Tealinc

Touchbase

January 2013

In This Issue

Visit us at:
www.tealinc.com

UP says: Industry Track Agreements are necessary to ensure that ownership, maintenance, and other responsibilities are clearly defined

Railroad & Policy Updates

In an email sent December 17, 2012, Union Pacific says that it is committed to providing excellent service to its customers, and doing so as safely as possible for both its employees and its customers. Maintaining a safe working environment for both [parties] starts with a Union Pacific Industry Track Agreement.

Industry Track Agreements are necessary to ensure that ownership, maintenance, and other responsibilities are clearly defined between Union Pacific and customers in order to maintain safe and efficient rail operation.

Over the next several months, the statement continues, Union Pacific will be working to identify customer facilities with no track agreement on file and we will be contacting the customers served at those locations in order to establish an agreement. If [the UP is] unable to locate an active track agreement for your track, you will receive an email from a representative within [the UP] Real Estate department, which is responsible for track agreement management and organization. The purpose of the e-mail, as explained by the sender, was to request your assistance in providing information about the track for use in preparing a new track agreement.

As part of this process, [the UP] will also be reviewing the insurance coverage at each facility where a track agreement is currently in place. If [the UP] determines after review of your current agreement that revisions are necessary to comply with current railroad insurance standards or to reflect more accurately current business practices, you may also be contacted by a representative from Ebix, Union Pacific's third party insurance management company. The Ebix representative will provide instructions for meeting the current insurance requirements and supplementing the existing track agreement.

The statement concludes by saying that if you have questions at any time during this process, please contact your Sales Representative, who would be happy to answer any questions.

Tealinc, Ltd. Also stands ready to assist you with this process. Contact us via email at **webmail@tealinc.com** or visit our website at **www.tealinc.com** for further guidance.

Mississippi River Shippers Shift Freight to Rail

Historically low water levels on the Mississippi River and a potential shutdown of waterway traffic will likely shift even more freight

Historically low water levels on the Mississippi River and a potential shutdown of waterway traffic will likely shift even more freight from barges to railroads.

Shippers of recycled metals put more southbound cargo normally bound for barges on the rails in December, and the mode shift is expected to intensify this month as water levels fall further, barge capacity tightens and freight builds, according to a Jefferies research note. Because of their

from barges to railroads

strong networks in the region, Union Pacific Railroad and Kansas City Southern Railway are best poised to gain from the modal shift.

The potential shutdown of Mississippi River barge traffic could affect 7.2 million tons of commodities valued at $2.8 billion, according to the American Waterways Operators and Waterways Council.

Learn more at: http://www.joc.com/rail-intermodal/class-i-railroads/mississippi-river-shippers-shift-freight-rails_20130102.html

Extension of Shortline Railroad Track Maintenance Credit

The shortline industry began the New Year with good news: Extension of the railroad track maintenance credit

The shortline industry began the New Year with good news: Extension of the railroad track maintenance credit.

The 45G tax credit has been extended until Jan. 1, 2014, as part of the "fiscal cliff" deal passed in the Senate and then in the House of Representatives. The credit is retroactive and applies to expenditures paid or incurred in taxable years beginning after Dec. 31, 2011.

The tax credit was originally enacted in 2004 and creates an incentive for shortline and regional railroads to invest in track rehabilitation and improvements by providing a tax credit of 50 cents per dollar spent on those improvements. Prior to the current deal, the credit, which is capped based on a mileage formula, expired on December 31, 2011.

Read more at: **http://www.rtands.com/index.php/freight/shortline-regional/shortline-tax-credit-extended-as-part-of-fiscal-cliff-deal.html?channel=276**

Mechanical Brief with Steve Christian

Impact switching: the costs are monumental

When I was a youngster, my father was transferred to McCook, Nebraska as the Roundhouse Forman. McCook was solidly a railroad town in those days. It was the division headquarters, crew change point and a dispatching center for the western lines of the Chicago Burlington and Quincy Railroad. There was an overhead walkway that linked the depot on the north edge of the rail yard to the roundhouse, store department, car department, bridge and building and maintenance of way facilities on the south side of the yard. At one time hundreds of people used this walkway to get to and from work.

