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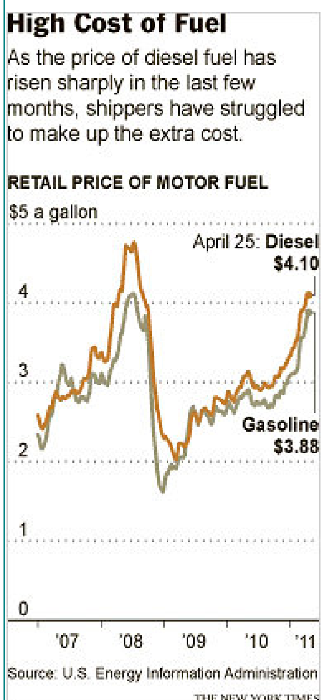
Shippers may raise fuel fees



"Simply to move all this stuff around, it is really hard to affect any cost savings. You have little in the way of alternatives"

Railroad Updates

These should be good times for railroads and trucking companies. After all, an improving economy means that more goods and commodities need to be delivered to the nation's ports and department stores.

But rising fuel prices have taken a toll on their business.

With diesel prices near their highest levels since 2008, the impact has started to appear in the first-quarter results of companies like Union Pacific, CSX, and Norfolk Southern railroad along with the Arkansas Best Corporation, which has a trucking subsidiary. Some shippers said they expected to raise fuel surcharges.

The timing, some economists say, could not be worse. Consumers are already paying steeper prices at the gas pump and may see prices climb in stores if diesel prices remain high. American manufacturers, meanwhile, are struggling to get back on their feet.

"The manufacturing sector is hit disproportionately hard by higher diesel prices," said Donald A. Norman, economist for the Manufacturers Alliance/MAPI, a public policy and economics research organization in Arlington, Va. "Simply to move all this stuff around, it is really hard to affect any cost savings. You have little in the way of alternatives."

Brandon Gale, the president of Retail Shipping Associates, said it was only a matter of time before the high fuel prices affected consumers. "It is a very straight-line relationship," he said. "When you see fuel at the pump going up, it is going to go up at the package, too."

Crude oil prices started going up early this year as turmoil spread through the oil-producing regions of the Middle East and North Africa. Increased global demand for fuel has added to the pressure on prices.

On Monday April 25, the average price for a gallon of highway diesel was $4.09, according to the Energy Information Administration, which posts fuel prices every week based on a survey of outlets around the country. The current averages are in the highest range since 2008, when prices peaked at $4.76 on July 14, and more than a dollar higher than in 2010.

The Energy Information Administration price functions as a reference point for trucking companies negotiating fuel surcharges with shippers. Railroads can use a less expensive type of diesel that does not reflect the highway taxes.

While some railroad companies say their businesses can benefit from higher diesel prices because shippers may migrate to trains from trucks, they are still paying millions of dollars more for fuel.

Union Pacific said in its report on the first quarter of 2011 that it paid

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Some cargo usually moves to trains when diesel prices are high because they are more fuel efficient than trucks

If what we saw in 2008 happens now, there will probably be some customers that will seek out rail service that have not in the past

Class I carriers reported a combined workforce of 155,842, up 1,340 from a month

average diesel fuel prices of $2.88 a gallon, up 33 percent from the same period in 2010. The higher costs — the company said it paid about $200 million more for fuel in the quarter than the same period in 2010 — sliced 8 cents off the company's $1.29 in earnings per share. Even so, the earnings were the company's highest for any first quarter in its history.

The company has already imposed fuel surcharges to recoup some of its higher costs. And while it did not say directly whether it would raise its surcharges, Tom Lange, a company spokesman, said, "It is how we are addressing it."

Another railroad company, the CSX Corporation, said in its first-quarter results report this month that higher fuel costs added $119 million to expenses in the year, bringing fuel costs to $402 million.

Norfolk Southern reported on Wednesday April 27 that railway operating expenses for the quarter were $2.0 billion, up 20 percent compared with first-quarter 2010. The increase was largely due to higher fuel costs, which rose by $135 million or 53 percent, primarily as the result of increased prices as well as the effects of an unfavorable arbitration ruling and higher traffic volumes.

Railroad companies can benefit in some ways from higher oil prices. When oil prices rise, so do the prices of other commodities, a signal of brisk demand for what is a large component of train freight.

"You can't look at rising oil prices in a vacuum," said H. Peter Nesvold, a managing director for research at Jefferies & Company. "It actually helps the volumes at the rails."

