Railroaded: The Transcontinentals and the Making of Modern America (2011)

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The work of historian Richard White has long been considered among the most innovative around, whether he is writing about the environment or Native Americans, or using the resources and possibilities of digital history to get students and scholars alike to think about the importance of geography, distance, and the space in between things. But his book on the expansion of U.S. railroad networks across the continent to the Pacific touched a number of nerves, proving highly controversial. Instead of seeing the men whose companies built and operated the transcontinental railroads as heroes who linked a continent together, he seemed to depict them as scam artists who convinced investors, the tax-paying public, and government officials to hand over the equivalent of billions of dollars in financing for railroads that could never be profitable. Is he being unfair? Or do these railroad tycoons sound all too familiar?

This selection begins with the 1884 arrival of Charles Francis Adams, Jr., the grandson of former president John Quincy Adams, as the president of the Union Pacific Railroad. The Union Pacific had completed the first intercontinental railroad in 1869. Not long afterward, it was revealed that the Union Pacific had bribed numerous congressmen, who in return helped the railroad issue bonds underwritten by the federal government. Many other financial shenanigans followed, and by 1880 the Wall Street tycoon Jay Gould had emerged as the company's dominant shareholder.

In June of 1884 Charles Francis Adams became president of the Union Pacific Railroad. [. . .] In 1878 he had been named a government director on the board of the Union Pacific and then had rejoined the board as a regular member in 1882. Adams had often been critical of railroad practice, particularly Union Pacific practice. Western railroads issued too many securities, received too little money from them, and, as a result, carried large loads of debt. They were too often corrupt and run for the profit of insiders. Poorly constructed and poorly managed, these railroads expanded too quickly into regions without the traffic to sustain them and duplicated their rivals' tracks where there was traffic. Adams came to the Union Pacific to rescue it. [. . .] Adams knew that he was taking on a "concern [. . .] in bad repute, heavily loaded with obligations, odious in the territory it served." He became president in the midst of the Panic of 1883–84, after workers on the railroad had just forced the management to rescind wage cuts. Congress was demanding the immediate payment of money due. [. . .]

Many of the Union Pacific's problems could be traced back to Jay Gould. [. . .] The Adams family was as illustrious and well-connected as any in the United States; Gould rose from poor beginnings. [. . .] Adams wanted the railroad out of politics; Gould knew that the railroad depended on politics. In some ways, however, Gould and Adams were not so different. [. . .] Both Gould and Adams had the same grim view of western railroads as hopelessly overbuilt, badly managed, and in need of reordering. [. . .] [Adams concluded that] "on any honest basis of capitalization the road would, even at the lowest rate which has ever been proposed, return not only a fair, but a large profit." Jay Gould did not differ on the essentials. In 1887 he rather disingenuously told the Pacific Railway Commission. [. . .] that the Union Pacific "would be all right if it were capitalized on a moderate basis" but that it could not compete with new roads costing $12,000 per mile.

In calling the Union Pacific overcapitalized, Adams and Gould meant that its outstanding securities had a greater par value than its actual assets. Late nineteenth- and early twentieth-century economists made a distinction between actual capital and capitalization. Capital was "tangible assets, such as real estate, rails, locomotives and cars [. . .] good will [. . .] contracts, alliances, and reputation." In short, all the assets of a corporation "intended for continuing productive use." Capitalization, on the other hand, represented the firm's outstanding securities: "the aggregate of this paper certification of value, taken at par."

In a well-run corporation funded debt and other securities—money obtained from stocks and bonds—translated rather easily into capital assets, and overcapitalization signified the acquisition of debt without the parallel acquisition of equivalent assets. The commonplaces of transcontinental financing—the giving away of stock, the selling of bonds at deep discounts, and the insider contracts for construction—virtually ensured that these roads' capitalization was far in excess of their assets. A company with low capitalization could charge lower rates and required less income to pay interest and reasonable dividends than a company with high capitalization. This was the problem that Adams was describing in the case of the Union Pacific, but the real question was how the Union Pacific came to be overcapitalized.

The concept of overcapitalization is now largely unfashionable and a little archaic. The idea of leverage has largely replaced it. Even in the nineteenth century Jay Gould argued that the value of securities, like the value of assets, was simply what people were willing to pay for them. Sometimes it was wise to accrue large debts to acquire assets; sometimes it wasn't. Time and the markets would make it clear whether accruing debt was wise. The issue was one of risk. If you could borrow at high rates and still make a profit with the borrowed money, then you were simply being an entrepreneur, a risk taker, and a person to be admired, not condemned. [. . .]

