Touchbase

April 2014

In This Issue

Visit us at:
www.tealinc.com

Railroads, shippers size up competitive switching proposal at STB hearing

NITL proposed that certain captive shippers located in terminal areas be granted access to a competing railroad if working within a reasonable distance

Railroad & Policy Updates

Railroads and rail shippers continued to cite the pros and cons about the National Industrial Transportation League's (NITL) competitive switching proposal at the Surface Transportation Board's (STB) hearing held Wednesday, March 26. The board also held a hearing on the proposal on Tuesday, March 25.

NITL proposes that certain captive shippers located in terminal areas be granted access to a competing railroad if there is a working interchange within a reasonable distance, perhaps 30 miles.

If implemented, the proposal would create unpredictable traffic flows, reduce high levels of customer service achieved over the past few years and diminish railroads' incentive to keep investing at record levels in critically needed transportation infrastructure, CSX Corp. Vice President of Service Design Cressie Brown testified at the hearing. The Association of American Railroads also testified that the proposal would undermine railroads' investments and impact service quality for shippers.

In CSX advisory councils and through periodic surveys, customers said they need more reliability to grow their own businesses, said Brown, adding that the NITL's proposal "turns back the clock" on resource and infrastructure gains achieved over the past decade.

The proposal also would force railroads, in certain circumstances, to open up their private networks to competitors, creating artificial competition and transferring revenues from railroads to the handful of customers who recommended the proposal, she testified.

"I am very concerned that the proposal will force cars to locations where we do not have the resources or infrastructure to handle them," said Brown. "It is not in the broader public interest to experiment with a forced switching scheme, which would ultimately create less reliable and less cost effective service for our customers."

Read the entire article:
http://www.progressiverailroading.com/federal_legislation_regulation/news/Railroads-shippers-size-up-competitive-switching-proposal-at-STB-hearing--39883

Mechanical Brief with Steve Christian

As someone who spends a considerable amount of time looking at railcars throughout the country, I have noticed that the quality of freight car (excluding tank car) marking on older cars seems to be going downhill. By freight car marking I mean:

- Railcar initials and numbers
- Load limit, lightweight
- Consolidated Stencil

Railcar marking / remarking

- Brake shoe stencil
- FRA Part 224 Reflective sheeting
- Dimensional and capacity stencils
- Non-standard piston travel ranges
- Spring numbers and sizes, snubber type, brake beams, coupler and draft information
- Other stencils that reflect unique or special equipment on the car

The days of paint stencils are pretty well over. Decals are easy to read and look professional. Most decals I deal with have the background color of the car (usually black, mineral brown or gray) incorporated with contrasting letters and numbers. Decals have a very aggressive adhesive that holds very well on properly prepared surfaces that are dry and above 35 degrees Fahrenheit. The key words to note in the last sentence are "properly prepared surfaces that are dry and above 35 degrees Fahrenheit".

Preparing steel cars for decals is different from aluminum cars

Here is how I think the surface should be prepared for a steel car:

- All loose scale and corrosion is removed by a wire brush or Scotch-Brite pad. Do not use a grinder. Grinding tends to close the pores of the metal and eliminates the anchor pattern needed for the adhesion of the decal to the car for the long term.
- Any bare steel needs, at minimum, a coat of Rust-Oleum type paint. Allow to dry appropriately based on temperature and humidity. The paint label should have that information. Don't rush the project.
- Prepare a 50% solution of isopropyl alcohol and water. Then wipe down the surface with a clean cloth until all dust and grime is removed. Allow sufficient time to dry completely.

Here is how I think the surface should be prepared for an aluminum car:

- Rough up the surface very lightly using a Scotch-Brite pad. Do not use anything more aggressive.
- Prepare a 50% solution of isopropyl alcohol and water. Then wipe down the surface with a clean cloth until all dust and grime is removed. Allow sufficient time to dry completely.

Scan back through the preceding text and imagine that procedure happening on a railroad "Rip" (repair) track. Also think about remarking cars after purchase on a remote storage track. The chances of getting all of the "properly prepared surfaces that are dry and above 35 degrees Fahrenheit" requirements seem unlikely. Therefore, I would recommend decal application be done at a contract shop that you are familiar with. Be specific on your scope of work and perform a follow up inspection or at minimum require photos of the completed decals.