In addition, some cargo usually moves to trains when diesel prices are high because they are more fuel efficient than trucks, industry officials said.

"Fuel costs are an important factor for us; it costs us more money to do what we do," said John T. Gray, a senior vice president for the Association of American Railroads. "Fortunately, it costs our competitors typically more money than it costs us."

He added, "If what we saw in 2008 happens now, there will probably be some customers that will seek out rail service that have not in the past."

Read more at:
http://www.nytimes.com/2011/04/27/business/27surcharge.html?pagewanted=1&_r=1

US Freight Rails Hiring Rises Sharply

The seven largest freight railroads had more workers in their U.S. operations as of mid-March than any time since February 2009, the Surface Transportation Board reported.

Those Class I carriers reported a combined workforce of 155,842, the STB said, up 1,340 from a month earlier and the strongest for any time since the freight rail economy began to recover from the recession in mid-2009.

earlier and the strongest for any time since the freight rail economy in 2009

The jobs gains follow the 1,198 that the Class Is added to their U.S. lines from mid-January to mid-February. But unlike that month, all seven railroads increased jobs in late February through early March.

Top railroads report their employment levels to the STB as of the first mid-month payroll date, and it takes about a month after that for the agency to compile them into a single report.

The latest increases came as freight traffic was picking up from winter lows, but also as the rail network was trying to dig out from a series of winter storms and regain fluidity across the country. The railroads added nearly 700 track maintenance workers and nearly 400 for the much larger category of train crew members.

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BNSF Railway accounted for most of the mid-March job gains, adding 759 workers from that point in February. CSX Transportation was next with 228 net new workers.

Read the article at: **http://www.joc.com/rail-intermodal/us-freight-rails-hiring-rises-sharply**

AAR Updates

AAR presents DOT with list of 'obsolete' rules under federal review process

The Association of American Railroads (AAR) is urging the U.S. Department of Transportation (DOT) to modify six regulations that cost the industry hundreds of millions of dollars each year. AAR submitted the list in response to DOT's request for comments regarding regulations issued by the Federal Railroad Administration (FRA) that are deemed "obsolete, unnecessary, excessively burdensome, or counterproductive."

"We support this concept of periodically reviewing regulations, and believe DOT is setting a good precedent with this proceeding," said AAR President and CEO Edward R. Hamberger. "Railroads, like many other modern industries, are constantly innovating, implementing new technologies and finding ways to be safer and more productive. In doing so, railroads and the technology we use, have outpaced some of the rules and regulations related to how we operate. So now is a good time to bring our rules up to speed to meet the realities of railroading in the 21st Century."

Railroads are constantly innovating, implementing new technologies and finding ways to be safer and more productive

AAR presented six rules for DOT and FRA to consider, noting that the review proceeding is not addressing ongoing or recently concluded proceedings, such as the FRA's recent review of positive train control (PTC) regulations. In March, the FRA and AAR agreed to put a federal lawsuit on hold while the agency undertakes two separate rulemakings to revisit the most costly federal mandate in U.S. railroad history.

The following are the areas that AAR asked DOT and FRA to revise regulations to better apply to today's modern railroad operating environment.

Locomotive Inspections – The concept of daily and periodic locomotive inspections dates back to the steam engine era of railroading. Today's modern diesel locomotive is equipped with electronic and self-diagnostic technology that negates the need to stop to inspect them daily or even

AAR asked DOT and FRA to revise regulations to better apply to today's modern railroad operating environment on Locomotive Inspections, Track Inspection Technology, Guard Face/ Check Gage Standards, Intermediate Brake Tests, Signal Inspections and Diesel Exhaust

periodically. The current FRA rules require daily and periodic inspections every 92 days, costing the nation's major freight railroads over $400 million annually. AAR noted there is no proof that current inspection regulations are necessary to keep low or reduce locomotive defects tied to accidents.

***Track Inspection Technology* –** FRA requires that minor defects that are irrelevant from a safety perspective be addressed immediately under FRA regulations. Railroads use track geometry and ultrasonic equipment that can detect very small rail defects. As a consequence, these modern inspection technologies result in railroads being forced to address defects that do not need immediate attention. AAR urged FRA to review its requirements, which the U.S. Government Accountability Office (GAO) has said could serve as a disincentive to the use of sophisticated technologies used to detect track flaws that pose greater concern to safety and operational efficiency.

