Touchbase

November 2007

In This Issue

- Railroad Updates
- AAR Updates
- Railroad Traffic
- Industrial Inside
- Financial Focus
- The Edge

Visit us at:
www.tealinc.com

Changes to BNSF Intermodal Storage Policy Effective November 5, 2007

CSXT Fuel Surcharge Will Change November 1, 2007

Railroad Updates

BNSF continues to review and modify its operating practices and service offerings in order to maintain network fluidity and improve service consistency.

As a result, BNSF is changing its Intermodal storage policy, which will apply to all Intermodal service levels and equipment types, effective November 5, 2007. Highlights of the simplified policy are summarized below:

Additional free time:

- At all facilities, Sundays will not be charged storage or be counted in the free time calculation (if free time has not expired)
- Reduced number of 24 hour (Group 1) facilities (from 8 to 3)
- No changes in daily rates if notification is made after 5:00 p.m. (local time), the day of notification is the following day

The new policy is effective for shipment notification that occurs on or after November 5, 2007. BNSF will continue to evaluate facility and operational efficiencies, and make changes to policies and procedures as needed to improve fluidity.

For a comprehensive overview of the policy changes and to find out more, read the entire article at:
http://newdomino.bnsf.com/website/updates.nsf/updates-marketing-consumer/A542E2E377A1D9138625736900585937?Open

CSXT HDF/Mileage Based Fuel Surcharge to Change November 1

The highway diesel fuel/mileage based fuel surcharge is published in CSXT Fuel Surcharge Publication 8661 and applies to all regulated linehaul freight rates existing or established by CSXT on or after April 23, 2007. It also applies to all linehaul freight rates and charges with respect to exempt, contract, private or other pricing documents that reference CSXT Publication 8661 on or after April 23, 2007.

The CSXT HDF/mileage based fuel surcharge of 22 cents per mile, which became effective October 1, 2007, will change to 24 cents per mile for shipments having a bill of lading dated on or after November 1, 2007.

The 24 cents per mile fuel surcharge is based on the "HDF Average Price" of 295.3 cents per gallon for the calendar month of September 2007. The "HDF Average Price" is on U.S. No. 2 Diesel Retail Sales by All Sellers, as determined and published by the U. S. Department of Energy, Energy Information Administration at www.eia.doe.gov.

CSXT WTI Fuel Surcharge

The CSXT WTI fuel surcharge is published in Tariffs CSXT 8100 and CSXT 8200 (Coal) and applies to all regulated common carrier linehaul

Following are the CSXT HDF/mileage based fuel surcharge rates for 2007:

- **April: $0.13/mile**
- **May: $0.17/mile**
- **June: $0.21/mile**
- **July: $0.20/mile**
- **Aug.: $0.21/mile**
- **Sept.: $0.22/mile**
- **Oct.: $0.22/mile**
- **Nov. $0.24/mile**

Reporting shows that the UP had a fuel expense recovery shortfall of $1.013 billion between January of 2003 and the end of March 2007. This means only 77% of increased fuel costs were recovered during that period.

Only 89% of their incremental fuel costs were recovered during the first quarter of 2007

freight rates and charges with respect to exempt, contract, private or other pricing documents that do not reference CSXT Fuel Surcharge Publication 8661.

The CSXT WTI fuel surcharge of 20.0%, which became effective October 1, 2007, will change to 22.8% for shipments having a bill of lading dated on or after November 1, 2007.

Read the entire article:
wwwhttp://www.csx.com/?fuseaction=customers.news-detail&i=27511

Union Pacific's Response to ACC Fuel Surcharge Study

On September 14, Jack Koraleski of the Union Pacific Railroad released the following statement to UP customers concerning the ACC Fuel Surcharge Study.

