United States Department of Agriculture
Agricultural Marketing Services
1400 Independence Avenue, SW
Room 3071-S, STOP 0201
Washington, DC 20250-0201

Benefits from the DM&E Rail Expansion

The Dakota, Minnesota and Eastern Railroad (DM&E) operates 1,100 miles of rail line in Illinois, Iowa, Minnesota, Missouri, Nebraska, South Dakota, Wisconsin and Wyoming. In 2005, DM&E transported 34,000 railcars of farm products, 10,300 railcars of food products and 4000 railcars of ethanol. DM&E connects with its sister railroad, the Iowa, Chicago & Eastern Railroad (IC&E), in Minnesota; IC&E transported 38,200 railcars of farm products, 24,600 railcars of food products and 6,000 railcars of ethanol in 2005. In 2006, the DM&E expects to transport 39,000 railcars of farm products, 9,000 railcars of food products and 4,500 cars of ethanol. The IC&E expects to transport 40,000 railcars of farm products, 28,000 railcars of food products and 9,000 railcars of ethanol in 2006.

Since 1998, USDA has supported the expansion of the DM&E into the Powder River Basin in Wyoming and the reconstruction of its existing rail lines. In comments to the Surface Transportation Board (STB), USDA acknowledged that the DM&E project could provide cost savings to agricultural producers that use its services. Cost savings could accrue to producers as the result of the DM&E project's potential to:

- Preserve and expand rail competition,
- Increase railroad efficiency for shippers, and
- Improve grain producer access to other markets.

The presence of effective rail-to-rail, rail-to-barge, or rail-to-truck competition is necessary to stimulate lower rail rates for shippers. When effective competition is present, rail rates are much lower. Generally, savings from lower transportation costs go directly to agricultural producers.

The number of competing railroads in Minnesota and South Dakota can affect rail rates and railroad efficiency. In Minnesota, DM&E mainly competes with Union Pacific and Burlington Northern Santa Fe Railway (3-railroad competition). But in South Dakota, DM&E's only major competitor is BNSF Railways (2-railroad competition). Past USDA research (1987-1989) measured the effects of competition upon rail rates.

When compared to markets where there is only 1 railroad:

- rail rates for shipping corn fall by 18% when 2 railroads compete,
- rail rates fall by an additional 11% when 3 railroads compete, and
- rail rates for shipping wheat and soybeans also decline with more rail competition, though not to same extent.[a]

Based on these conditions, the rail rate savings for 2-railroad competition would be $0.15 per bushel for corn. For 3-railroad competition, there could be an additional $0.09 per bushel saved. These savings are estimated using first quarter 2006 average BNSF rail rates for corn of $0.81 per bushel.

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[a] James M. McDonald, "Competition and Rail Rates for the Shipment of Corn, Soybeans, and Wheat," Rand Journal of Economics, Vol. 18, No. 1, Spring 1987.

Grain Producer Access to Other Markets

In 1998, USDA first supported the concept that the DM&E project could increase grain producer access to other markets. At that time, most of the DM&E's agricultural traffic was hauled to the Mississippi River for transloading onto barges[b]. But DM&E was unable to provide year-round service since the river is frozen during the winter months. DM&E was also unable to provide efficient rail service to Pacific Northwest (PNW) markets – mainly due to worn track conditions and restricted train speeds of 10 miles per hour. However, since that time, the DM&E has acquired the IC&E line. Today, the DM&E railroad has free access to a number of critical destinations, including Chicago, IL, Kansas City, MO, Minneapolis, MN, Great Lakes ports, and the Mississippi River. The combined DM&E and IC&E has also been able to successfully eliminate what are known as "paper barriers" which would restrict the interconnection with other railroads.

Effects on Farm Program Payments

Under the 2002 Farm Bill, farm program payments may also be reduced as a result of higher prices paid to crop producers due to increased rail competition. Grain producers are eligible for two types of farm program payments that could be reduced if increased rail competition increases the price producers receive for grain. These two types of payments are counter-cyclical payments and marketing assistance loan payments.

Counter-cyclical payments – occur if the national average price for a crop, such as corn, falls below the target price set under the 2002 Farm Bill. For corn, counter-cyclical payments were triggered for both the 2004 and 2005 crops. If increased rail competition boosted the price received by corn producers in Minnesota and South Dakota by the amounts presented earlier, these higher prices would raise the national average price received for corn by about $0.01 per bushel. For the 2004 and 2005 crops, this increase in the national average price received for corn would have reduced counter-cyclical payments paid to all corn producers by as much as $75 million in each of those years, saving taxpayers $150 million. Put another way, increased rail competition could potentially reduce counter-cyclical payments for corn by $75 million per year, if corn prices in the future are similar to prices in 2004 and 2005.

Marketing assistance loan payments – occur when the local market price (called posted county price or PCP) for a crop, such as corn, falls below the crop's loan rate established under the 2002 Farm Bill. In this situation, a producer can elect to repay the marketing assistance loan at the PCP, receiving a payment equal to the difference between the loan rate and the PCP. Based on the conditions described above, increased rail competition leading to higher prices paid to corn producers served by the DM&E could potentially reduce marketing assistance loan payments for corn by as much as $165 million, if corn prices in the future fall below the loan rate.

Based just on our analysis of what additional rail capacity would mean as a result of the DM&E upgrade project, for just one of the crops (corn) that is eligible for federal farm program

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b Industry experts, at that time, believed that increased efficiency and access to PNW and processor markets, in addition to the benefits of preserving rail competition, could add as much as $0.20 per bushel to the price corn and wheat producers received.

payments, the federal government could save roughly $240 million if counter-cyclical and marketing assistance loan payments are made in the future. These savings to the federal government could be greater when factoring in other crops such as wheat, oats, soybeans, oil seeds, grain, and sorghum.

Other Benefits

- Provide savings for energy consumers by reducing transportation costs for coal.
- Create new ethanol and biofuels production opportunities with more efficient rail transportation.
- Reduce the cost of inputs used by farmers through the movement of anhydrous ammonia and other agricultural chemicals by rail.
- Reduce highway congestion by taking trucks off the roads. This will mitigate damage to roads and bridges that are already in "fair to poor" condition.
- Create a safer railroad with more modern tracks, signaling, and communications systems.
- Create new higher paying jobs for the region that will boost the rural economy.
- Preserve a regional railroad vital to rural communities that otherwise may be lost.