Jay Gould, widely suspected of looting the Union Pacific, wanted to shift attention elsewhere [. . .] so he told a story that made overcapitalization the story of risk, the monetary cost of a heroic past. When the Union Pacific was built, he told the members of the Pacific Railway Commission in 1887, it paid "as high as $5 or $10 a piece for ties, and the iron rails, I think, cost $300 a ton, and men had to take their lives in their hands to go out there. You know the Indians were after them." With a minimum of 2,640 ties to a mile, Gould conjured up a road whose ties alone cost from $13,200 to $26,400 for each mile built. With iron at $300 a ton, an additional $26,400 would be necessary to build a mile of road. The unassembled, ungraded road—without spikes, wooden trestles, fishbars, bolts, buildings, ballast, and the labor to assemble them—already supposedly cost from $39,000 to $52,800 a mile. Listen to Gould's story, and overcapitalization was simple. [. . .] The reason the railroad cost so much was that such a risky enterprise forced promoters to promise great rewards and pay high prices. Economists in more mundane ways still tell Gould's story. The high cost of capital in the Pacific Railway—the difference between the face value of securities and what people actually paid for them—can be taken as investors' rational calculation of risk.

Gould knew all about risk, but he was also a magician. Like any magician, he sought to create an illusion by attracting spectators'eyes to one thing and away from the action that actually achieved the desired result. Gould told simple stories of a heroic past, not complicated stories about exchanges of paper. Slight, perhaps smiling, speaking softly as he always did, the small, dapper man sitting at number 10 Wall Street testifying before the Pacific Railway Commission told stories and performed railroad finance. . . . Gould drew attention to risk in order to attract it away from fraud. [. . .] That was the magician's trick. It concealed the secret that both he and Adams, in a rare moment of agreement, wanted kept quiet: overcapitalization was more the result of fraud, deception, and insider dealing than of entrepreneurial risk taking. [. . .] Every Union Pacific train carried its consequences, and every Union Pacific customer paid its freight. [. . .] The Associates [financiers and railroad entrepreneurs like Leland Stanford and Collis P. Huntington, who had organized most of the transcontinental corporations and secured various land grants and support for bond issues from federal and state governments], were chimeras able to change form at will, and by changing form, they created value. . . the Central Pacific, the Southern Pacific, the WDC, and others "were but convertible terms with these four or five movers in them, and they were fused constantly one into the other, and there was no distinction. The corporations were the individuals, and the individuals were the corporations. The Associates proffered a deal, went to the other side of the table, put on another set of hats, and accepted the deal. In the books and ledgers of these companies, trades that appeared to be between a wide variety of entities were not what they seemed. [. . .]

If a western Rip Van Winkle had fallen asleep in 1869 and awakened in 1896, he would not have recognized the lands that the railroads had touched. Bison had yielded to cattle; mountains had been blasted and bored. Great swaths of land that had once whispered grass now screamed corn and wheat. Nation-states had conquered Indian peoples, slaughtering some of them and confining and controlling most of them. Population had increased across much of this vast region, and there were growing cities along its edges. A land that had once run largely north-south now ran mainly east-west. Each change could have been traced back to the railroads.

The railroads' initial contribution to conquest and development was their transport of troops and their supplies. Native resistance to Mexican, Canadian, and American state control persisted longest at a distance from the railroads. The world of isolated posts adrift in a native sea gave way to a world where troops concentrated by rail to the places nearest an outbreak to crush resistance. [. . .] But conquering and dispossessing Indians did little for the railroads in and of itself; to generate traffic, western railroads had to induce both producers and consumers to move west. Henry George, Terence Powderly, and other antimonopolists were wrong in thinking that the railroad corporations sought to hold land for speculative profit. The men who managed the railroads recognized that the most profitable traffic came from a thickly settled country of small freeholders. [. . .] Railroads dealt with speculators, but they preferred selling land to small farmers. [. . .] Like so many carnival barkers, railroad publicity bureaus promoted the virtues of the West and cajoled potential settlers to seize the opportunity that the railroads offered. [. . .] Virtually all the big land grant roads invested in publicity bureaus and immigration agencies to attract settlers. [. . .]