> "The media reported [September 13, 2007] that the American Chemistry Council, a Washington, D.C. based lobbying group, has released a 'study' claiming that Union Pacific was among a group of railroads that over-charged for fuel during the past several years.
>
> While commissioning a privately managed study is a well-known lobbying tactic in Washington, this particular project sets new standards for data manipulation and selective use of the facts. Since the issue of fuel surcharges is important to many of you, I think it is important to correct the record.
>
> Union Pacific has publicly reported data on its fuel surcharge program since 2003. The data we reported included fuel consumption, average price per gallon, fuel surcharge revenue, and incremental fuel expense. This information is included in audited financial statements including the company's Form 10-Q, which is filed with the Securities and Exchange Commission. There is no question of its accuracy.
>
> Truthful reporting shows that Union Pacific had a fuel expense recovery shortfall of $1.013 billion between January of 2003 and the end of March 2007. This means we recovered only 77% of our increased fuel costs during that period. We recovered 89% of our incremental fuel costs during the first quarter of 2007.
>
> Obviously, the differences between the actual audited numbers and the conclusions of the ACC "study" will become clear as a detailed analysis of it is completed during the next few weeks. But the charges against our company are so outrageous that I felt compelled to highlight the truth immediately."

Read the entire statement at:
http://dx01.my.uprr.com/pubdir/inetbull.nsf/10ad5b33cfbd82148625705a000ea680/455ae79adf4d09cc862573560078960f?OpenDocument

AAR members include the major freight railroads in the U.S., Canada and Mexico, as well as Amtrak and several short line holding companies. Based in Washington, DC, the AAR is committed to keeping the railroads of North America safe, fast, efficient, clean, technologically advanced, and secure

AAR Updates

If you are new to the Rail Industry or even an experienced veteran, it is important to understand who the A.A.R. is and what role they play in your transportation process. Over the past month we have received notifications that numerous Open Top Loading Rules have been altered, changed or are under revision. These loading rules impact how your team secures loads on a number of different railcar shipments including flatcars, open tops, gondolas, coil cars, etc.

If you are curious as how your company is impacted, most Class I railroads can easily supply this information or for a yearly subscription fee you may register for the AAR Circulars. If you have questions or are curious as to how loading rules have changed pertaining to your commodity, we will be happy to help you do some research to get you up to speed with the proper AAR mandated process. You may also contact the AAR for further directives.

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

Railroad Traffic

September chemicals, grain carloads up; metals and metal products, crushed stone, sand and gravel, lumber products carloads down

U.S. railroads originated 1,340,285 carloads of freight in September 2007, down 11,536 carloads (0.9 percent) from September 2006, the Association of American Railroads (AAR) reported today. U.S. railroads also originated 963,278 intermodal units in September 2007, a decrease of 24,625 trailers and containers (2.5 percent) over September 2006.

Five of the 19 major commodity categories tracked by the AAR saw U.S. carload increases in September 2007 compared to September 2006. U.S. intermodal traffic is not included in carload figures.

Commodities showing carload gains in September 2007 included chemicals (up 7,669 carloads, or 6.7 percent, to 121,901 carloads); coal (up 6,533 carloads, or 1.1 percent, to 575,331 carloads); and grain (up 6,195 carloads, or 6.9 percent, to 96,009 carloads).

For the first nine months of 2007, total U.S. rail carloads were down 426,513 carloads (3.2 percent) to 12,707,878 carloads.

Commodities showing carload decreases in September 2007 included metals and metal products (down 13.5 percent,); crushed stone, sand, and gravel (down 5.6 percent); and lumber or wood products (down 16.5 percent).

In the third quarter, total carloads on U.S. railroads fell 1.6 percent. Carloads of chemicals rose 3.8 percent, while grain carloads rose 4.3 percent. Carloads of crushed stone and gravel fell 8.2 percent in the third quarter; carloads of metals and metal products were down 12.0 percent; and carloads of lumber and wood products were down 16.1 percent.