The impact was usually so hard that the cars would literally jump when coupling in. The crash could be heard all over town and was just a normal occurrence in this railroad town

In the summertime, my friends and I would climb the stairs to the walkway and settle in to watch the switch crew bring a cut of cars up from the yard. The switch crew would proceed to kick cuts of cars through the “puzzle switch” to make up trains. The overhead view of the switching operations was amazing. The switch engine would roar, the cars would bang as the slack was taken up and the switchman would reach in and pull the pin lifter while giving the stop signal to the engineer. That group of cars would lurch ahead and go speeding down the track to crash into the other cars on the target track. Many times, a second cut of cars was dispatched to another track before the first one coupled in. The impact was usually so hard that the cars would literally jump when coupling in. The crash could

Railroads have gone to great lengths to cut down on impact switching

be heard all over town and was just a normal occurrence in this railroad town.

While this was commonplace in those days, this is no longer acceptable. Railroads have gone to great lengths to cut down on impact switching. The cost of impact switching is monumental. Much of the damage and resulting cost shows up later in hidden damage to equipment and lading. I define "impact switching" as switching that involves severe "Draft" and "Buff" forces being exerted. "Draft" is the term for the pulling motion while "Buff" is the pushing motion while switching. These forces are transferred throughout the railcar, locomotive and all connecting cars.

Much of the damage and resulting cost shows up later in hidden damage to equipment and lading.

As I noted, the railroads have addressed impact switching with great success. Equipment damage, lading damage, derailments and injuries have been reduced drastically by these efforts.

It is time for industrial switching operations to address this problem. Here are some of the usual causes of impact switching at industrial sites:

1. Misjudging distances when switching
2. Blind pushes of cars
3. Excessive speed
4. Hard "hits" to make a knuckle lock drop
5. Slippery track
6. Radio failure
7. Coupling into a string of cars with all the slack taken in.
8. Coupling and uncoupling on a curve or uneven track

Training and holding personnel responsible are the keys to stopping impact switching

Training and holding personnel responsible are the keys to stopping impact switching. Of course there is much more that needs to be done. I have fought the good fight and learned the hard lessons from my many years involved with switching. There is no need to repeat these hard lessons in your operations.

Let Tealinc utilize our years of knowledge and experience to bring impact switching under control in your organization. We stand ready to provide training materials and on-site training at your facility.

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 annual rail traffic for 2012; monthly traffic for December mixed

The Association of American Railroads (AAR) reported January 3, 2013 mixed 2012 rail traffic compared with 2011. U.S. rail intermodal volume totaled 12.3 million containers and trailers in 2012, up 3.2 percent or 374,918 units, over 2011. Carloads totaled 14.7 million in 2012, down 3.1 percent or 476,322 carloads, from 2011. Intermodal volume in 2012 was the second highest on record, down 0.1 percent or 14,885 containers and trailers, from the record high totals of 2006.

In 2012, 12 of the 20 carload commodity categories tracked by AAR saw

“Coal and grain typically account for around half of U.S. rail carloads… A number of key rail carload categories showed solid improvement in 2012, including categories like autos and lumber that are most highly correlated with economic growth”

increases on U.S. railroads compared with 2011. The biggest gains were petroleum products, up 170,994 carloads or 46.3 percent; motor vehicles and parts, up 114,221 carloads or 16.5 percent; crushed stone, sand and gravel, up 71,012 carloads or 7.9 percent; and lumber and wood products, up 18,659 carloads or 13 percent.

The commodities with the biggest carload declines in 2012 from 2011 were coal, down 726,257 carloads or 10.8 percent; grain, down 106,289 carloads or 9.5 percent; and metallic ores, down 22,421 carloads or 5.7 percent. Excluding coal and grain, U.S. rail carloads in 2012 were up 356,224 carloads or 4.9 percent over 2011, their third straight year-over-year annual increase.

“Coal and grain typically account for around half of U.S. rail carloads, so when they’re down, chances are good that overall rail carloads are down too, as we saw in 2012,” said AAR Senior Vice President John T. Gray. “That said, a number of key rail carload categories showed solid improvement in 2012, including categories like autos and lumber that are most highly correlated with economic growth. Meanwhile, intermodal just missed setting a new volume record in 2012. In 2013, freight railroads look forward to continuing to provide the world’s safest, most cost effective freight rail transportation service.”

