Erie in Promising Position

Results of Bernet management should begin to show with installation of new power—Dividend possibilities

UNQUESTIONABLY, the Erie has today the most promising prospects that it has ever had at any time in its long and checkered career. Whether the promises are sufficient to justify the present high quotations on Erie stocks might be a fair question. Those who are willing to pay these high prices evidence their confidence in the ability of the Van Sweringens to make money even in Erie. Van Sweringen control has meant Bernet management and no doubt there is a general expectation that J. J. Bernet will prove able to make the Erie prosperous with the same skill he showed in transforming the Nickel Plate from a second rate property into one of the leading factors in the traffic situation and the railroad strategy of trunk line territory. It is possible that the values of Erie stocks are also increased a few points by the hope that the Interstate Commerce Commission will allow the Chesapeake & Ohio to acquire control of the Erie as planned in the present merger proposals.

The Erie has three issues of stock, first and second preferred and common. The first preferred has had a price range thus far in 1927 between 52⅜ on January 4 and 66¼ on August 4 and is now selling at about 62. The second preferred has closely paralleled it with a price range between 49 and 64½ and is now selling at about 61. The preferred issues are both 4 per cent non-cumulative. If the dividends were being paid the prices would give a yield of 6½ per cent. A large number of the stocks of industrial companies paying dividends of $4 a share sell on the stock exchange at the present time at prices below these non-dividend Erie preferred issues. The common stock reached its 1927 low on January 3 with 39½. It had a high price on September 30 of 69¾ and is now selling not far from the last named figure. At one time in 1922 this stock could have been bought at 7. In 1923 it had a price range between 10⅛ and 22¾; its high in 1926 was 42.

The Erie is controlled by the Van Sweringens through the Vaness Company and the Chesapeake & Ohio. The Erie stock controlled by the Chesapeake & Ohio is all held by a subsidiary company known as the Virginia Transportation Corporation and the Chesapeake & Ohio has been given an option which allows it to purchase—the Interstate Commerce Commission being willing—all of the Erie stock held by the Vaness Company. The holdings were as follows, on May 1, 1927:

Number of Shares

	Common	1st Preferred	2nd Preferred	Total
Owned by Chesapeake & Ohio	357,300	137,405	50,495	545,200
Optioned	345,239	23,695	22,305	391,239
Total	702,539	161,100	72,800	936,439
Total outstanding	1,124,819	479,044	160,000	1,763,863
Per cent owned	31.8	28.7	31.5	30.9
Per cent optioned	30.8	4.9	14.0	22.2
Total	62.6	33.6	45.5	53.1

The common stock owned was acquired at an average cost per share of $38.58 and the option calls for a price of $34.50.

Bond Conversions

From the figures given above, it will be observed that the Erie's total outstanding stock on May 10, 1927, totaled $176,386,300. The amounts have been slightly changed since by the conversion into stock of series D, 4 per cent convertible bonds which had the privilege of conversion in a ratio of $100 of bonds into $200 par value of stock until October 1, 1927. The total of these bonds outstanding in the hands of the public on December 31, 1926, was $19,627,100 and all but $309,200 were converted. The amount of common stock outstanding was, therefore, increased by $38,635,800 and is now $151,117,700.

The Erie this year sold $50,000,000 5 per cent refunding and improvement mortgage bonds, the issue being offered to the public at 94½. The proceeds were used to