That railroads produced settlement is one of two great truths about agricultural settlement in the American West, and it is modified by a second one: somewhere between the 98th meridian and the 100th meridian the possibilities for agricultural settlement narrowed. Here were the semiarid lands of the American steppe. And farther west lay even less promising lands: the most arid sections of the Great Plains, the Rocky Mountains, and then, running south to north, the Sonoran Desert, the high deserts of the Great Basin, the semiarid Columbian Plateau, and, finally, more mountains to the west. Even on the West Coast, only Oregon's Willamette Valley, sections of the Central Valley in California, and parts of the Santa Clara Valley provided the kind of arable agricultural land for which eastern and European farmers yearned. Everywhere else heavily timbered, infertile, or arid lands promised little for small farmers without large investments of labor and capital. Much of the agricultural history of the late nineteenth and early twentieth centuries was simply the attempt of railroad men, boosters, and farmers to extend settlement deeper into the arid regions. [. . .] West of the 98th meridian settlers came relatively slowly and in disappointingly small numbers. [. . .] Between 1880 and 1890 the Sacramento Valley had lost twenty thousand of its natural increase in population. Nevada actually shrank in population after the railroad arrived. Yet over the course of the generation between 1870 and 1900 the cumulative impact of western railroads on the entire region was tremendous. There were 2 million non-Indians in states lying all or in part west of the line of the Missouri River in 1870. The vast majority of them were in eastern Texas, eastern Kansas, and California. In 1900 there were 10.4 million.

It had taken Anglo-Americans roughly two and half centuries to secure the continent up to the Missouri River. They used the railroads to control the remainder in a generation. Canada and Mexico accomplished the equivalents.

[. . .] [But] the equation of progress with growth, wealth, religion, and "civilization" [. . .] are all part of a long line of "say what you will" justifications of what otherwise might seem unsavory episodes in the American experience. In the end there were more Americans, more American things and products, more American churches and more "civilization," and who could argue with that? In the more pedestrian terms of modern social science, the social benefits of the railroads trumped their costs. [. . .] [Yet] The railroads seemed unable to achieve a balance between too much and too little. They enabled farmers and miners to produce far more cattle, wheat, and silver than the world needed. They opened up some of the most productive farmlands in the world and some of the most unproductive. Poverty, as Henry George observed, increased in the midst of progress.

Regional lines in California and the Midwest could have handled most of the productive traffic. Rail lines connecting Chicago, Kansas City, and St. Louis with the lands east of the 98th meridian would have allowed the settlement of the prairies and other lines connecting California and western Nevada with San Francisco Bay would have created a sufficient Pacific rail network. Long before the Northern Pacific and the Great Northern arrived, the Oregon Railroad and Navigation Company had given the Northwest a combination of river and rail transportation that allowed the settlement of the great wheat-raising region of the Palouse.

The development of the rest of the region would have been delayed without multiple transcontinentals, but what would have been lost? Mines that glutted the market for silver? The catastrophes that befell both cattle and buffalo on the Great Plains? The suffering of those who settled lands that could not sustain them all over the West? The calamities that afflicted Indians who lost their land, their way of life, and often their lives?

For Joseph Schumpeter the damage capitalism did was the source of its power. In his famous phrase, "creative destruction was its essence." Schumpeter made the entrepreneur's benefits available in the short term, while society often had to wait for its share. The classic deferred gratification of the bourgeoisie was the farthest thing from the entrepreneur's mind. He wanted great wealth, and he wanted it now. As Schumpeter saw it, entrepreneurs must reap more than they sow so that the children of those displaced by their innovations will eat more than their parents. In Schumpeter the abuses of capitalist enterprises, while real, were always transitory; their achievements, at least in the economic realm, seemingly permanent in that they set the stage for further progress as long as the process of creative destruction was allowed to continue. [. . .] [But] In assessing the social utility of the railroads, I want to include social costs harder for economists to measure. I want to be conscious of the price—not necessarily calculated in losses that markets measure—and to consider who benefited and who lost. The issue facing the transcontinental railroads was a simple one. Having built ahead of demand, they had to create traffic in places where there was precious little to sell. Given their high fixed costs, the railroads could not simply wait for profitable traffic to appear. Hauling something, even at a loss, was better than hauling nothing. In attempting to cut economic losses, the railroads helped create both what might be called dumb growth and environmental catastrophes.

Questions

1. How do you evaluate White's argument that the social cost of the transcontinentals was greater than their benefits?
2. The railroads were private corporations, but they made the argument that without special help from the government—land grants and underwriting of securities, in particular—they would have been unable to create the social good that the railroads represented. Was this plausible?
3. Take another look at White's conclusion. Should we side with Schumpeter, or with White? What if we look at our own time?