the finest engines and cars and other equipment, ballasting it, and making it the show road west of the Mississippi, and perhaps east, too.

Meanwhile he ran it up to concert pitch. He could put his finger on big men or little things. One day he might be discovering a genius like Julius Kruttschnitt to handle his traffic, or another like J. C. Stubbs to get it, and the next day he might be noticing the smallness of the water tank pipe which a Union Pacific fireman was adjusting on to his locomotive tank,—while the train waited. Mr. Harriman was not satisfied with the excuse that "all the pipes on the line were just that size." He ordered them enlarged. Several minutes were saved whenever a locomotive took water. The cash difference to the U. P. during the next year figured up to something like $300,000.

### (2) MORE FROM INVESTMENTS THAN FROM OPERATION.

Yet Mr. Harriman's conduct in railroading tells only half the story to the stockholder. The situation is unique.

Suppose the reader owned last year one share of Union Pacific stock. He got $10 in dividends. This seemed conservative, since he could cipher that his share of the profits of the company was $16.23.

Now less than $8.04 of this was from transportation operation. The more than $8.19 balance was from "other income,"—mostly from the dividends of shares owned by the Union Pacific in the profits of companies *not operated by itself*.

In other words: Mr. Harriman's wisdom as head of an investment concern would seem even more important to the purchaser of Union Pacific stock than Mr. Harriman's efficiency as a railroad man.

Why is this enormous amount of stock held? Answers are as many and various as on the problem of a protective tariff. No use to discuss them without getting two pictures in mind, eleven years apart.

About 1898, the Union Pacific Railroad was a wretched fragment of 1800 bankrupt miles. It stretched from Omaha to Ogden,—the former on the Missouri River, the latter by the shores of Salt Lake.

Now it was not to work up small local business between these interior points, through a raw country, that the Kuhn-Loeb syndicate had raised $81,500,000 cash to pay off the United States Government and the other mortgagees of the scandal-stricken line.

BETWEEN THE DEVIL AND THE DEEP SEA.

No,—what the U. P. needed was *through business*. And in this respect it lay between the devil and the deep sea.

The latter could be reached from Ogden only over the Southern Pacific, the weapon of the rich "Huntington crowd." The part of the devil was played at Omaha by a group of the old guard of American railroads,—the Missouri Pacific, Northwestern, St. Paul, Burlington, and the Rock Island,—all so powerful as to have fought their way through the '93 depression.

Hemmed in, the Union Pacific would take through traffic on other roads' terms, or do without. If the Southern Pacific did not like its rates eastward, it could route the freight itself through New Orleans. The St. Paul or the Northwestern could hand westbound freight over to the Northern Pacific at St. Paul.

Even after the syndicate had made its first reach,—buying lines that ran to Kansas City on the southeast and Portland to the northwest,—things were not much better. The "devil" was again personified at Kansas City by the Atchison, Alton, Great Western, and Wabash. And here again, it was the Southern Pacific which met the U. P. at Portland,—the "deep sea,"—and which held the line to San Francisco, the Pacific port of greatest consequence.

Into the foreground of this scene entered about 1899 Mr. Harriman, whose membership in the U. P. crowd had up to then been inconspicuous. Then the fighting began. We must pass by several of the biggest railroad deals and wars in history. In each case the spoils of battle were the stock certificates of some other road,—the kind that carried the votes.

As a result, we have the second picture, lightly sketched by the following exhibit from the Union Pacific's latest report. It is entitled "Investment Stocks Owned":

| Description. | Shares held. |
|---|---|
| Atchison, preferred | 100,000 |
| Baltimore & Ohio, common | 323,342 |
| Baltimore & Ohio, preferred | 72,064 |
| Chicago & Alton, preferred | 103,431 |
| Chicago & Northwestern, common | 32,150 |
| Chicago, Milwaukee & St. Paul, common (old) | 13,400 |
| Chicago, Milwaukee & St. Paul, common (new, 65 per cent. paid) | 32,725 |
| Chicago, Milwaukee & St. Paul, preferred (new, 65 per cent. paid) | 18,450 |
| Great Northern, preferred | 35,786 |
| Great Northern ore certificates | 77,164 |
| Illinois Central, common | 201,231 |
| New York Central, common | 142,857 |
| Northern Pacific, common (old) | 1,128 |
| Northern Pacific, common (new, 62½ per cent. paid) | 18,016 |
| Northern Securities stubs | 7.249 |
| Railroad Securities, common | 34,829 |
| Railroad Securities, preferred | 19,359 |
| Southern Pacific, common | 900,000 |
| Southern Pacific, preferred | 342,000 |

At the present time of writing these stocks are worth about $300,000,000. And that isn't all the story.