Erie, Operating Results, Selected Items

Years ended December 31, 1916 and 1920 to 1926

	1916	1920	1921	1922	1923	1924	1925	1926
Average mileage operated	2,257	2,259	2,309	2,309	2,325	2,325	2,323	2,317
Total operating revenues	$74,311,262	$122,163,099	$113,428,076	$106,874,103	$132,978,455	$119,090,856	$118,543,456	$125,473,504
Total operating expenses	53,453,701	133,014,159	106,117,042	100,101,523	108,070,145	95,784,775	93,238,535	99,173,496
Net operating revenues	20,857,561	Def. 10,851,060	7,311,034	6,772,580	24,908,310	23,312,081	25,304,920	26,300,008
Railway tax accruals	2,220,333	3,804,226	3,729,593	3,863,226	4,260,303	4,521,873	4,750,791	4,868,271
Railway operating income	18,628,600	Def. 14,690,442	3,531,754	2,860,993	20,539,117	18,698,549	20,509,435	21,386,470
Net equipment and joint facility rents—Dr.	2,147,414	2,303,676	2,369,860	2,216,082	2,218,704	1,626,372	2,978,815	3,333,748
Net railway operating income	16,481,186	Def. 1,319,953	1,161,893	644,911	18,320,413	17,072,177	17,530,619	18,052,723
Dividend income	2,042,420	3,842,942	9,191,700	11,095,150	6,027,537	7,002,537	3,177,537	5,913,995
Gross income	22,382,830	*18,516,983	*16,815,729	11,854,444	23,111,730	24,781,924	21,698,418	24,927,371
Interest on funded debt	10,361,415	10,610,358	10,701,403	10,771,533	10,532,553	11,079,862	10,945,520	10,781,715
Net income	6,027,664	4,438,586	2,694,425	Def. 3,132,770	8,435,273	9,601,629	6,729,307	10,113,393
Sinking and other reserve funds	881,920	976,015	1,099.171	946,047	1,217.065	1,238,262	1,146,915	1,368,901
Surplus for year	4,631,912	3,462,570	621,452	Def. 4,078,817	7,218,208	8,363,367	5,582,391	8,744,493
Earnings per share on common stock	$1.85	$0.83	None	None	$4.14	$5.16	$2.69	$5.50
Revenue ton-miles (thousands)	9,770,367	11,137,692	8,574,212	8,277,801	11,363,377	9,880,513	9,469,280	10,407,368
Rev. pass. miles (thousands)	628,395	740,129	683,422	648,421	680,537	666,139	672,065	650,594
Rev. per ton per mile (cents)	0.584	0.862	1.065	1.021	0.957	0.966	1.000	0.980
Total revenue tons	44,359,341	46,467,928	34,692,317	36,301,364	50,437,718	43,104,928	42,894,577	46,680,845
Tonnage of bituminous coal	8,636,187	12,036,731	6,959,744	7,797,689	11,534,424	8,343,217	8,334,899	8,856,584
Per cent of total	19.47	25.90	20.06	21.48	22.87	19.36	19.43	18.97
Tonnage of anthracite coal	9,312,088	9,988,829	9,973,687	6,079,508	11,557,800	10,026,306	7,392,567	10,178,531
Per cent of total	20.99	21.50	28.75	16.75	22.91	23.26	17.23	21.80
Transportation ratio	38.55	56.60	46.53	45.46	38.59	38.69	38.52	38.45
Operating ratio	71.93	108.88	93.55	93.66	81.27	80.43	78.65	79.04
Per cent net railway operating income to total operating revs.	2.22	......	1.02	0.60	13.78	14.33	14.79	14.39

*Includes standard return and guaranty.

retire $20,299,450 6 per cent collateral trust notes, a $10,000,000 short term note redeemed one year prior to maturity and current bank loans. The financing had the advantage of clearing up all of the Erie short term indebtedness and important maturities of funded debt until 1930. The road's funded debt now stands at $213,298,600 in addition to which there are outstanding some $20,000,000 of equipment trust obligations. The stock outstanding now totals $215,021,100. The total capitalization is about $440,000,000 of which the funded debt, inclusive of the equipment obligations constitutes 52 per cent, which proportion would not be so bad if the Erie could only show greater earning power.

It was a feature of early Erie history that it promptly went into receivership in every period of severe financial stringency. In recent years the Erie has shown some improvement. It earned something on the preferred in 1921 but nothing on its common. In 1922, it reported a substantial deficit and since then has been able to report earnings per share on the common stock after allowance for the unpaid and fortunately noncumulative 4 per cent preferred dividends and after allowance for sinking and other reserve funds, as follows: 1923, $4.14; 1924, $5.16; 1925, $2.69, and 1926, $5.50.

