



# **CN's Aquisition of the EJ&E: A Political Economy Analysis**

Christopher Berry  
Ethan Bueno de Mesquita

The University of Chicago

# Is there really a political economy of trains?

- Policy, including transportation policy, is the outcome of a contest between competing interests
- As a result, only part of the policy-making process is about cost-benefit analyses and the merits
- Political economy is about the other part

# CN and the EJ&E

- CN has proposed to acquire the EJ&E
  - Reroute trains around Chicago
- Positive Externalities
  - Regional and national economic, environmental, and security benefits
  - Reduced rail traffic in Chicago neighborhoods (including ours) and some suburbs
- Negative Externalities
  - Increased rail traffic in some suburbs
- Resulting in a politically charged regulatory process with uncertain outcome





## A thought experiment: 2 scenarios

- Suppose railroads own the right to run as many trains as they want
- Suppose people of Barrington have the right not to have trains run if they choose not to
- In the absence of government intervention, would the number of trains running through Barrington be different under two scenarios?

We are from the University of Chicago,  
shouldn't the market solve this?

**Coase Theorem:** In the absence of transaction costs, if property rights are well defined, then if there are two competing interests, even in the presence of negative externalities

- Outcomes will be efficient
- The ultimate outcome is invariant to the initial assignment of property rights



# The Logic of the Coase Theorem

- Efficiency
  - If property rights well defined, one party can compensate the other
- Invariance
  - Through efficient bargaining the more profitable activity should always occur
- Suppose net benefits
  - If CN own rights: Then run trains
  - If residents own rights: CN compensates them
- Suppose net loses
  - If CN owns rights: Residents pay CN not to run (or buy EJ&E)
  - If Residents own rights: No trains run

# Why Might the Coase Theorem Fail

- Unclear property rights
- Large transaction costs
- More than two parties
- Credibility/Commitment problems
- An empirical example of failure:
  - <http://nissan.com/>
- When Coase Theorem fails, market fails to solve problem
  - Public policy should try to approximate Coasian outcome



# Principles of good policymaking

- The social good is hard to define
- One uncontroversial notion is Pareto Efficiency
  - Policy A Pareto Dominates Policy B if A makes at least one person better off and no one worse off
- Hard to find such policies, since all policies seem to have winners and losers
- If a policy is positive *on net* we can create Pareto Efficiency (Hicks-Kaldor)
  - Adopting good policies and compensating the losers



# Is the CN Acquisition Hicks-Kaldor Efficient?

- Winners (in order of directness)
  - Owners of CN and the EJ&E
  - 1.25 million residents of city neighborhoods
  - 1.2 million suburban residents with reduced traffic
  - The region and nation
- Losers
  - 900,000 suburban residents with increased traffic
- So why isn't easy to get approval with compensation?

# Politics of Regulatory Approval

- In principle non-elected boards (such as STB) are insulated from politics
- In practice, not so
  - Career ambitions
  - Various forms of pressure
- Who can effectively exert pressure
  - Those who are mobilized
  - Those with clout

# Comparing the Winners and Losers: Clout

- CN
  - Large corporation with lobbying presence
  - Not U.S. owned
- City Residents that Benefit
  - Median income: \$46,000
  - Demographics: 70% minority
- Suburban Residents that are Hurt
  - Median income: \$76,000
  - Demographics: 67% white



# Comparing the Winners and Losers: Mobilization

- Suburban opponents more mobilized.  
Why?
  - **Opportunity Costs:** South Side city residents have bigger issues to petition their government on, suburbs may not
  - **Prospect Theory:** People tend to be more motivated by losses than by gains
  - **Size of Effects:** We haven't quantified the per person gains and losses, but draft EIS makes them look roughly equal

# Evidence of undue influence from opponents

- 7 “scoping meetings” to assess costs and benefits
  - 6 in suburbs
- 39 poster locations announcing those meetings
  - 38 in suburbs
- 22 minority outreach meetings
  - 21 in suburbs
- 8 meetings to take comments on draft EIS
  - 7 in suburbs
- State-level leadership has not supported the plan

# What's the likely outcome

- If you looked at this *ex ante* you'd think the combination of corporate and city interests would win
- CN was late to understanding the politics
- Suburbs are highly mobilized
  - Congressional delegation has proposed legislation
- The outcome is highly uncertain
  - No guarantee good policy will be good politics