Look at the first item,—100,000 shares of Atchison. Consider it together with the fact that U. P. bankers and directors are on record as owning 300,000 shares more,—a total of 17 per cent. of the voting stock of the Atchison Railway. When this road exchanges traffic with others at Kansas City, let us say, will it escape the fact that more than one-sixth of its common stock is owned by one particular railway,—the Union Pacific? From testimony now coming out in the Government's suit it would seem safe to answer No.

Something similar could be said for many other items on the list.

Then consider that the Northwestern is practically the western end of the New York Central; that the B. & O. controls the Reading and through it the Central of New Jersey; and that the Georgia Central is owned outright by E. H. Harriman.

Is it not plain that one can trace the course of a freight car under Mr. Harriman's control, command, or influence all the way from Portland or San Francisco or Chicago or New Orleans to New York or Philadelphia or Baltimore or Savannah,—and back again?

ARE THE INVESTMENTS AN UNMIXED BLESSING?

The bitterest opponents of the U. P.'s "investments" grant their traffic advantages. Some even find points of wisdom financially. Though objecting strongly to the stockholdings on other grounds, the *Evening Post* does believe that "an annual income of $16,765,000 would prove an anchor to the windward for any railroad during a stringency in the money market. By far the strongest point, however, is the independence obtained by the ownership of $316,725,740 free assets in bonds and stocks, a large part of which is made up of what is called high-grade stock market collateral."

Some critics, however, ask why the Union Pacific sold a whole lot of bonds,—$97,000,000,—during the year ending June 30, 1908, when hundreds of millions of its money were held in stocks quoted at much less than they had cost it.

A reply made by the *Wall Street Journal* shows that the Union Pacific at least did better than most other railroad companies could have done during August, 1907, in borrowing money at only 4.6 per cent.

Then comes the "final analysis," favored by supporters of Cæsar, Napoleon, and Harriman,—that the plan succeeds,—that this railway-investment company made more money during the depression than many roads managed in the old-fashioned way. The trouble with such reasoning is that it covers the past more than the future of the Union Pacific.

Thus the London *Economist:* "It is at present the most successful mixture in the world of transport and stock-dealing. But its success depends on the personality of one man, and not without reason are its securities ranked among the most speculative in the American market."

The usual criticism seems to lie in the feeling that Mr. Harriman has gone too far,—that a railroad ought to stick to its knitting,—that this $300,000,000 investment ought to go back into more machinery of transportation, directly or indirectly.

"The function of a railroad corporation should be confined to the furnishing of transportation," declared an Interstate Commerce Commission report. A couple of years ago there were about 50,000 square miles of territory in the State of Oregon alone, surrounded by Harriman lines, undeveloped,—"while the funds of those companies which could be used for that purpose," the Commerce Commission complained, "were being invested in stocks like the New York Central and other lines having only a remote [illegible] to the territory in which the Union [illegible]ystem is located."

[illegible] this is only poetic justice, and may-[illegible]ounded on permanent business principles,—that the money received from railroad earnings should go back to help the growth of the sections that supplied those earnings.

(3) STOCK PROFITS AND PUBLIC POLICY.

Whether or no the "investments" continue as profitable as the operations, their plan may change perforce.

A year ago a suit in equity was filed by the United States Government at Salt Lake City, alleging that the Union Pacific by the purchase of the Southern Pacific and the San Pedro, Los Angeles and Salt Lake, otherwise known as the Clark road, as well as by stockholdings in the Atchison, Northern Pacific, and Great Northern, had stifled competition in transcontinental business and created a monopoly in violation of the Sherman law.

Some of the testimony in this case was first hand and important. Witnesses like E. T. Jeffery, president of the Denver & Rio Grande; Stuyvesant Fish, former president of the Illinois Central; Edward P. Ripley, president of the Atchison, bore witness that there was less competition or no competition between the "Union" and the "Southern" at certain points west of the Mississippi.

The Southern Pacific stock now held by the U. P. is worth some $150,000,000. This belongs to the U. P. stockholders. If the Government wins, will they lose? The *Wall Street Journal* thinks not, on the basis of precedent:

> To take the most pessimistic view of this litigation, Mr. Hill and his stockholders in the Northern Securities case merely swapped the black certificates of the Northern Securities for the red and green of the Northern Pacific and Great Northern, and the control remained in *statu quo*.
>
> If forced, the Union Pacific could do somewhat likewise; or, better still, the stockholders of the Union Pacific could vote to distribute the stock among themselves, a feasible plan, and simultaneously vote to transfer it to Mr. Harriman and two or three other trustees, the latter to give the stockholders certificates of beneficial interest in the stock. Here, too, control would remain in *statu quo*.

Only lawyers and history can answer the question whether Mr. Harriman is great and good, or merely great. That he makes money for his tens of thousands of stockholding partners, and that he or his successors may reasonably be expected to continue the same scale of profits, may be the conclusion of the unsentimental investigator.