

Reuters

FEATURE-DM&E seeks funding for rail to supply coal, ethanol

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By Nick Carey

SPRINGFIELD, Minn., June 30 (Reuters) - In a region where disintegrating farmhouses are a grim reminder of the departure of families who once scratched a living from the earth, business leaders are pinning their hopes on an ambitious new rail project.

Cedar American Rail Holdings Inc. has plans for a new \$6 billion line for its Dakota, Minnesota & Eastern Railroad that would bring coal east from the Powder River Basin in Wyoming. It would also move more grain and ethanol from places like Springfield, which is 130 miles southwest of Minneapolis.

But the privately held company needs \$2.5 billion in U.S. government funding, and the proposed rail faces opposition from one of the cities in its path.

Roger Vaske, manager at the Harvest Land Cooperative grain facility, said upgrading the rail link would create jobs and halt the exodus from his community.

"This could keep us in the game for another 25 years," he said as he looked toward the grain silos by his office.

Vaske said the proposed project, the largest U.S. rail construction in a century, is also why privately held biofuel company US BioEnergy Corp. may build a Springfield plant requiring 37 million bushels of corn a year to produce 100 million gallons of ethanol. Vaske's plant handles 16 million bushels a year.

The plant would employ more than 40 people, and Vaske said it would give the region a boost by increasing local demand for corn.

"We must stop rural America bleeding," he said. "People want to come back, and they need jobs to come back to."

US BioEnergy declined to comment but pointed to DM&E's line in an April press release on the potential ethanol plant.

VeraSun Energy Corp. <VSE.N>, which went public on June 14, has two ethanol plants near DM&E's line and is building a third.

U.S. demand for coal and ethanol is soaring, but supply is tight. As a result, utilities and ethanol producers are eager for Cedar American to lay track..

A new line would boost coal supplies and provide competition for Union Pacific Corp. <UNP.N> and Burlington Northern Santa Fe Corp. <BNI.N>, the two U.S. railroads serving the basin now,

said Fitch Ratings analyst Stephen Brown.

Neither railroad would comment on the issue.

Analysts and the project's few opponents say Cedar American has not provided details on how to fund the project and repay a government loan if one is granted.

The Federal Railroad Administration is assessing the railroad's \$2.5 billion loan application, and spokesman Steven Kulm said the agency could not say how long that would take.

EIGHT YEARS AND WAITING

Sioux Falls, South Dakota-based Cedar American wants to lay 262 miles of new track into the vast coal field, upgrade much of its 2,500 miles of existing track, and buy locomotives and rolling stock. It would be the biggest U.S. rail project since a 1909 link from Seattle to the Midwest.

Cedar American Chief Executive Kevin Schieffer said the line could carry 100 million tons of coal annually, plus 50 million tons of other commodities.

Cedar American began touting the new line in 1998 to supply utilities with low-cost, low-emission coal from the Powder River Basin.

Rising natural gas prices have encouraged utilities to seek cheaper coal as an alternative. Meanwhile, demand for corn-based ethanol has spiked after U.S. refineries began using it to replace water-polluting MTBE, or methyl tertiary butyl ether, as an additive to gasoline.

Cedar American has also grown, doubling in size when it bought the Iowa, Chicago & Eastern Railroad in 2002, and now serves much of the Midwest.

"A combination of (our) larger network, plus rising demand for coal and ethanol has created the perfect storm for us," Schieffer said.

He said coal mines and utilities have become more interested in the line because of problems Union Pacific and Burlington Northern have bringing enough coal out of Wyoming to meet demand. Coal companies in the Powder River Basin even helped plan DM&E's proposed route, Schieffer said.

Vic Svec, spokesman of St. Louis-based Peabody Energy <BTU.N> which mined 125.7 million tons of coal in the basin last year, declined to comment on Schieffer's statement.

"But we support all investments in rail capacity to bring more coal to the market," he said.

William Berg, chief executive of La Crosse, Wisconsin-based Dairyland Power Cooperative, welcomed the project saying it would ease delivery problems and lead to lower prices for the utility's 575,000 customers.

But not everyone is happy. Rochester, Minnesota, home to the renowned Mayo Clinic and on

DM&E's network, has fought the project, citing safety and pollution concerns. The clinic even commissioned a study saying that Cedar American could not afford to repay the government loan if the line is built.

Schieffer dismissed Rochester's claims, saying the city does not have financial data to back them.

Analysts agreed that assessing the line's viability is difficult because Cedar American has not provided that data.

"In theory it's a good project," said transportation analyst Tony Hatch of ABH Consulting in New York, "but until we see some numbers it's impossible to tell for sure."

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