***Guard Face/Check Gage Standards* –** FRA has overly stringent standards for guard-check gage and guard-face gage in frogs, a track structure used at the intersection of two running rails. While the agency often cites railroads for violation of these minimum standards, AAR is unaware of deviations from the standard being a factor in any derailment. AAR urged FRA to review these standards which seemingly provide no clear safety benefit.

***Intermediate Brake Tests* –** FRA requires that every 1000-1500 miles, railroads must inspect brakes en route to determine if they are properly applying and releasing. For trains equipped with electronically controlled brakes, the interval is 3500 miles. However, modern technology, such as wheel temperature detectors, has made these visual inspections obsolete. AAR urged FRA to revise its rules to eliminate intermediate brake tests where wheel temperature detectors are used.

***Signal Inspections* –** FRA has multiple periodic inspection requirements for railroad signals, which also do not take into account advances in modern railroad operations and technology. Railroads are increasingly relying on electronic health monitoring to provide status updates on equipment. AAR urged FRA to revise its rules to reflect the use of technology in monitoring the health of railroad signals.

Diesel Exhaust – While FRA has applied permissible diesel exhaust exposure limits as outlined by the Occupational Safety and Health Administration (OSHA) rules, the agency's wording in its own version of the rule has created confusion. In fact, misinterpretation of its rule – which has been interpreted as prohibiting even one molecule of diesel exhaust in the cab – has set an impossible standard for railroads to meet. AAR urged FRA to amend its rules to more clearly apply OSHA's standards.

Read the entire article at: **http://www.aar.org/NewsAndEvents/Press-Releases/2011/04/04-DOT.aspx**

Railroad Traffic

March freight rail traffic increases as

The Association of American Railroads (AAR) reported April 11, 2011 that monthly rail carloads in March 2011 increased 3.4 percent compared with

economy continues to show signs of recovery

the same month last year, for a total of 1,493,553 carloads. According to AAR's monthly *Rail Time Indicators* report, intermodal traffic in March increased 8.5 percent for a total of 1,111,301 trailers and containers compared with March 2010. On a seasonally adjusted basis, carloads were up 2 percent and intermodal was up 0.5 percent over February 2011.

"As the economy steadily improves, rail traffic is continuing to make gains as well," said AAR Senior Vice President John Gray. "And we are seeing intermodal traffic make larger gains with the containerization trend continuing. Containers accounted for 85 percent of intermodal traffic in the first quarter of this year."

March also saw the addition of 1,198 employees, bringing the total number of Class I rail employees to 154,502 nationwide. As of April 1, 2011, 283,649 freight cars, or 18.7 percent of the fleet, remain in storage. This represents a decrease of 22,667 cars from March 1, 2011.

March 2011 marks the thirteenth straight month for carload and the sixteenth straight month for intermodal traffic increases on a year-over-year basis

March 2011's carload traffic percentage increase is the lowest of any month since early 2010 due, in part, to strengthening rail traffic volumes in the 2010 comparison month. Despite that, March 2011 marks the thirteenth straight month for carload and the sixteenth straight month for intermodal traffic increases on a year-over-year basis, showing the continued gradual upward trend in rail traffic.

Overall, 15 of 20 commodity categories saw carload gains on U.S. railroads in March 2011 compared with March 2010. Traffic gains were led by metallic ores, up 45.8 percent; motor vehicles and parts, up 17.6 percent; pulp and paper products, up 16.2 percent, and petroleum and petroleum/coal products, up 14.5 percent. Of the five commodity categories reporting declines for the month only two saw significant decreases: primary forest products, down 15.4 percent, and waste and nonferrous scrap, down 11.7 percent.

Coal carloads continue to suffer from reduced electricity demand, with U.S. railroads originating 673,977 carloads in March 2011, up 0.1 percent over March 2010. In March 2011, U.S. railroads originated a total of 158,240 carloads of chemicals, up 10.2 percent over March 2010, and averaged 31,648 carloads per week. This represents the highest weekly average for chemical carloads for any month in history, likely due to increasing volumes of ethanol shipped largely by rail.

Learn more at: **http://www.aar.org/NewsAndEvents/Press-Releases/2011/04/11-RTI.aspx**

Industrial Inside

A Yellow investment that's outshining gold

Plunging into commodities might not be your thing, but they are one of the main games in the marketplace this year — and a way to fight back against inflation. [And it's not just talk about precious metals.] There are other commodities and commodity exchange-traded funds (ETFs) worth your attention right now.