AAR also announced mixed December 2012 rail traffic, with U.S. railroads originating 1,086,990 carloads, down 4.2 percent from December 2011. U.S. rail intermodal originations totaled 888,002 containers and trailers in December 2012, up 1.7 percent over December 2011.

During December 2012, 11 of the 20 carload commodity categories tracked by AAR saw increases compared with December 2011.

Read the entire article at: https://www.aar.org/newsandevents/Freight-Rail-Traffic/Pages/2013-01-03-railtraffic.aspx

Industrial Inside

New five-year outlook shows that supply and demand conditions in wood products for the long-awaited ‘super-cycle’ are now taking hold, with the full impact still some 3+ years away!

With the return of a demand-driven wood products market in 2012 – due to rapidly increasing housing starts in the U.S. – it is now forecast that lumber and panel prices will move to new highs in 2013 and record highs for lumber in 2014. A North American “super-cycle” has been predicted by Wood Markets since 2008 as a result of emerging supply-side constraints (mainly on forests and logs) as well as changing demand dynamics, but the global financial crisis that started in late 2008 and an unusually slow U.S. housing market recovery have delayed this event until 2012. With the expectation of strong growth in U.S. housing starts over the next five years, combined with a better balance in the housing inventory and a recovering economy, the U.S. supply chain is expected to become overwhelmed at times during the next five years, allowing wood products prices to soar. While there are a number of assumptions that are required to maintain steady economic growth, a strong wood products recovery amidst a tightening timber and mill supply base is still expected.

These and other findings on U.S. and Canadian lumber markets as well as forecasts for all engineered panels were released on December 12, 2012 by

Report examines an overall tightening of the global timber supply base; forecasts that it is mainly in North America where scarcities will be felt

As many large U.S. corporate forest companies with sawmills have sold their private timberlands to TIMOs, timber prices are eventually forecast to rise and be sold more on the margin, tightening the economics of sawmilling in the U.S. and potentially limiting incremental lumber production

WOOD MARKETS in its 8th edition report: *WOOD Markets 2013 • The Solid Wood Products Outlook • 2013 to 2017.* The report examines an overall tightening of the global timber supply base, but forecasts that it is mainly in North America where scarcities will be felt. With China now importing more and more logs and lumber from North America and with U.S. demand now rebounding, some key structural constraints are expected to keep log and lumber supplies tight relative to demand growth, including:

- A collapse of the Russian logging sector in 2009 from the global financial crisis where log exports are now less than 40% of their 2007 level as they continue to decline in 2012.
- Changes to the Russian log export tax that continues to leave Russian log exports less available and expensive.
- After a “cooling-off” period in 2012, China’s requirement to feed its growing wood deficit will see a return to steady demand growth for imported logs and lumber from North America and other sources.
- The mountain pine beetle epidemic in the B.C. Interior will, by the end of the decade, kill about 60% of all the pine trees in the BC Interior. This will permanently reduce Western SPF lumber production starting in about 2014 or 2015.
- The Quebec government (which controls 90% of the forests in the province) will have reduced the timber harvest by at least 30% between 2004 and 2013, permanently reducing lumber production.
- Consequently, Canada’s lumber production will plateau by about 2015, allowing for essentially no increases in exports to the U.S. and will, therefore, see its’ U.S. lumber import market share plummet to two-thirds of its historical level. By the end of the decade, B.C. and Quebec lumber shipments will collectively be lower by some 10 billion bf as compared to peak shipments in 2004.
- The role of Timber Investment Management Organizations (TIMOs) will play out as log markets strengthen. As many large U.S. corporate forest companies with sawmills have sold their private timberlands to TIMOs, timber prices are eventually forecast to rise and be sold more on the margin, tightening the economics of sawmilling in the U.S. and potentially limiting incremental lumber production.

A key question that the report addresses is: “Where will the U.S. get its lumber after mid-decade?” This is almost the same question that WOOD MARKETS asked and addressed in its recent *China Book: Outlook to 2017* but in that report, the question was: “Where will China get its logs and lumber after mid-decade?”