U.S. intermodal traffic was down 101,458 trailers and containers (3.2

"Traffic this year is still down a bit from the record-setting pace of 2006, but there is no doubt that over the longer term freight transportation demand will continue to grow"

percent) in the third quarter and was down 178,842 trailers and containers (1.9 percent) for the first nine months of 2007 to 9,024,633.

Total volume for the first 39 weeks was estimated at 1.31 trillion ton-miles, down 1.7 percent from 2006.

"Traffic this year is still down a bit from the record-setting pace of 2006, but there is no doubt that over the longer term freight transportation demand will continue to grow," noted AAR Vice President Craig F. Rockey. "The U.S. Department of Transportation estimates that demand for freight rail service will increase 88 percent by 2035.

According to a recent study by Cambridge Systematics, in addition to huge sums needed to maintain our existing freight rail infrastructure, approximately $148 billion must be invested to expand our freight rail network over the next three decades to make sure that adequate rail capacity exists to meet future demand. If these capacity enhancements aren't made, everyone in the country will feel the impact."

Combined cumulative rail volume for the first 39 weeks of 2007 on 13 reporting U.S. and Canadian railroads totaled 15,747,208 carloads, down 2.8 percent (455,038 carloads) from last year, and 10,833,394 trailers and containers, down 1.2 percent (129,272 units) from 2006's first 39 weeks.

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

Industrial Inside

Investment in fuel ethanol distilleries has soared since the late-2005 oil price hikes

Farmers, feeders, food processors, ethanol investors, and grain-importing countries are basing decisions on incomplete data

Investment in fuel ethanol distilleries has soared since the late-2005 oil price hikes, but data collection in this fast-changing sector has fallen behind. Because of inadequate data collection on the number of new plants under construction, the quantity of grain that will be needed for fuel ethanol distilleries has been vastly understated. Farmers, feeders, food processors, ethanol investors, and grain-importing countries are basing decisions on incomplete data.

The U.S. Department of Agriculture (USDA) projects that distilleries will require only 60 million tons of corn from the 2008 harvest. But [according to the] Earth Policy Institute (EPI), estimates that distilleries will need 139 million tons [are more realistic]—more than twice as much. If the EPI estimate is at all close to the mark, the emerging competition between cars and people for grain will likely drive world grain prices to levels never seen before. The key questions are: How high will grain prices rise? When will the crunch come? And what will be the worldwide effect of rising food prices?

One reason for the low USDA projection is that it was released in February 2006, well before the effect of surging oil prices on investment in fuel ethanol distilleries was fully apparent. Beyond this, USDA relies heavily on the Renewable Fuels Association (RFA), a trade group, for data on ethanol distilleries under construction, but the RFA data have lagged behind movement in the industry.

According to the EPI compilation, the 116 plants in production on December 31, 2006, were using 53 million tons of grain per year, while the 79 plants under construction—mostly larger facilities—will use 51 million tons of grain when they come online. Expansions of 11 existing plants will use another 8 million tons of grain (1 ton of corn = 39.4 bushels = 110 gallons of ethanol).

As the world corn price rises, so too do those of wheat and rice.

In addition, easily 200 ethanol plants were in the planning stage at the end of 2006. If these translate into construction starts between January 1 and June 30, 2007, at the same rate that plants did during the final six months of 2006, then an additional 3 billion gallons of capacity requiring 27 million more tons of grain will likely come online by September 1, 2008, the start of the 2008 harvest year. This raises the corn needed for distilleries to 139 million tons, half the 2008 harvest projected by USDA. This would yield nearly 15 billion gallons of ethanol, satisfying 6 percent of U.S. auto fuel needs. (And this estimate does not include any plants started after June 30, 2007, that would be finished in time to draw on the 2008 harvest.)

This unprecedented diversion of the world's leading grain crop to the production of fuel will affect food prices everywhere. As the world corn price rises, so too do those of wheat and rice, both because of consumer substitution among grains and because the crops compete for land. Both corn and wheat futures were already trading at 10-year highs in late 2006.

