Touchbase

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The National Mining Association says its conversations with Powder River Basin producers point to a 2.4 percent increase in 2007.

Railroads managed 10 percent increase in 2006 coal deliveries despite derailments

Tentative settlement reached more than two weeks after CN workers began strike

Railroad Updates

Feds Reject Railroad Loan

On February 26th, the Federal Railroad Administration announced that it was denying a $2.3 billion loan request by the Dakota, Minnesota and Eastern Railroad Co., which has tried for some 10 years to finance a third rail line into Wyoming's prolific Powder River Basin coal mining district.

Federal Railroad Administrator Joseph H. Boardman said he believed the risk of DM&E defaulting on the loan was too high.

For utilities in the Midwest and East, rail transportation remains the biggest cost of using Powder River Basin coal. For that reason, Wyoming coal producers could benefit from the competition a third rail company could bring, said Marion Loomis, executive director of the Wyoming Mining Association.

Currently, only BNSF Railway and Union Pacific Railroad serve the Powder River Basin coal industry. Loomis said BNSF had the industry to itself for many years, but when Union Pacific entered the basin in the 1990s, utilities saw a 30 percent decrease in the cost of transportation.

"So it would have been my hope that if we saw additional competition that we'd see those shipping rates moderate, and utilities would look even more favorably on Powder River Basin coal," Loomis said in a phone interview Monday.

But neither UP nor BNSF -- nor their utility customers -- seems to be waiting for a third line in the Powder River Basin. Recovering from derailments in 2006, the railroads managed an astonishing 10 percent increase in coal deliveries in 2006 and continue a massive capacity expansion.

Read the entire article at:
http://www.casperstartribune.net/articles/2007/02/27/news/wyoming/85b518522cd48b4b8725728f0004e199.txt

CN and UTU Reach Tentative Settlement

On February 24th the Canadian National Railway announced that it has reached a tentative settlement with the United Transportation Union (UTU) more than two weeks after CN workers went on strike. During the same announcement, the CN announced that the UTU's 2,800 conductors and yard-service employees remain on strike at CN pending ratification while the CN continues to offer freight service across its network in Canada with management personnel filling in for striking UTU members.

CSXI Fuel Surcharge to Rise to 17 percent March 1st

Drayage-only fuel surcharge for March will be 22 percent

AAR Implements the Removal of 1995 Southern CH-36 Wheels

Read the entire article:
http://www.cn.ca/about/media/news_releases/2007/1st_quarter/en_News20070221a.shtml

CSXI Fuel Surcharge On The Rise Again

After a one-month reprieve, CSX Intermodal's fuel surcharge is heading up again. The company will implement a March surcharge of 17 percent compared with February's 15.5 percent surcharge.

CSXI previously applied fuel surcharges of 17.5 percent in January and December, 16.5 percent in November, 17.5 percent in October and 23 percent in September.

CSXI adjusts its surcharge the first Monday of each month based on the difference between the U.S. Department of Energy's (DOE) price index the previous Monday (in this case, Feb. 26) and $1.10. CSXI calculates the percent difference between the DOE's "Retail Diesel Fuel Price Index" and $1.10, multiplies the figure by 10 percent and then again by 100. On Feb. 26, the DOE reported a diesel retail price of $2.55 per gallon. If the U.S. National Average Fuel Index equals or exceeds $2.79 per gallon, CSXI increases its fuel surcharge 0.5 percent for every four-cent increase in fuel price.

March's 17 percent surcharge applies to CSXI's ramp-to-ramp, ramp-to-door, door-to-ramp and door-to-door rates. The drayage-only fuel surcharge for March will be 22 percent.

Read the entire article:
http://www.progressiverailroading.com/prdailynews/news.asp?id=10286

AAR Updates

On February 23rd, the AAR issued circular C-10468 implementing the removal of 1995 Southern CH-36 wheels at the repair track and scrapping 1980, 1989, 1993, 1991, 1992, 1995 and 1996 Southern CH-36 wheels at the wheel shops. These measures are planned steps in the process of identifying and replacing all suspect 36-inch Southern wheels, determined to have a significantly higher failure rate than other wheels, from the North American interchange fleet.

Call us if you have questions regarding this matter.

Visit the AAR at:
http://www.aar.org

Railroad Traffic

Due largely to severe weather in much of the country and continued weakness in the housing and automotive sectors, U.S. rail carload traffic fell 6.8 percent in the first five weeks of 2007 compared with the first five weeks of 2006, the Association of American Railroads (AAR)

Freight carload lower in January

reported. U.S. rail intermodal traffic fell 1.6 percent in January.

