

Concessions demanded by Electromotive (Caterpillar)

There are 465 CAW Members at EMD

The employer has demanded the following concessions....

\$21 million annually reduction in wages and time off per year.

\$1.5 million dollars per year in benefit cost reductions.

\$6.9 million dollars cut out of Pension and Retiree benefit costs

\$10 million dollars out of the SUB fund.

The savings listed above would be gained by concessions the employer has tabled in the following areas:

A wage reduction for all classifications. The deepest cut is \$18.50 per hour for about 50% of the workforce.

Elimination of the Defined Benefit Pension Plan

Elimination of retiree benefits

Substantial reduction in shift premiums

Elimination of COLA

Reduction in overtime compensation

Elimination of 4 holidays annually

Elimination of vacation of between 64 and 120 hours of vacation time

Elimination of survivor income benefits, income maintenance plan, SUB plan, SWW protection, maternity top, retiree medical, retiree life insurance etc...

25% co-pay for the cost of premiums of medical, drug, dental, vision, hearing aid coverage

25% co-pay at time of purchase of the cost of drugs

Major reduction in dental and other benefit coverage amounts

Elimination of protection of skilled trades work

Electro-Motive Diesel and Progress Rail Services

The Acquisition:

On June 1, 2010 it was announced that Progress Rail Services, a wholly-owned subsidiary of Caterpillar, would buy EMD for \$820 million. The move came just five years after EMD was spun off from GM to private equity groups Greenbriar and Berkshire Hathaway (the details were not disclosed at that time, but that deal was reported to be worth “less than \$500 million”).

While it is not surprising that private equity firms would eventually sell EMD, this move is a fairly bold push into new territory for the purchaser. Generally speaking, the sale has not generated much commentary in the media, other than to acknowledge the transaction.

However, those few analysts that have ventured an opinion highlight that Caterpillar has in fact been building their presence in the railway industry over the last few years, and that this is a part of a logical expansion. In fact, the release announcing the sale highlights that Caterpillar has invested some \$2 billion in rail activities since 2006.

Caterpillar has added locomotive manufacturing capacity, in Muncie Indiana (after receiving millions of dollars in state aid. Caterpillar recently announced they would build a new facility in Brazil and they have contracted with Bombardier to build Locomotives in Mexico.

Progress Rail Services:

Founded in 1982 and based in Albertville, Alabama, Progress Rail Services is essentially in the “service” side of supporting the rail industry, rather than being an operator of railways, or a manufacturer of railway equipment. Their main business operations revolve around MRO activity (maintenance, repair and overhaul), both of rail equipment (locomotives and rail cars), and track (switching equipment and rail beds.)

Presently, the company has 110 “facilities” in U.S., 28 in Mexico, 4 in Canada and 1 in Brazil which range in size from major overhaul shops to much smaller repair shops.

In terms of getting a detailed look at the company’s operations and finances, we do not have much access to information. Progress Rail Services originated as a privately-held company, became a division of another private company in 2000 (Progress Energy) and was then sold to private equity investors in 2005 (One Equity Partners) for a reported \$405 million. Private companies do not have to publicly report detailed financial and operational information.

Caterpillar bought Progress Rail Services in 2006 for \$1 billion, marking their entry into the railway industry. Progress Rail Services has been maintained as a wholly-owned subsidiary, keeping their management and operational structure somewhat independent from Caterpillar, but it is clear who the boss is at the end of the day. Caterpillar owns 100% of Progress Rail Services, and ultimately it is just another division of the much larger global giant.

Even though Caterpillar is a publicly-traded company, which means we have all sorts of information on the whole company, Progress Rail Services is such a small part of the overall company (less than 5% of revenue), that they do not report separate information.

The only financial details available on Progress Rail Services date from 2005 when estimates of their revenue were reported while it was sold to equity investors. At that time it was estimated to have annual sales of \$1.2 billion. A separate report from 2008 noted that they had about 4,800 employees worldwide.

We are not entirely strangers with Progress Rail Services within our union. We have a bargaining unit of about 45 people in Winnipeg with the company as part of Local 101. I don't have the full history on it, but my understanding is that Progress Rail Services obtained some of our work from Canadian Pacific Railway back in the mid-1990s, and there has been a long back-and-forth about flow rights between the operations. In the broadest sense, it appears that Progress Rail Services grew historically across North America largely as a means for railways to outsource much of the MRO activity that had traditionally been done in-house (...likely with lower wages and fewer unions).

Although Progress Rail Services has no history in locomotive manufacturing, or manufacturing generally, they obviously are in the rail industry (unlike private equity firms). And most important for our concerns, EMD has been bought by someone in it for the long-term as we are now part of the equipment manufacturing giant, Caterpillar.

The Caterpillar Empire:

Best known for its construction and excavation equipment, Caterpillar is a world-leader in the equipment industry. Founded in 1925 and headquartered in Peoria, Illinois, the company had revenues of \$32 billion last year (a bad year), and some 95,000 employees in 50 countries worldwide.