General Characteristics

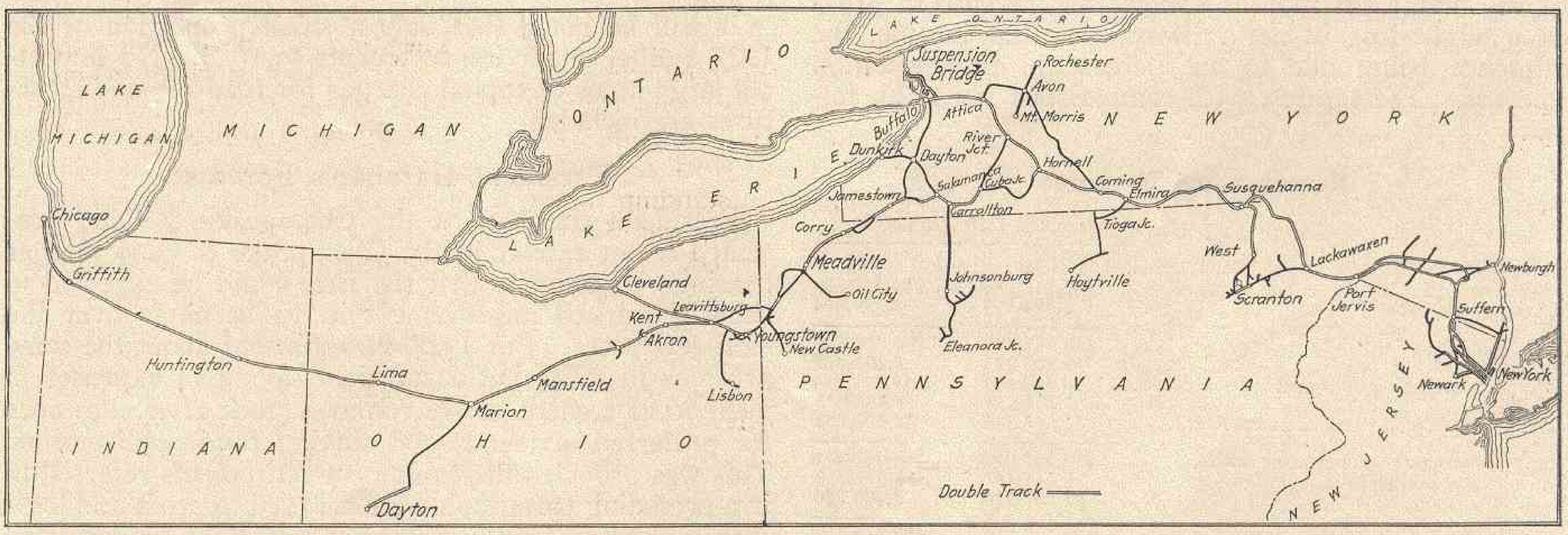
As a railroad, the Erie had been handicapped by its lack of financial strength and inability to secure capital for important capital improvements. The road is generally regarded, however, as being well operated. It has at least had enough net income to allow it to expend large sums for equipment, for improvements of track structure to support heavy equipment, for signals, etc., and its shops are such that one of the reasons offered in favor of the merger with the Chesapeake & Ohio is that the latter will be able to use Erie shop facilities for the repair of its power. It is, however, likely that in future years the Erie will find it necessary to expend large sums for grade crossing eliminations in New York state and in the thickly settled suburban area in northern New Jersey and at other points as well as for more adequate stations, etc., all representing that sort of expenditures that yield less net return per dollar expended. Some idea of the Erie's ability to find money to spend out of earnings or by means of equipment trust obligations is given in the brief tabulation of capital expenditures during the past four years shown in the first column on this page. The budget for 1927 calls for an expenditure of about $28,000,000; the greater part of which will be for equipment.