On the carload side, U.S. rail traffic was down virtually across the board, with 17 of the 19 major commodity categories tracked by the AAR registering declines. Commodities showing the largest declines in January 2007 included motor vehicles and equipment (down 21.8 percent); crushed stone, sand, and gravel (down 18.7 percent); and coal (down 2.3 percent).

Intermodal — the movement of truck trailers or containers on rail cars — accounts for approximately 23 percent of U.S. Class I rail revenue. In January 2007, the trailer component of U.S. intermodal traffic was down 12.7 percent, while containers were up 1.9 percent.

Total volume for January was estimated at 157.6 billion ton-miles, down 5.6 percent from the same period last year.

"Railroads are hopeful that solid economic growth continues, and they are confident that the... infrastructure and equipment investments they've made in recent years will continue to yield dependable, cost-effective service for their customers."

"January rail traffic was lower than we would have liked to see, but railroading this month has been a tremendous challenge," noted AAR Vice President Craig F. Rockey. "Railroads are hopeful that solid economic growth continues, and they are confident that the tens of billions of infrastructure and equipment investments they've made in recent years will continue to yield dependable, cost-effective service for their customers."

Canadian rail carload traffic (which includes both the Canadian and U.S. operations of the two largest Canadian railroads) fell 3.9 percent in January 2007, while Canadian intermodal traffic fell 0.5 percent. Carloads of chemicals on Canadian carriers were up 13.3 percent carloads in January, while carloads of metallic ores were down 7.3 percent and carloads of lumber and wood products were down 19.6 percent.

Carloads carried on Kansas City Southern dé Mexico (formerly Transportación Ferroviaria Mexicana - TFM), a major Mexican railroad, were down 12.8 percent in January 2007, while intermodal units carried were up 9.3 percent.

Visit the AAR at:
http://www.aar.org

Industrial Inside

U.S. newsprint prices steadily dropping

Newsprint statistics released on January 31st by the Pulp and Paper Products Council (PPPC) showed a continuing decline in U.S. consumption and rising consumer inventories. At the same time, reports indicate that U.S. newsprint prices were down sharply for the month.

U.S. daily newsprint consumption reached 626,000 tonnes in December, up 2.0% compared to a year earlier. For the year's total, U.S. daily newspapers consumed just over 7.0 million tonnes of newsprint, a drop of 7.1% from 2005 while total U.S. newsprint consumption was flat (down 0.1%) year-over-year in December and down 6.3% for the year's total of nearly 8.8 million tonnes, according to the PPPC.

Pope & Talbot, a Portland, Oregon producer of market pulp and soft wood lumber, announced a $30 price increase for its northern bleached softwood market pulp grades to customers in all markets effective April 1. The company's new prices will be $820 in the North American market and $790 in Europe.

Meanwhile, newsprint inventories remain high for consumers. All U.S. users had 825,000 tonnes in stock at the end of December, a drop of 47,000 tonnes from a month earlier and down 102,000 tonnes from a year ago. U.S. daily newspapers had 749,000 tonnes of inventory at the end of December, 10,000 tonnes below a month earlier and 58,000 tonnes less than a year ago.

North American mill inventories, however, dropped by 21,000 tonnes in December, to 306,000 tonnes by month's end. This was 3,000 below the inventory level a year ago.

Mill stocks destined for the North American market were higher, rising by 13,000 tonnes in December, to 213,000 tonnes, which was 18,000 tonnes higher than last December 31. However, mill stocks destined for overseas dropped 34,000 tonnes in December, to 93,000 tonnes, which was 20,000 tonnes less than a year ago.

North American newsprint producers lowered their output by 2.2% in December compared to a year ago, bringing the year's total production to nearly 12.0 million tonnes, which was 6.3% less than in 2005.

Good news for exports

North American newsprint shipments to overseas were up a sharp 24.2% in December vs a year earlier, but remain 9.8% lower for all of 2006 compared to 2005. A total of just over 2.2 million tonnes was shipped overseas in 2006.

Shipments to all markets were up year-over-year in December, including Western Europe (up 96.8%), Latin America (up 10.8%), Japan (up 47.2%), and non-Japan Asia (up 7.0%). However, for the year's total, only Latin America showed an increase over 2005, increasing by 13.0%. All other countries dropped, including Western Europe (down 35.0%), Japan (down 29.6%), and non-Japan Asia (down 9.2%).

"Threat alone" of Chinese newsprint imports is enough to pressure prices

Imports from overseas, though, remain down, despite reports that Chinese newsprint might be making inroads into the U.S. market. PPPC reported that December's imports were down 63.2% vs the previous December and total 2006 imports were off 25.2% year-over-year. However, according to Mark Wilde, paper and forest products analyst at Deutsche Bank, "the threat alone" of Chinese newsprint imports is enough to pressure prices. "The market appears headed for another shakeout," he said.