With corn supplies tightening fast, rising prices will affect not only products made directly from corn, such as breakfast cereals, but also those produced using corn, including milk, eggs, cheese, butter, poultry, pork, beef, yogurt, and ice cream

With corn supplies tightening fast, rising prices will affect not only products made directly from corn, such as breakfast cereals, but also those produced using corn, including milk, eggs, cheese, butter, poultry, pork, beef, yogurt, and ice cream. The risk is that soaring food prices could generate a consumer backlash against the fuel ethanol industry.

Fuel ethanol proponents point out, and rightly so, that the use of corn to produce ethanol is not a total loss to the food economy because 30 percent of the corn is recovered in distillers dried grains that can be fed to beef and dairy cattle, pigs, and chickens, though only in limited amounts. They also argue that the U.S. distillery demand for corn can be met by expanding land in corn, mostly at the expense of soybeans, and by raising yields. While it is true that the corn crop can be expanded, there is no precedent for growth on the scale needed. And this soaring demand for corn comes when world grain production has fallen below consumption in six of the last seven years, dropping grain stocks to their lowest level in 34 years.

From an agricultural vantage point, the automotive demand for fuel is insatiable. The grain it takes to fill a 25-gallon tank with ethanol just once will feed one person for a whole year. Converting the entire U.S. grain harvest to ethanol would satisfy only 16 percent of U.S. auto fuel needs.

It is time for a moratorium on the licensing of new distilleries, a time-out, while we catch our breath and decide how much corn can be used for ethanol without dramatically raising food prices. The policy goal should be to use just enough fuel ethanol to support corn prices and farm incomes but not so much that it disrupts the world food economy. Meanwhile, a much greater effort is needed to produce ethanol from cellulosic sources such as switchgrass, a feedstock that is not used for food.

Findings have suggested larger impacts on corn prices than had previously been predicted, and pointed to eventually negative margins in ethanol production at a time when promoters were claiming that little could derail the ethanol train

Ethanol Production Breakdown

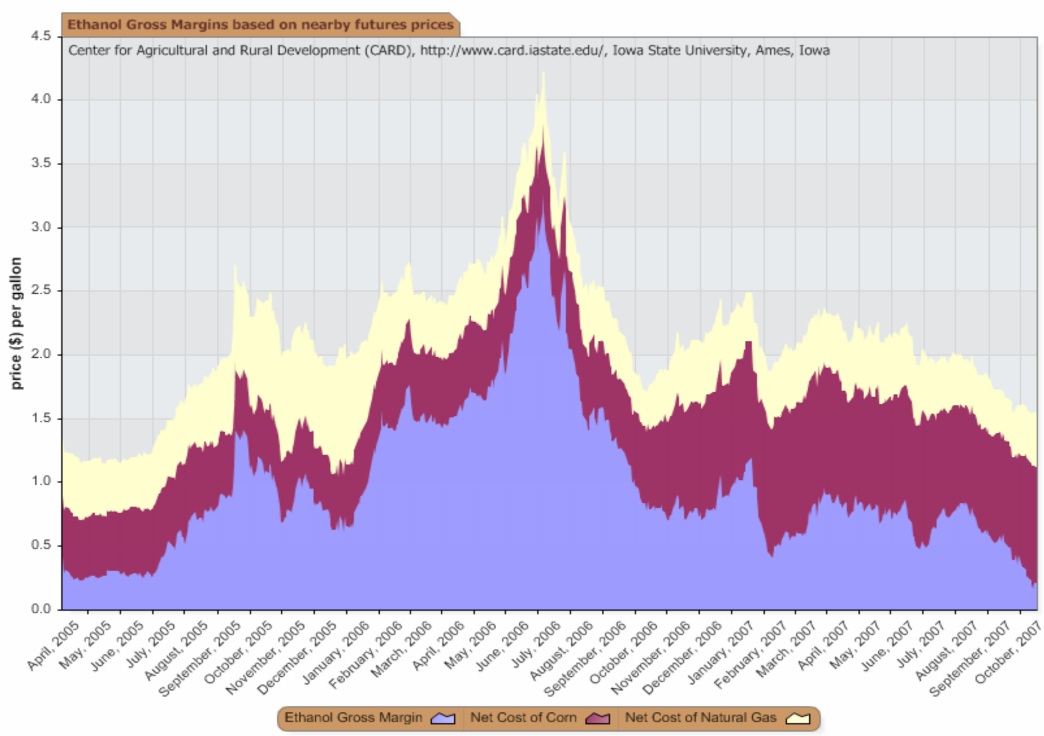
During the first week of October, the announcement that VeraSun is suspending work on an Indiana ethanol plant underscored the economic impact of "irrational exuberance" in any market.