Surface preparation and application conditions are critical to insure that the reflective sheeting stays in place on the car for many years

Now for a little preaching. I have seen the aftermath of loaded farm trucks, semi-trailers and cars run into the side of trains on rural unprotected crossings (no lights or crossing arms) late at night. The results are gruesome. I, personally, have approached crossings that I was very familiar with late at night only to be surprised that a train was stopped over the tracks. Thankfully all cars must be equipped with FRA Part 224 Reflective Sheeting by November 28, 2015. Surface preparation and application conditions are critical to insure that the reflective sheeting stays in place on the car for many years. I have seen way too many cars with reflective sheeting peeling off the cars because there was no surface preparation. The peeled off portions had rust, dirt, grease and corrosion stuck to the adhesive backing. My conscience wouldn't allow me to place the safety of others at risk because of poor application procedures. I am sure yours wouldn't either.

If you have any questions, Tealinc stands ready to assist you in any way we can. Put our knowledge and varied experience to work for you.

Steve Christian is the Manager Value Creation-Railcar Performance Manager for Tealinc, Ltd. You may contact Steve directly out of our Nebraska office at (308) 675-0838 or via email at ***steve@tealinc.com****.*

Railroad Traffic

AAR reports mixed traffic for February 2014

The Association of American Railroads (AAR) reported on March 6 mixed U.S. rail traffic for the month of February 2014, with carload volume decreasing and intermodal volume increasing compared with February 2013. Intermodal traffic in February totaled 993,807 containers and trailers, up 1.1 percent (10,729 units) compared with February 2013, which represents the 51st-consecutive year-over-year monthly increase for intermodal volume. U.S. carload originations totaled 1,100,858 in February 2014, down 1.1% (12,061 carloads) from February 2013.

Commodities with the biggest carload are grain, and grain mill products

Nine of the 20 commodity categories tracked by the AAR each month saw year-over-year carload increases in February over the same month last year. Commodities with the biggest carload increases last month included grain, up 12.3 percent or 8,696 carloads, and grain mill products, up 10.1 percent or 3,645 carloads.

Commodity categories with carload declines last month included coal, down 3.5 percent or 15,571 carloads from February 2013, and primary metal products, down 7.2 percent or 3,092 carloads. Excluding coal and grain, carloads were down 5,186 carloads or 0.9 percent in February 2014 over the same month last year.

Commodity with decline carload are coal, and primary metal products

"It would be nice to be able to separate out the effects of the harsh winter on rail traffic, but we can't do that. We can probably expect improvements in the rail numbers in the months ahead, assuming that the weather and the economy cooperate," said AAR Senior Vice President John T. Gray. "In the meantime, crude oil has become a significant part of the railroad business. Railroads know how important it is to move crude oil safely, and they are committed to continually searching for ways to make this happen."

Visit the AAR at:
https://www.aar.org/newsandevents/Freight-Rail-Traffic/Pages/2014-03-06-railtraffic.aspx#.UzGmSs5n4dw

Industrial Inside

The first forecast by U.S. Department of Agriculture (USDA) analysts for the 2014-2015 crop year was presented recently at the agency's annual

USDA: Fewer acres of corn but potential for record crop

Agricultural Outlook Forum.

USDA's first take on the 2014 crop year was prepared by its wheat, feed grains, rice and oilseeds interagency commodity estimates committees. The early 2014-2015 outlook for grains and oilseeds is driven by expectations for larger crops and reduced prices for wheat, corn and soybeans. Reduced plantings of wheat and corn are partly offset by an increase for soybeans as relative returns support more soybean plantings for many producers.

USDA delivered news farmers do not want to hear: "Futures, cash and farm-level prices for wheat, corn and soybeans are all expected to fall in 2014-2015 as record U.S. corn and soybean production continues to support large global supplies."

"Futures, cash and farm-level prices for wheat, corn and soybeans are all expected to fall in 2014-2015…"

Expected returns for wheat, corn and soybeans were historically high in late 2012 and early 2013 supporting producer intentions to plant a combined 230.8 million acres in 2013, exceeding the 30-year high of 230.1 million acres in 2012. Persistent spring wetness prevented planting last year for some producers and limited the final, three-crop total to 228.1 million acres for 2013. For 2014, the three-crop total is projected at 227 million, down mostly on lower soft red winter wheat seedings last fall.