“Both countries will need to import increasing volumes of lumber and logs that will be tied more and more to international market forces as global timber and lumber supplies tighten,” explains Russell Taylor, President of WOOD MARKETS. “U.S. housing starts are expected to rebound from 550,000 units in 2009 to the long-term sustainable level of 1.5-1.6 million starts by 2017 and Chinese housing and wood demand is expected to grow further after the new government’s economic policies are unveiled in Q2/2013. The net result is that log and lumber demand in these countries are expected to grow steadily and drive global supply and prices.”
The outcome will be rising and even record-high U.S. lumber prices. In fact, *WOOD Markets 2013* is forecasting that export duties on Canadian

“U.S. housing starts are expected to rebound from 550,000 units in 2009 to the long-term sustainable level of 1.5-1.6 million starts by 2017 and Chinese housing and wood demand is expected to grow further… The net result is that log and lumber demand in these countries are expected to grow steadily and drive global supply and prices.”

lumber to the U.S. will essentially be at a ‘zero-rate’ for all five years of the forecast as compared to maximum duties of 5% or 15% (depending on the Canadian province) for most of the last five years. “Increasing prices will see the return of European lumber to the U.S. market – and lots of it – to fill the widening gap as Canadian lumber production and exports slow,” said Gerry Van Leeuwen, Vice President, “and, as a matter of fact, some European supplies are already starting to arrive at current prices, which are already at six-year highs!” Nevertheless, as European log costs are more than double those of North American logs, much higher lumber prices are required to attract significant volumes from Europe. So, higher prices are inevitable as the supply chain struggles to secure and move rising volumes!

Five-year forecasts on OSB and plywood also see strong prices, but not as high as what are in store for lumber. By comparison, the particleboard and MDF sector will see more limited growth, but higher demand and prices are also forecast in the report.

However, the entire “super-cycle thesis” requires strong and growing demand in the U.S. market as well as stable to increasing demand in other global markets (no global economic recession), especially in Asia. Without these conditions and the other key ingredient, increasing lumber demand, it is possible that the super-cycle could stall early or the timing may be pushed out further. In any event, the prospects of a tightening of the global timber and lumber supply are a reality and are expected to play out over the next five years!

Full details on the five-year outlook for the U.S and Canada’s consumption, imports, exports, production and price trends, etc., are available in *WOOD Markets 2013 • The Solid Wood Products Outlook • 2013 to 2017*. Visit **http://www.woodmarkets.com/pressreleases.html**

RTA: Short-line tax credit extension means more tie demand in 2013

RTA: Short-line tax credit extension means more tie demand in 2013

The recent extension of the short-line tax credit is a "game changing" piece of legislation for hardwood and softwood tie demand in 2013, according to the Railway Tie Association (RTA). An updated econometric tie demand forecasting model shows 500,000 to 1.2 million ties will be added to market demand this year, RTA officials said in a release issued to members.

"This raises the total 2013 forecast for new wood tie demand to 23.3 million on the low end, to an upper end of 24 million," they said. "This is an immediate positive for loggers, sawmills and wood treaters."

"This raises the total 2013 forecast for new wood tie

The American Taxpayer Relief Act (H.R. 8) that was enacted on Jan. 2 extended the Section 45G tax credit for two years: retroactive to Jan. 1, 2012, to cover last year and through Dec. 31 to cover 2013. The Section 45G provision enables short lines to claim a tax credit of 50 cents for every dollar invested in track rehabilitation, up to a cap equal to $3,500 times the railroad's total track miles.

To extend the tax credit beyond 2013, lobbying work needs to begin now, said RTA Executive Director Jim Gauntt in the release.

demand to 23.3 million on the low end, to an upper end of 24 million"

"There are 81 new members of Congress, very few of which will have any knowledge of, or experience with, the railroad industry. Likewise, of the 255 co-sponsors of the just-passed 45G legislation, 47 are now gone and will have to be replaced with new co-sponsors," he said. "As we have done in the past, we need to do our part by bringing the message to the congressmen who represent us and understand the importance of our facilities."

Read more at: http://www.progressiverailroading.com/prdailynews/news.asp?id=34786

Financial Focus

U.S. out of slow lane, but can't find fast lane

U.S. economy is likely to experience more of the "new normal" early on in the new year. What's the new normal? An economy growing around 2%, workers' wages rising about 2% a year and roughly 150,000 jobs being created each month.