Iowa State University's Center for Agricultural and Rural Development (CARD) has been taking what appears to me to be a brutally objective look at the ethanol business for the past couple of years. Bruce Babcock and Dermot Hayes and their colleagues have probably not been on the ethanol industry's dinner party invitation list after the publication of their work. Their.

GRAPH NOTE:

This ethanol price (represented by the top of the buff-colored area) is the lowest it has been since mid-2005, when the market really started to respond to higher oil prices. In addition, corn now accounts for much more of the cost of producing ethanol, while natural gas costs, which surged in late 2005, are near what appears to be a normal level.

Figure 1 shows the most recent estimates from CARD regarding the financial performance of ethanol producers. The graph breaks the total price of ethanol into the amounts spent for natural gas, corn and margin above gas and corn costs. This graph is based on $1.55/gal. of ethanol, $3.69/bu. for corn and $7.05/mm/BTU in natural gas costs.



The shocking part of this graph is the decline of the blue area, which represents gross margin over corn and energy costs. It is not a net margin. Ethanol producers must still pay labor, transportation, overhead and fixed costs out of these funds before arriving at a net

What may be more important is that it

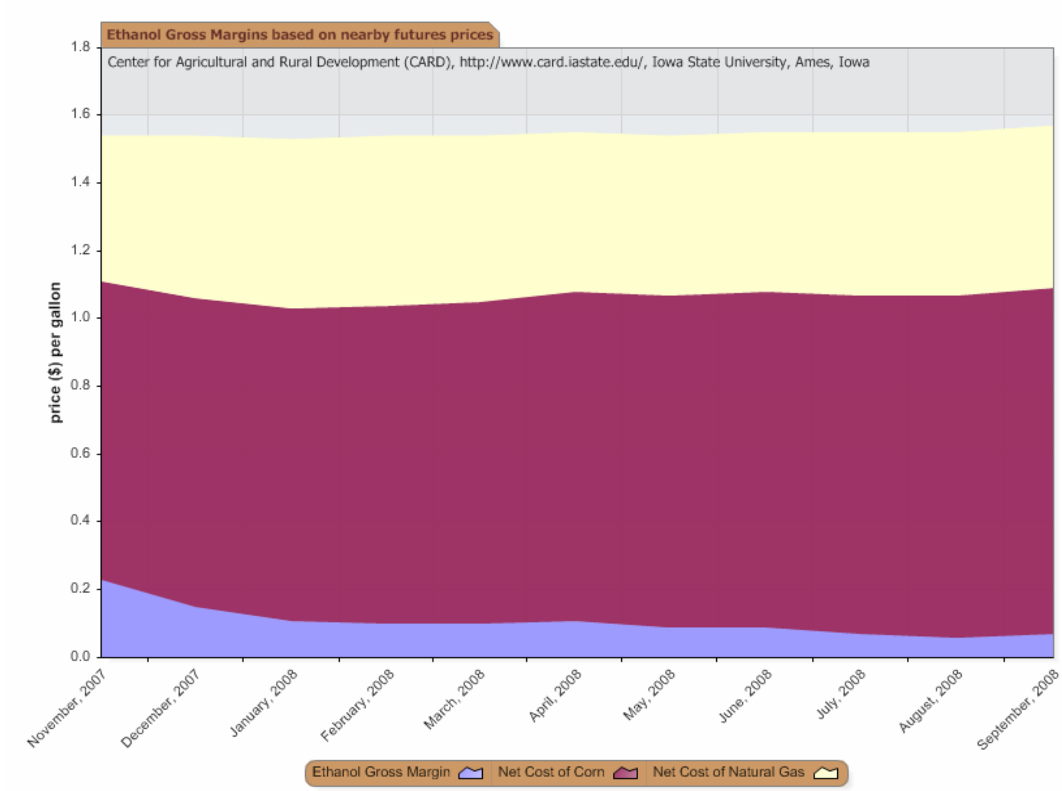
doesn't appear that things are going to get better for ethanol producers any time soon

