

# Warren Buffett, Railroads and Virginia

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The financial world has been all a twitter since Berkshire Hathaway moved to acquire all of the outstanding stock of the Burlington Northern Santa Fe Railway, a transaction which closed on February 12. The fact that legendary investor and folk hero Warren Buffett would make such a bet on a railroad is pretty amazing to some. Railroads have long been cited by many of the investment elite as a type of business to be avoided. More remarkable yet, Buffett split his "B" shares fifty-for-one, a game-changer in terms of Wall Street now that Berkshire has been added to the S&P 100 index.

Has the old man gotten out of his groove? He says "no", that this is an "all-in" bet on the future of America; reflecting his bullish view on the economic future of our nation. In numerous articles since written about Buffett and the BNSF, the oracle of Omaha repeatedly asserted that as America prospers, so will BNSF. Let us hope so. If one were going to purchase a railroad, Burlington would be a good pick -- a fine company, with good management, a great franchise, and reasonably-assured profitability for the years just ahead. But will it be a good fit in Berkshire's portfolio long term, after the novelty of owning a huge slice of the U. S. rail industry has subsided?

In times past, would-be railroad barons have consistently underestimated the huge requirement for capital investment to sustain their lines. Except for occasional good years, the Class I rail freight companies are notorious for not earning their cost of capital.

Coal represents about 45% of all tons of freight originated by U. S. railroads, and BNSF originates more of it than anybody else. Years ago, an old industry sage, who knew both the coal business and railroading, observed that if you had a profitable coal franchise you could play around with running a merchandise operation (now largely represented by what is termed rail "intermodal"); otherwise you were likely to be out of luck! Intermodal (trucks on rail) is the other large chunk of BNSF business. There are major changes afoot in both coal and intermodal, which at this point are hard to assess insofar as Burlington is concerned. But it is interesting that Buffett is reported to have said, on "The Charlie Rose Show", that: "We will wean ourselves off of coal over time and we should". Matt Rose, CEO of BNSF, would almost certainly disagree.

Why should any of this be of particular concern to Virginia? Because the tectonic plates of U. S. railroading are still shifting. Rarely does a shift occur (read as rail mergers) but that the impact is felt here in the Commonwealth. And rarely has such an event brought lasting benefit to the Old Dominion. Right now, we are fortunate to have a railroad headquartered in Virginia that is just as good as, or even perhaps a tad better than, BNSF. That of course would be Norfolk Southern. If Buffett can provide BNSF CEO Matt Rose sufficient cover and resources to build

intermodal to the next level, that would be great. On the other hand, if BNSF gets spun off after a period of disillusionment, or if somebody in Omaha, or Ft. Worth, attempts to put NS and BNSF together, then that could be problematical for Virginia. It could also be positive. We should stay on top of the Berkshire railroading story.

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