Not bad, but well below the nation's typical performance. At this stage of a recovery, the U.S. economy normally grows around 3% a year and adds upward of 200,000 jobs a month. Wages also tend to rise a bit faster.

"The economy is growing, but not fast enough to move the needle in terms of its potential"

"The economy is growing, but not fast enough to move the needle in terms of its potential,' said Steve Blitz, chief economist at ITG Investment Research. "We are on a low-trajectory growth rate."

Investors won't get any evidence to show otherwise this week, either. The economic calendar is extremely light, highlighted by the U.S. trade deficit and secondary reports on weekly jobless claims, small-business activity and the price of imported goods.

"The data is not going to be driving much activity this week," said Julia Coronado, senior economist at BNP Paribas.

Several top officials at the Federal Reserve are also slated to give speeches. Although the central bank is not expected to change its strategy soon, markets always pay close attention to what Fed VIPs say.

Like the economy, jobs are growing only modestly.

In the middle lane

The trajectory of the U.S. economy has been remarkably stable — some would say flat — over the past two years. In both 2011 and 2012, the U.S. had created an average of 153,000 jobs a month.

The modest increase in jobs dovetails with modest growth in the economy. In some ways, the U.S. has been remarkably resilient despite a number of headwinds, such as a housing bust, manufacturing slowdown, frequent U.S. budget fights, European financial crisis and a global economic slump. The problem is, the economy can't break out of its slow-growth straitjacket and conditions are still not ripe for faster recovery.
The early part of 2013, what's more, will generate fresh headwinds.
For one thing, a temporary tax cut applied to worker's paychecks in 2012 has lapsed. That will cut take-home pay by 2% a week for most U.S.

The trajectory of the U.S. economy has been remarkably stable

— some would say flat — over the past two years

employees. A person earnings $50,000 a year before taxes, for example, will pay an additional $1,000 to the government.

Another big budget fight in Washington, meanwhile, looks increasingly likely. The ability of the U.S. to pay its debt could be temporarily impaired unless Congress raises the legal limit on how much the government can borrow.

Republicans who control the House say they won't raise the limit unless President Obama agrees to deep spending cuts over the next decade, including some reductions in 2013 that could also act as a drag on the economy. The White House insists it won't negotiate.

Looking behind unemployment data

What the December unemployment figures mean for the U.S. economy and for investors.

A similar face-off in the summer of 2011 disrupted U.S. and global financial markets and briefly threw the economy out of whack.
What should help the economy over the next few months, on the other hand, is the sharp drop in gasoline prices. Lower fuel costs for consumers could offset part of the drag caused by the expiration of the payroll tax break.

By and large, most economist expect the U.S. to continue along its current growth path through the first half of 2013

The result is that wages are now expanding somewhat faster than inflation, a big reversal from earlier in the year. Hourly earnings have climbed 2.1% in the past 12 months, compared with a 1.8% increase in inflation.

By and large, most economist expect the U.S. to continue along its current growth path through the first half of 2013. Some predict — and hope — for faster growth at the back end of the year.

If that last two years are any indication, however, the new normal might be here awhile.

"This year we are going to absorb a lot of fiscal tightening," Coronado noted.

Learn more at:
http://www.marketwatch.com/story/us-out-of-slow-lane-but-cant-find-fast-lane-2013-01-06

The Edge

The presidential, senate and house elections are over and not much has changed politically, the Mayan calendar ended and the world kept on chugging along as usual, the country continues to face a decision on whether or not to increase the debt ceiling yet again or take on some fiscal responsibility and my neighbor says his wife didn't die from the flue on December 24th so he went ahead and bought her a Christmas present. The course of events would be humorous if they didn't have such a drastic impact (sans my neighbors' wife) on the economic health of the United States.

Our team at Tealinc compared notes on the events that we have helped solve over the past year and while we don't have any Mayan predictions or solutions for fiscal irresponsibility of our political leaders we do have some "free" advice.

Mechanical Inspections. They're more than a quick overview or checklist to do for the lease or purchase process. In one instance the drive by inspection that was completed last year on a set of 115 cars revealed this year that it was certainly a drive by inspection. The corporate office insisted on a less thorough inspection from a less qualified inspector to save money on what they considered a simple check off process. One year later we're apply our in-house expertise and a detailed inspection process to manage the repair process on all of the railcars.