GRAPH NOTE:

Figure 2 shows the same CARD calculations based on ethanol, corn and natural gas futures. The blue area representing gross margin becomes just a sliver at the end of 2008, even with a stable ethanol price

Plants will continue to operate as long as they can cover variable costs. Corn and energy (whether natural gas or coal) are the primary components of those variable costs, so it appears that as long as there is any blue area in these graphs, corn will still go into ethanol

profit. That gross margin hit a new low for the time period covered here three weeks ago -- and it has improved little since then.



Does all of this mean the demise of the ethanol business? No. There is a lot of momentum here. Investors are not going to leave plants half-built. The Indiana plant apparently had site work done but no work had commenced on structures. They will complete the plants that are under construction and that will roughly double our current ethanol capacity by late 2008 or early 2009.

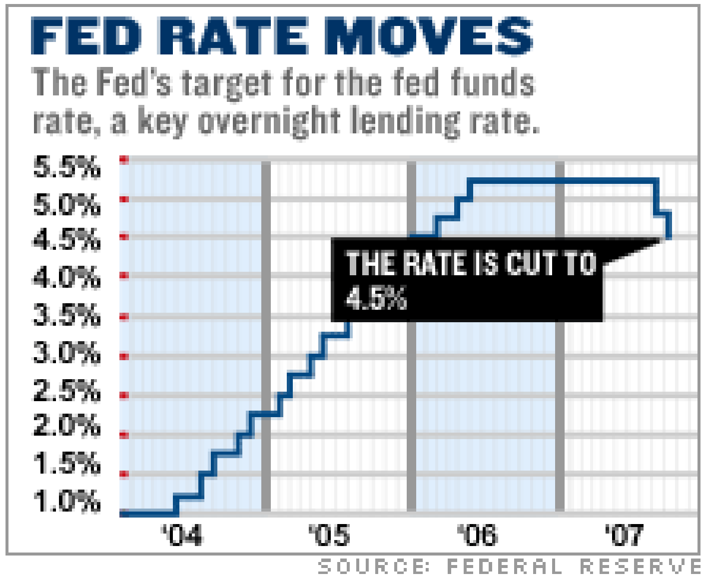
In addition, plants will continue to operate as long as they can cover variable costs. Corn and energy (whether natural gas or coal) are the primary components of those variable costs, so it appears to me that as long as there is any blue area in these graphs, corn will still go into ethanol.

Corn demand is still going to be higher than in the past. The question is whether anyone -- ethanol makers included -- will make any money.

Adapted from:
http://nationalhogfarmer.com/images/1012mkt.doc and
http://www.treehugger.com/files/2007/01/ethanol_distill.php

Financial Focus

The Federal Reserve lowered the target or a critical short-term interest rate by a quarter of a point Wednesday October 31, citing continued concerns about weakness in the housing market.



Citing turmoil in the housing market, Bernanke and Co. lower a key short-term rate by a quarter of a point to 4.5 percent to keep the economy on track. But the central bank also said it's worried about inflation

But the Fed indicated that it is also worried about inflation, a possible sign that the central bank may not cut rates again at its next meeting in December.