For instance, corn prices are also hitting new highs, and are now back to levels last seen at the peak of crude oil prices in mid-2008. Furthermore,

Scarcity combined with rising demand from China causes corn prices to skyrocket

inventories are reported to be at 15-year lows — and they are still declining, according to analysts. This is a surprise in a way, because higher prices should have killed demand by now.

Yellow corn is up more than 120% in the past year

It's a little hard to believe, but you know the big hubbub about physical gold hitting new heights, up more than 20% in the past year? But the shiny yellow metal has got nothing on physical ears of golden kernels. Yellow corn — the type fed to animals being prepared for slaughter, as well as to ethanol refineries — is up more than 120 percent in the past year.

The problem is scarcity. Weather has been bad, and not enough was planted.

"Essentially, we don't have any corn. That's the bottom line," said Sterling Smith of Country Hedging, a commodity broker in St Paul, Minn., to the *Financial Times.*

40% of 2010 U.S. corn was turned into 900,000 barrels a day of ethanol

It's a paradox that these higher prices haven't yet affected core inflation enough to worry the Federal Reserve — or even make a dent in demand. Smithfield Foods (NYSE: SFD), a major pork producer, told investors that it has not seen any "consumer fatigue [due] to pricing."

Of course, a lot of this corn is going into our cars. The Department of Agriculture estimates that 40% of last year's U.S. crop was turned into 900,000 barrels a day of ethanol. One reason is that rising crude oil prices have kept the cost of "corn oil" competitive.

We can expect the situation to go from serious to critical if U.S. cornfield yields

We can expect the situation to go from serious to critical if U.S. cornfield yields are threatened over the rest of this year. And if crude oil moves toward the $150-plus area, which [the author] expects due to an acceleration of turmoil in the Middle East, then this rally in corn may be just getting started.

are threatened over the rest of this year

The ETF for corn prices is Teucrium Corn Fund (NYSE: CORN), and it has traded as many as 250,000 shares a day in the past few weeks, though the average is around 100,000.

Where will future demand come from? It looks like China, according to a Barclays' analyst in a recent Bloomberg report.

The analyst, Sudakshina Unnikrishnan, told the wire: "The problem really is that we haven't seen any letup in Chinese demand."

And a Macquarie Group analyst added that risks to the U.S. crop from snow, cooler weather and increased global demand may help push corn to a record $10 a bushel as early as June.

China is "increasingly becoming more reliant on imports because of domestic diet conditions and inventories"

Imports by China "could be as high as 2.5 million metric tons, easily double that of last year," said Unnikrishnan, who correctly predicted in November that increased cotton purchases by China would help drive prices to an all-time high.

China is "increasingly becoming more reliant on imports because of domestic diet conditions and inventories," she told Bloomberg.

The main reason for the rise of corn demand in China has been to feed animals, as the real increase is in protein consumption. A JPMorgan analyst told the wire service: "People are getting wealthier, so they eat more meat. That's why you need feed, soybeans and corn to feed the livestock with."

Read the article at: **http://www.investorplace.com/38689/corn-etf-outperforming-gold/**

Financial Focus

Bernanke: inflation to rise under moderate growth

Federal Reserve Chairman Ben Bernanke said the economic recovery is expected to proceed at a moderate pace as he discussed the Fed's economic projections during his first press conference following a statement from the Federal Open Market Committee on Wednesday April 27, 2011.

Projections for 2011 economic growth were lowered to 3.1 - 3.3 percent from January's range of 3.4 - 3.9 percent and projections for 2011 core inflation were raised to 1.3 - 1.6 percent from 1 percent to 1.3 percent. Unemployment is now expected to fall between 8.4 percent and 8.7 percent in 2011, compared with prior expectations for a range of 8.8 percent to 9 percent.

Fed is looking for stronger job creation and confidence that the recovery is sustainable

While taking questions from the press, Bernanke said the Fed's use of the "extended period" language is dependent on resource slack and expectations for inflation. He said the Fed is looking for stronger job creation and confidence that the recovery is sustainable. While the central bank expects that inflation will come down to a more normal level, the Fed is also watching to make sure that inflation expectations "remain well-anchored." Bernanke added the language suggests that the Fed won't make

The Committee voted to keep the target interest rate at zero to 0.25%

any drastic changes to monetary policy but that the economy will largely dictate the pace of policy action.

The briefing, which is meant to increase transparency at a time when rising food and energy prices have triggered concerns about the Fed's ability to keep inflation in check, follows an FOMC statement that offered little new information. The Committee voted to keep the target interest rate at zero to 0.25 percent, maintained language promising to keep interest rates low "for an extended period," and made no changes to its $600 billion asset-purchase plan.