USDA's initial estimates of 2014 corn are record production, on record-high yields, as well as record levels of use, reports Texas A&M grain marketing economist Mark Welch. This forecast is based on normal weather conditions for spring planting and summer crop development.

Combined acres of corn, soybeans and wheat are anticipated to drop by 1.1 million from last year.

A corn crop of 13.985 billion bushels is projected from 92 million acres and an average yield of 165.3 bushels per acre, which would be an all-time record high corn yield, notes Welch.

USDA's projected 2014 corn production is up just slightly from the record 13,925 million in 2013. The 2014-2015 corn supply is projected to be up 5 percent at a record 15,491 million bushels, mostly reflecting a 660-million-bushel increase in beginning stocks.

USDA's initial estimates of 2014 corn are record production, on record high yields…

Higher expected yields support the record crop with planted and harvested area both down on the year. Harvested area is projected at 84.6 million acres, down 3.1 million from 2013.

Read the entire article at:
http://www.agriview.com/news/crop/usda-fewer-acres-of-corn-but-potential-for-record-crop/article_c01c112f-cf2f-5537-a8cb-da5f350428f4.html

---

Financial Focus

The Federal Reserve announced on March 19 that it will continue to gradually withdraw economic stimulus, but decided to move its goalposts for raising interest rates.

Fed moves economic goalposts

At the conclusion of Janet Yellen's first meeting as chair, the central bank announced a decision to reduce monthly bond purchases by $10 billion, down to $55 billion a month starting in April.

But the economy is still being supported through near-zero interest rates, which have been in place since 2008. As for when those rates would rise, policymakers decided to abandon their previous threshold of 6.5% unemployment, in favor of a broader view of the job market.

"When the Committee decides to begin to remove policy accommodation, it will take a balanced approach consistent with its longer-run goals of maximum employment and inflation of 2 percent," the statement said.

Forward guidance: The Fed modified its so-called forward guidance for a potential interest rate hike, because its previous guidance of 6.5% unemployment wasn't leaving much wiggle room.

The unemployment rate stood at 6.7% in February. And according to its latest economic forecasts released on March 19, the Fed now believes the unemployment rate could fall as low as 6.1% this year.

The Fed has now decided to move toward a more qualitative approach in determining interest rate policy.

"This assessment will take into account a wide range of information, including measures of labor market conditions, indicators of inflation pressures and inflation expectations, and readings on financial developments," Fed officials wrote in the statement.

Speaking to reporters after the meeting, Yellen said the job market has improved more than many had anticipated, though she stressed that it's still weak and offered a list of various labor market measures that the Fed would be looking at.

The unemployment rates stood at 6.7% in February...Fed believes the unemployment rate could fall as low as 6.1% this year

Yellen said repeatedly that the change in guidance does not signal any immediate shift in the Fed's current policy intentions. She said rates would likely remain low for a "considerable period" after the Fed's bond-buying program ends.

Investors were spooked after Yellen responded to a question by suggesting that a "considerable period" could be defined as around six months. That led investors to believe that rates could rise sooner than previously thought. The Dow Jones industrial average was down more than 100 points in afternoon trading.

Tapering: The Fed has been buying bonds -- mainly long-term Treasuries and mortgage-backed securities -- since September 2012 in an attempt to stimulate the economy. But it began reducing the program this year in a process nicknamed "tapering."

The Fed has said it would continue its plan to taper by $10 billion a month unless its outlook for the economy changed substantially.

...economists have speculated that the slump was a temporary result of extreme weather, and indicators would recover in spring

While the job market had been in a rut over the winter, economists have speculated that the slump was a temporary result of extreme weather, and indicators would recover in spring.

In its statement, the Fed said economic activity slowed during the winter months, "in part reflecting adverse weather conditions."

Yellen said bad weather contributed to a spate of weak economic data over the first few months of the year. But she said most Fed officials expect the drag from cold weather will "begin to wash out in second quarter."

Only one Fed member formally dissented against the statement. Minneapolis Fed President Narayana Kocherlakota felt that the change in forward guidance could weaken the Fed's credibility and cause uncertainty.