Year	Road	Equipment	Equipment: Less credits	Equipment: Net	Total
1923....	$3,203,711	$18,097,517	$8,637,803	$9,459,714	$12,663,425
1924....	4,022,080	13,323,846	4,222,123	9,101,724	13,123,804
1925....	4,638,795	4,089,040	4,451,739	Cr. 362,699	4,276,096
1926....	4,545,222	4,567,677	2,374,374	2,193,302	6,738,524
	$16,409,818	$40,078,080	$19,686,039	$20,392,041	$36,801,849

Traffic

The Erie, as befits its location in trunk line territory, has a diversified traffic. The most important commodities handled are coal and California perishables. In 1926 bituminous coal constituted 19 per cent of the total tonnage, a good portion of which was received from connections. Bituminous coal may be expected to become a more important item of Erie tonnage on account of the community of interest with the Chesapeake & Ohio. The tonnage received from the Chesapeake & Ohio via Hocking Valley at Marion has expanded sharply since the completion of the Chesapeake & Hocking and is reported now to average about 100 cars daily.

The Erie handles also a large volume of anthracite coal, this commodity totaling in 1926, 21.8 per cent of the total tonnage. This coal is received principally from the Erie's own coal subsidiaries which include the Pennsylvania Coal Company; the Hillside Coal & Iron Company, etc. (The Erie owns five coal companies, two of which operate bituminous mines.) The coal operations yield not only traffic but substantial sums in the form of dividends. The Erie purchased the Pennsylvania Coal Company in 1901 at a price of $40,000,000 and the company has been estimated by one competent authority to have a present value of $60,000,000 and all five companies a value of $84,000,000, while others estimate the values to be as high as $150,000,000. The value of $84,000,000 is equivalent to $56 a share on the amount of Erie common stock at present outstanding. The coal properties yield substantial sums in dividends, the average annual receipts from this source having totaled about $4,100,000 in the 16½ years ended December 31, 1926. The dividend receipts from the coal companies in 1926 totaled about $5,500,000 which was equivalent to over one-half the Erie's total net income.



The Erie Railroad

Handles Perishable Freight

The Erie handles much the larger proportion of the California perishable freight moving between Chicago and New York, although recently the Pennsylvania, which is also especially equipped at New York on account of its large tonnage of Florida perishables, has succeeded in obtaining about 20 per cent of the business. The Erie has on occasions complained that it receives an inadequate division of the rate from California points and the fact that the traffic moves in refrigerator cars, on which mileage payments must be made, does not help the situation. The Erie, however, solicits the business assiduously and leaves nothing undone to give prompt third morning delivery at the New York end.

Rate Structure

The Erie appears to suffer as relates to its rate structure. Its average receipts per ton-mile in 1926 were only 0.980 cents. These compared with the New York Central's 1.051 cents; the Pennsylvania's 1.024 cents; the Lackawanna's 1.31 cents and the Lehigh Valley's 1.156 cents. This helps explain, therefore, the relatively poor ratios of operation and the general lack of earning power which is an Erie characteristic. In 1926, the road had a transportation ratio of 38.45; an operating ratio of 79.04 and its ratio of net railway operating income to total railway operating revenues was 14.39 per cent. The eastern district in 1926 reported a transportation ratio of 35.6; an operating ratio of 74.8 and a net railway operating income ratio of 17.8 per cent.

J. J. Bernet has been president of the Erie since January 1, 1927. He has not been in charge of operations a sufficient length of time to have effected improvements sufficient to show marked changes in the earnings or operating statistics. The latest earnings report—that for the first eight months—shows an increase in gross but a slight loss in net railway operating income, the difference being due to an increase in transportation expenses. The figures, with comparisons for 1926, follow:

Revenues and Expenses

	January 1 to August 31	
	1927	1926
Freight revenue	$65,816,296	$64,638,524
Passenger revenue	8,404,915	8,799,074
Total, including other revenues	$80,961,699	$80,207,888
Maintenance of way	9,903,233	9,893,467
Maintenance of equipment	19,542,891	19,877,644
Traffic	1,394,854	1,385,075
Transportation	31,843,526	31,001,231
Total, including other expenses	$65,717,322	$65,130,478
Net operating revenues	15,244,377	15,077,410
Taxes	3,380,580	3,400,200
Railway operating income	$11,844,638	$11,643,383
Net railway operating income	9,111,882	9,491,662

New Power

One of the first things that the new management did, however, promises to prove of utmost importance in the Erie's future economy of operations. It announced a budget for 1927 of some $25,000,000 of which about $22,000,000 was for new equipment. The latter includes 50 new 2-8-4-type freight locomotives, 30 switch locomotives, 50 new passenger train cars and 25 caboose cars, as well as the equipping of 125 present Mikado locomotives with mechanical stokers and feed-water heaters. The 50 new road freight locomotives are just going into service. Half of them are being supplied by the Lima Locomotives Works; they were described in the *Railway Age* of October 8. The other half are being furnished by the American Locomotive Company and a description of them will be found on another page of the current issue. The locomotives have been put in service between Marion, Ohio, and Meadville, Pa., 203 miles and between Marion and Hornell, N. Y., 477 miles, respectively, and are already showing marked economies in train-load, train-speed and fuel consumption which will be reflected in due course in the operating statistics and in the transportation and operating ratios.

Equipment Retirement

At the same time, the budget called for the retirement of 327 old locomotives, 270 passenger cars, 4,765 freight cars and a sizeable amount of work equipment. It is noteworthy that none of the freight cars are to be replaced. The total book value of the equipment to be retired will be $8,400,101. The Erie is desirous of charging off the amounts in excess of the accrued depreciation to profit and loss but if the Interstate Commerce Commission should not permit this there will have to be a substantial charge to retirements and operating expenses, namely about $4,900,000, which, if made, will very likely have an adverse effect on the price of Erie stock. The retirement program is already nearly carried out. On January 1, 1927, the Erie reported the ownership of 1,456 locomotives but on September 1, 1927 it reported only 1,217. On September 1, also, it reported that 21.1 per cent of its power was held for repairs as against only 13.3 per cent on January 1. The number of locomotives stored in serviceable condition on September 1, 1926, was 234, on January 1, 1927, 131 but on September 1, 1927, only 14. This equipment situation does not look promising but, of course, the entire situation is changed by the delivery of the 50 new road freight locomotives and also the 30 new switch engines.

It will be noted that only a small proportion of the 1927 budget is for improvements to road. No important large items of capital charges for roadway and structures are included.

President Harahan's Forecast

President Harahan of the Chesapeake & Ohio presented as an exhibit in the Chesapeake & Ohio merger hearings an estimate that the Erie could be expected to show a marked improvement in its earnings over the next few years. For 1927, he estimated about the same gross as in 1926, but a sufficient saving in expenses to yield $6.95 a share on the common stock after allowance for preferred dividends and sinking fund requirements. This was provided the equipment retirements referred to in a preceding paragraph were charged to profit and loss; if they were charged to retirements in 1926, he estimated the 1927 per-share earnings at $1.93. He expected a progressive improvement each year following and 1931 results of $14.00 a share; an operating ratio of but 72.6 and a transportation ratio of 36.5. For each year he allowed a dividend income of $5,304,000 as against the $5,913,995 actually received in 1926. If Mr. Harahan's estimates of per-share earnings were adjusted to the basis of the amount of common stock outstanding since the conversion of the series D bonds, his 1927 estimate would become about $5.17 a share and his 1931 estimate about $10.40. Earnings in 1926 actually were $5.50 on the former capitalization which would be equivalent to $4.10 on the present common stock outstanding.

THE CHICAGO, MILWAUKEE & ST. PAUL is now distributing to the public a folder entitled "Flashes" which contains information of general interest regarding railway problems. The issue for October calls attention to the taxes which the railroads pay back to the public and discusses railway electrification, showing the number of miles in operation and the number of miles in the United States.