While North America still accounts for the largest share of sales, Caterpillar has become much more global in recent decades. Among the company's 237 separate manufacturing plants, 102 are in the U.S., and 135 are elsewhere in the world.

In terms of where we fit it, what is somewhat unique about Caterpillar is that when they make acquisitions they appear to largely leave the structures alone. Many companies purchased by Caterpillar are not simply merged into existing operations, but continue to exist as “A Caterpillar Company” (the tag-line we see under the logo for Progress Rail Services).

At present there are some 23 separate subsidiaries within the Caterpillar empire, including Progress Rail Services, but also such varied operations as Anchor Coupling (hoses), Balderson (tools), Hindustan (loaders in India), Prentice (forestry machinery), Solar Turbines (generators), Wealdstone (military vehicle support and parts), and more.

In terms of expanding their rail-related business, Caterpillar is using Progress Rail Services as their umbrella. It is somewhat odd that they would report that Progress Rail Services was buying EMD, and many reporters appropriately headlined their stories that Caterpillar was buying EMD (which is much more accurate).

Being part of a publicly-traded global manufacturing giant has its upsides, including their desire to expand their rail business, manufacturing experience, global reach, access to capital and more. However, when it comes to getting specific information on the performance of Progress Rail Services (before and after the addition of EMD), there is not much available.

Caterpillar does not report separately for its subsidiaries, and only reports financially on three broad categories of “Machinery,” “Engines,” and “Financial Products,” and by very broad geographic regions (e.g. North America, Asia-Pacific, etc.). Being a small division within a much broader company is typical for Canadian operations. It means that we will be able to take a look at the overall performance of the company, and make some broad estimates of how “our” operations are doing – but it will not be detailed.

By my quick calculations, after the addition of EMD’s roughly \$2 billion annual revenue (a level expected in more normal times) to Caterpillars’ “Engine” division, EMD operations will only represent about 15% to 20% of divisional revenue (and less than 5% of Caterpillar’s overall revenue).

If we can’t take a close look at Progress Rail Services, then let’s look at the larger picture. How is Caterpillar doing? Overall, the company is doing quite well compared to other manufactures. They were hit incredibly hard during the downturn in 2009 as construction took a nosedive, and commodities (mining, oil and gas, forestry) took a steep slide. But they are seeing some recovery these days, and the outlook for the year ahead is much better. A few key numbers:

Caterpillar, Revenue and Net Profit, Actual and Estimates, 2007-2011		
Year	Revenue (\$billions)	Net Profit (\$billions)
2007	\$45.0	\$3.5
2008	\$51.3	\$3.6
2009	\$32.4	\$0.9
2010 <i>forecast</i>	\$38.1	--
2011 <i>forecast</i>	\$44.0	--
<i>Source: Capital IQ</i>		

Although revenue plunged by 37% last year, Caterpillar actually managed to make a profit (slim, but a profit nonetheless). Compared to other manufacturers during the economic crisis, this is no small feat. A recent survey of analysts shows an average forecast for an 18% increase in revenue this year, and another 15% in 2011 – bringing the company’s revenue back to more historical levels.

In their latest quarterly earnings report, the company reported \$233 million net profits in the first quarter, and they upgraded their revenue forecast for the year to range between \$38 to \$42 billion. As the global economy slowly recovers, the main drivers of their core business (construction and commodities) will certainly lead to better times overall.

Investors have looked favourably on Caterpillar throughout these turbulent times. Although the company’s stock took a deep hit in early 2009 (along with the rest of the stock market), they have actually recovered most of the loss as their stock price has doubled in the last year. And compared with the Dow Jones Index, or the S&P Index, Caterpillar is doing much better. A longer term look over the last five years shows Caterpillar stock appreciating by 40% during this period, compared to the Dow and the S&P remaining essentially flat.



The top of the house at Caterpillar is doing quite well. Even though he had to take a pay cut in 2009, CEO J.W. Owens still managed to scrape by with \$8.75 million in total compensation last year (down from peak pay of \$17.1 million in 2007). With Mr. Owens' 5-year pay packet totalling \$43.2 million, things can't be too bad at Caterpillar.

In 2010 the top 8 executives were paid \$67,645,404 .
 In 2010 Retired Chairman/CEO received more than \$22 million dollars in compensation including \$16 Million dollars in restricted stock.

Despite their strong performance, Caterpillar has a legendary and nasty history of interaction with unions. You will recall that the UAW waged an epic battle against Caterpillar in a 17-month strike that ended largely in defeat in 1996 (a deeply concessionary 6-year agreement was eventually reached in 1998). And since then Caterpillar has not let up. A subsequent round of difficult bargaining in 2004 resulted in a narrowly-accepted settlement containing more concessions, a two-tier wage system and another 6-year agreement.