Learn more at:
http://money.cnn.com/2014/03/19/news/economy/federal-reserve-statement/index.html?iid=SF_BN_Lead

The Edge

It's been a long winter for most of you and while it's warmer in my part of Colorado than it has been for much of the rest of the country, you can imagine my chagrin when March 2 rolled around and I was assigned to represent Tealinc at the Rail Equipment Finance conference in glorious Palm Springs, CA. This was my third time attending and I always look forward to hearing presentations packed full of graphs from the past, updates on current industry events and educated "crystal ball" future forecasting.

The tone of attendees and presenters at the conference (rail shippers, financial institutions, lessors and railroads) was mostly optimistic. As 2014 Q1 comes to a close, we acknowledge that the country is headed out of the worst economic time to face our generation, the worst drought in more than 50 years is behind us and the largest transition in energy (coal – natural gas) is altering the railroad industry. It's said that with these monumental changes behind us, we are now set to build a new normal. Of course one wonders what the economic path for 2014 holds for us, will the wet winter lead to a too wet spring and summer impacting crops and what will CBR legislation and further studies on Bakken fracking do to natural gas pricing?

The total North American railcar fleet grew by one percent (1%) year-over-year 2012 to 2013 with the biggest gains in tank cars (up 24,000 units) and flatcars (up 3,000 units) and the biggest losses to the fleet were boxcars (down 3%), open tops (down 3%) and gondolas (down 2%)

Umler Equipment Index - Revenue-Earning Fleet
4th Quarter 2013

GROUP	COUNTS AS OF 31-DEC-13	COUNTS AS OF 30-SEPT-13	% CHANGE
Box Cars	129,316	129,542	-0.2%
Covered Hoppers	481,617	480,615	0.2%
Flats	199,050	198,948	0.1%
Gondolas	230,149	231,307	-0.5%
Open Hoppers	145,727	146,267	-0.4%
Tanks	340,944	333,767	2.2%
TOTAL	**1,526,803**	**1,520,446**	**0.4%**

Chart from Railinc.com – click here to see the entire update

Still the industry is distraught by the continued troubles in the coal market. New regulations, continued low natural gas pricing, and barriers for coal exportation continue to pose road blocks for the coal industry. Coal players have some creative thinking to do to stay ahead but lessors and storage facilities aren't seeing the inventory of coal cars they we were seeing 6 months ago. Speculation is that weather and hellacious railroad service (attributable to both weather delays and crew issues) have ramped up equipment orders and most think that the coal market will stabilize in 2014.

On the other side of the energy picture, fracking is king through the oil play areas (think Marcellus, Bakken, Niobrara, etc. If you're intrigued, here's a great map) and the increase in monthly production volumes continues to support horizontal well efficiency. While the oil play transportation story has been tank cars for crude by rail (19% of all new railcar builds in 2006 were tank cars compared to 55% in 2013!) and covered hoppers for frac sand (did you know 40-60 cars are required per rig?), big demands for raw product transportation vehicles (mill gonds and flatcars for road and housing infrastructure, plastic pellet cars for chemicals) are required. There's also the looming tank car retrofit program that has tank car suppliers worried.

The steel market is enduring its typical volatility and consolidation persists; a mode of transportation for scrap and finished steel products remains complicated. The mill gondola fleet has decreased 12% in the last 10 years and surplus assets remain hard to find.

When focused on the grain market, it's reported that the USDA is predicting record planting levels in 2014. While there are still quite a few 4750's in the North American railcar fleet, this year will see the last of the 40 year cars age out and demand for fertilizers and soda ash cars will lead to increased inventory tightness in this versatile car type. The once oversupply of higher cube grain cars and DDG (dried distillers grain) cars are being worked through if not already corrected and the backlog continues for larger cars and the railroad has been losing modal share to trucking since 2002 for shorter hauls. The moral of the covered hopper market looks to be that you may need to brace yourself if you don't already have car supply in check – it will be hard to find cars.

Finally, a constant point of conversation (both during networking breaks and presentations) was service, service, service… and the lack thereof. Average train speed is down and while winter weather has been an explainable reason, train speeds have been deteriorating since last year.

The writing is clearly on the wall. This is the time to take advantage of market opportunities. It's a good time to lease (unless you're looking for tank cars, prices aren't bad), it's a good time to buy (prices aren't bad), it's a good time to sell (did I mention prices aren't bad!) and if you trust Warren Buffet, it's a great time to be involved in rail.

We look forward to earning your business!