Newsprint pricing bleak

Newsprint prices have been dropping for months, falling by $15/tonne through December, and down another $20/tonne in January, Wilde reported. He lists the Jan. 1 price for 30-lb newsprint at $640/tonne

Newsprint consumption is down 24.2% since it peaked in 1999

"There is really no material change in our expectations for the U.S. economy since I last reported to Congress a couple weeks ago" said Bernanke

Futures show Fed closer to cutting interest rates

and FOEX Indexes Ltd. reported that the U.S. benchmark price for 30-lb newsprint fell by $4.40, to $617.32/tonne for the week ending January 16 and fell another $2.58, to $614.74/tonne for the week ending January 23.

Forecasts call for further reductions in newsprint prices this year. Paul Quinn, paper and forest products analyst at Salman Partners, projects 2007 annual prices to drop $33/tonne from 2006's list price average of $668/tonne.

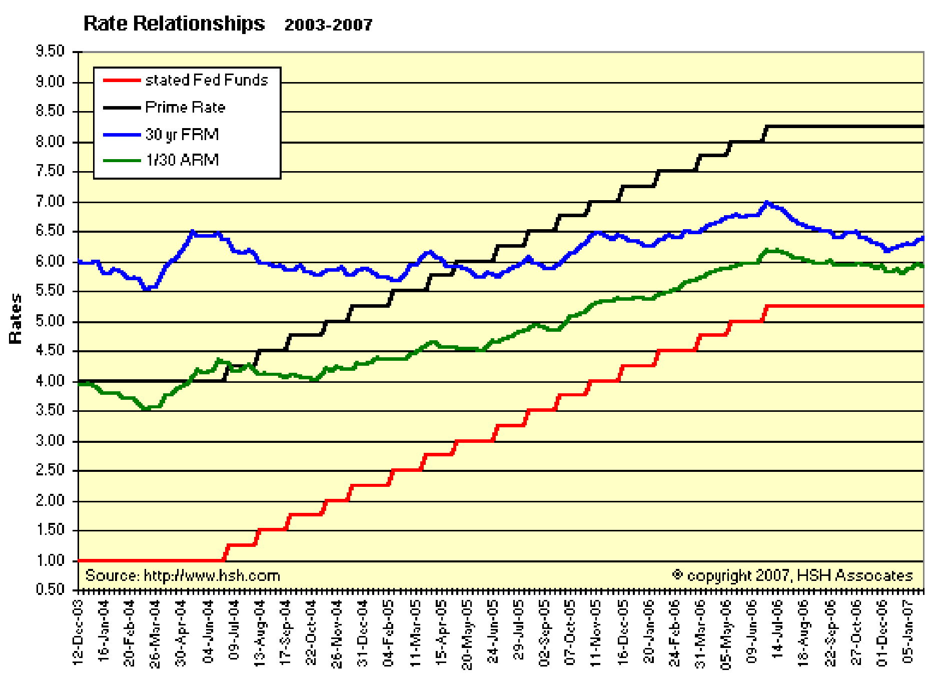
Newsprint consumption is down 24.2% since it peaked in 1999, noted Quinn. "Newsprint publishers have increased their campaign to reduce consumption by format (broadsheet to tabloid and web-width reductions) and page count (elimination of daily stock tables)," he said.

Graphs featured at:
http://www.editorandpublisher.com/eandp/columns/forestwebs_display.jsp?vnu_content_id=1003540342

Financial Focus

Federal Reserve Chairman Ben Bernanke told members of Congress February 28th that U.S. financial markets appear to be "working well" and are functioning normally, one day after the Dow posted its biggest one-day point loss since the market reopened after the Sept. 11 attacks.

Responding to a question from a member of the House Budget Committee, Bernanke said that the central bank was closely monitoring the stock market after the Dow slumped 416 points Tuesday amid a sell off in stocks worldwide.



Graph: **http://library.hsh.com/?row_id=91**

Next Federal Reserve meeting March 20-21

Bernanke said the sell off did not change the Fed's view on U.S. economic growth. "There is really no material change in our expectations for the U.S. economy since I last reported to Congress a couple weeks ago," he said.

"If the housing sector begins to stabilize and if some of the inventory corrections that are still going on in manufacturing begin to be completed, there is a reasonable possibility of strengthening of the economy sometime during the middle of the year," he added.

On Wall Street, stocks rebounded from Tuesday's selloff after Bernanke's comments.