In another instance we were involved on the front end of the inspection process for 235 cars. We put a program in place for the cars prior to acceptance into service and for the past two years have average less than industry norms on down time and mechanical repair costs, insuring availability of the railcars to haul product and spend less time on bad order tracks or in repair shops.

The lesson here, you may have to invest more on the front end to get a qualified inspector and a detailed inspection but if you're serious about leasing or buying the railcars (or locomotives) it's inexpensive considering the cost of a mistake.

Railcar Availability. In one instance we performed a mechanical inspection for a customer and while we found out that the railcars were in great condition the bridge they were parked behind wasn't. Two hundred cars behind a FRA condemned bridge on a shortline railroad are expensive to truck out!

In another instance we found that the shortline owner, a grain company, decided they weren't going to operate their ten mile line anymore and were in the process of finding a new operator. Our advice to the potential buyers of the 30 railcars on the line – wait until you're sure they can be pulled to interchange before committing to the cars.

The lesson here, look around and use your peripheral vision and thought processes when accessing availability of railcars. Don't just assume that since they're parked on a track that it actually is interchangeable. Also of use is to ask for storage, switch and repair rates and timing of all three prior to signing up for equipment

Rail Rate Negotiations. When my girls were little we'd build ferry houses out of sticks and grass. The idea was to build the house and it would attract ferries, usually taking an evening or two before they'd show up. During the course of the next day or so I'd sprinkle ferry dust (glitter) sparingly in the ferry house evidencing the presence of a ferry since the dust fell off their wings onto the inside of the house. While there may be little girl ferries there aren't any rail rate ferries.

We're fortunate that we have few clients that expect us to shake ferry dust on rail rate makers to arrive at Tinker Bell pricing.

Some examples of projects we're currently working on, that give our clients a leg up on negotiations are as follows.

A bulk fertilizer client is in the initial stages of developing additional rail distribution hubs. They realize they could purchase software that demonstrates rail cost ratios and proposed pricing that the railroads should find acceptable. However they also realize that outside of the ferry dust world railroads have monopolistic and duopolistic pricing power that tends to negate what they should do with what they can do on pricing and service. Our assignment is to find that combination of distribution and service rail networks that optimizes the transport and commodity price favorably for our client.

A minerals mining client is producing product that currently all ships locally by truck. They realize that to expand they're going to need to put a significant amount of product on rail. As it was described to me by the client, "we have access to rail so it should simply be a matter of figuring out how to load the product timely in railcars and ship it down the track". "But after you dig down one layer deeper you realize that all the details are what really make it work so the load and ship theory falls apart in a hurry". The lesson here is not to make any assumptions about the details. If you don't know ask or get a professional involved.

Industry Rail Switch Operations / Yard Utilization Planning. The challenge of keeping an industrial rail operations yard fluid is difficult at best. Some examples of challenges we've been involved in this past year are as follows.

Case one we reviewed the operations for an inbound raw commodity yard that also had ties into finished product outbound requirements. About once a week there'd be traffic jams that required the serving Class I railroad to literally pull a string of railcars out so the yard could get back to being operational. Our recommendation was to move the unloading point on raw inbound product to allow for more cars to be unloaded without having to perform additional switches. The switch operation was cut down from five switches to two for the same amount of commodity discharged.

Case two was similar in that an Industrial rail processing yard was getting congested about once a month. In this case the outbound finished product was pretty steady in production and shipment patterns. The inbound product was not managed in quite the same manner and would result in bunching of loading railcars and subsequently very large demurrage bills. A review of the transportation management plan revealed that changes in management practices would negate the majority of the bunching issues hence significantly reducing demurrage bills.

The lesson in both cases is that the solution is often not an expensive capital investment but a review of practices and processes.

Common Sense Approach. Granted to take a common sense approach to solving a problem or preventing one from occurring or developing a distribution process along with all the details you have to first have a significant amount of experience and experiences from which to draw upon. It also helps to take a fact based approach in arriving at solutions. Here at Tealinc we combine our industrial peripheral vision with common sense and facts to arrive at solutions for our clients, no fairy dust applicators need apply!

We look forward to earning your business!