The Committee acknowledged recent increases in inflation but repeated expectations that it will be "transitory" and reiterated its promise to "pay close attention to the evolution of inflation and inflation expectations."

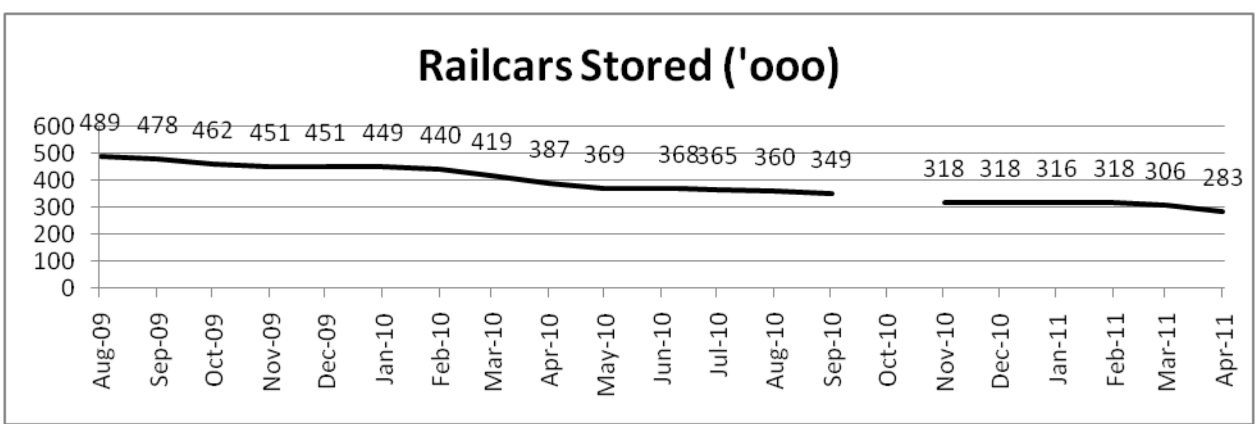
Read the article at:
http://www.thestreet.com/story/11096532/1/bernanke-inflation-to-rise-under-moderate-economic-growth.html?cm_ven=GOOGLEN

The Edge

Volatile is probably the word of choice for those of us involved in the transportation industry.

Some of the Key Drivers we've experienced are:

- Over 100,000 railcars pulled out of storage the either went back to work or to the scrap yard (see chart below)
- General increase in overall traffic (rail, truck, barge) with exception of any traffic related to the housing or construction industry
- General increase in new railcar orders with a concern on where all the castings are going to come from to timely supply the market
- Steep ramp-up in service requirements by all railroads with most requirements being woefully met by most railroads.



What's driving this market and is it sustainable?

What's causing the volatility?

- We made a strong statement last month and continue to believe that the export market continues to drive the transportation market in the US. Coal and grain shipments to both east and west coast ports continue to move at a very strong pace. These commodities require a significant amount of resources comprised of crews, track, equipment, locomotives and time to move.
- Railroad service generally lags demand and that case is proven over the past several months. We've discussed service issues on railroads with all sorts of commodity shippers and receivers from box car folks to bulk grain, grain products, coal, lumber and aggregate producers and receivers. All but one is satisfied with their service at the current time. We're not knocking the railroads. Railroads employ a tremendous amount of capital and operating resources to move a single ton of product. A lot of these resources are paid in hourly time increments. If they're not fully employed then the railroad doesn't make a return on their investment and in turn must increase the top line (read rate increases) to offset costs.
- There is flat domestic demand with rare exception of a few select industries enjoying an uptick in domestic output of more finished goods to replace import good interruptions.
- Natural disasters are also playing a large role in the current situation of delivery and service. There has been and continues to be prolonged and major flooding throughout river valley areas of the US. Tornados in certain areas have devastated plants and shipment operations.

What can you do as a shipper or receiver?

- Plan for interruptions. The cost of carrying additional inventory versus running out needs to be part of your overall equation. Figure out which hurts less and plan accordingly.
- Increase your underlying supply chain. Order or support more truck, rail or barge shipments. If necessary supplement railroad supplied equipment with private equipment.
- Understand exact service provisions by the transport mode in which you're working. Will the truck, barge or railroad be able to deliver your goods when required? If not what back up plan should you have in place to negate service interruptions?

Remember volatile times create opportunities if you're prepared for them.

We look forward to earning your business!