"Some will say he passed with flying colors: he sounded reassuring," Tony Crescenzi, chief bond market strategist with Miller, Tabak & Co., told Reuters. "The Fed is still confident in this situation. It is his first real test after a financial event."

Still speculators say that the heightened chance of a rate cut is linked to a perception that investment risk is rising, heightened by a global equity market selloff sparked by a plunge in China's market and weak U.S. economic data.

We'll continue to watch the market as it will undoubtedly continue to fluctuate until the Fed's next meet in late March.

Learn more at:
http://money.cnn.com/news/specials/fed/

The Edge

Not since the mid-1970's has new freight car acquisitions sided with the railroads being the primary buyers. During the 1970 timeframe railroads came to a stark realization: the amount of money they were putting into infrastructure (rail, ties, people and systems) and locomotive equipment left little money to buy railcars.

During the 70's, 80's and early 90's, railroads encouraged private shippers to purchase their own boutique fleets (tank cars, specialty cars, or single use having one origin and destination). The trend widen in the mid-1990's until we saw between 80 and 90 percent of the new railcars being purchased in 2002 – 2005 by non-railroad buyers (e.g. lessors or shippers).

The message has been clear: If you want to ship a commodity that won't allow the railroads to increase railcar fleet utilization then you need to provide your own rail equipment.

So where are railroads concentrating on railcar ownership or control? To answer this question one needs to look at the revenue commodity mix and opportunity for increased utilization of railcars within that commodity mix.

- **Intermodal traffic** appears to be in the lead for many railroads, followed closely by coal, grain and chemicals. Intermodal railcars are largely provided by TTX (a railroad owned lessor).

- **Coal cars** are still largely provided by operating lessors and utilities (public and private) but have been subject of many pooling discussions in the past and given the importance of increased utilization will probably be part of a pool network at some point in the future (regardless of who owns the railcars).
- **Grain cars** are mixed between railroad owned and controlled and operating lessors. However the grain fleet is one where at least the western Class I railroads have successfully used a bid process and/or Dutch auction to successfully control the utilization on tens of thousands of railcars. And why not? Utilization has come from one turn per car every 30 to 45 days to 3 to 4 turns per month – that's productivity.

After you step away from the major volume commodities into the chemical world you see more private ownership for two reasons:

1. There is no utilization efficiency found in moving a car from point A to point B and back again, and
2. Railroads have successfully steered away from any hazardous type commodity for liability reasons.

When you look into the myriad of other commodities that railroads transport you can categorize the railroads fleet commitment to those areas where, from a marketing perspective, the railroad needs to provide railcars to haul the business (not necessarily from a utilization perspective) and to those areas where railcar utilization can be increased by backhauls in the same railcar (for example lumber and plate steel). If your commodity falls outside of this realm and doesn't have either a competitive bent or potential utilization efficiency gain you'll probably need to plan on providing your own railcars.

So far the message has been clear.

Times are changing though! In the past year the railroads have added another dimension that begs further consideration. The railroads have not only shifted from using price as a deterrent or enhancement to traffic but are also using the ability of shippers and private car owners to place railcars with the railroads as a way to manage their infrastructure and margins.

We've seen train-set restrictions placed on new aluminum coal trains causing train-sets to go from the railcar manufacturer to the storage track. The railroads message, we like aluminum coal cars because they carry approximately 10 more tons of coal than the steel ones – but we're not letting them on our system until you get rid of some of the steel sets first.

In December 2006 UP announced (Industrial Products announcement 2006-216) they were done supplying covered hoppers for salt. If you want to ship bulk salt you need to do it in your own cars. The message: this is an underutilized car type (seasonal) has little secondary opportunity and no distribution efficiency. Albeit they don't mind hauling the commodity from A to B but the shipper/receiver needs to take on the infrastructure requirements of owning the railcars and parking them in the off season.

On January 30, 2007 BNSF announced that is was in the process of divesting its fleet of woodchip gondolas used in woodchip service. Specifically, "As the fleet ages and cars are being retired, BNSF has determined that the economic returns do not justify reinvesting in this equipment type (i.e. extending the life of existing equipment or replacing aging equipment with new)." They advise that shippers who use BNSF woodchip gondolas begin making plans for replacing this transportation capacity. The BNSF is conveying the same message UP did on salt covered hoppers. If UP or BNSF finds a railcar type that is underutilized they're not only going to shift the responsibility of an underutilized asset off their books but are also going to shift the infrastructure requirements of supporting the railcars to the shipper.

Here at Tealinc, Ltd our message remains the same. If you’re not working on creating efficiencies for the railroads the railroads will help you either create those efficiencies or will force you to absorb the inefficiency. If we can help you identify your opportunities, please don’t hesitate to call on us.

We look forward to earning your business!