The widely-expected move comes on the heels of a half-point rate cut by the central bank in September and leaves the federal funds rate at 4.5 percent, its lowest level since January 2006.

Move comes on the heels of a half-point rate cut by the central bank in September and leaves the federal funds rate at 4.5 percent, its lowest level since January 2006.

Not all of the Fed's policy committee members voted in favor of a rate cut, however. Thomas Hoenig, president of the Federal Reserve Bank of Kansas City, preferred no change to the federal funds rate. The Fed also lowered its largely symbolic discount rate by a quarter of a point to 5 percent. That decision was unanimous.

The federal funds rate, an overnight lending rate for banks, is important to the economy since it influences how much interest consumers pay on credit card debt, home equity lines of credit and auto loans. It also impacts how much it costs corporations to borrow money.

Weakness in the housing market and problems with subprime mortgages - loans made to those with less-than-perfect credit - have led to billions of dollars in writedowns at major financial institutions. For this reason, most investors believed the Fed would lower rates again in an attempt to limit the mortgage meltdown's spillover into the broader economy.

The Fed acknowledged the danger of the housing problems. "[T]he pace of economic expansion will likely slow in the near term, partly reflecting the intensification of the housing correction," the Fed said in its closely watched statement.

"Housing will continue to be a drag," said Thomas di Galoma, head of

Dollar hits new low after rate cut

Fed also said that it felt Wednesday's rate cut, combined with the rate cut in September, "should help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets"

With the dollar weakening against other global currencies, some fear that further rate cuts could fuel even more inflationary pressures

U.S. Treasury trading with Jefferies & Co.

"If the Fed sees weaker housing data, they probably will drop rates another quarter point later this year. In the back of everyone's mind, people are wondering how will banks and brokers come out of this. Those fears are not going away overnight," di Galoma added.

But the Fed also said that it felt Wednesday's rate cut, combined with the rate cut in September, "should help forestall some of the adverse effects on the broader economy that might otherwise arise from the disruptions in financial markets."

And some market observers have expressed concerns that with oil prices rising above $90, inflation may still be a threat. So the Fed could be making a mistake by lowering interest rates further, some maintain.

With the dollar weakening against other global currencies, some fear that further rate cuts could fuel even more inflationary pressures.

"This is a hemlock situation. The rate cuts will be self-defeating," said Haag Sherman, co-founder and managing director of Salient Partners, an asset management division of investment bank Sanders Morris Harris Group. "The more you cut rates, the more dollar depreciation you will see and ultimately more pressure on commodity prices like oil and gold."

To that end, the Fed said in its statement that "recent increases in energy and commodity prices, among other factors, may put renewed upward pressure on inflation."

Learn more at:
http://money.cnn.com/2007/10/31/news/economy/fed_rates/index.htm

The Edge

This month I've decided to do an extrapolation (maybe rambling) of several topics that may be of interest to our readers.

Rail Customers Slow Shipments. The customers of the railroad industry appear to be in a chaotic state. As extrapolated in this newsletter, major commodity areas have been hard hit in recent times (including the dollar exchange with foreign currencies).

When one looks at AAR statistics, commodities hauled continue to decline. Class I railroads are off approximately 3.2% in originated carloads for the first 35 weeks of 2007 verse 2006 and the only bright spots are chemicals and petroleum, up 2.3% and 5.7% respectively.

Creation of additional local demand by the ethanol industry continues to affect the corn transportation numbers shifting much of this additional tonnage to local truck. It appears that this has been offset somewhat by the movement of Dried Distillers Grain (DDG) into the feed market to replace the void left by the corn price run up. One would expect feed wheat to do likewise but $5 to $8 cash wheat (basis adjusted) in the country forces much of this grain into normal human consumption channels.

Not surprisingly, the housing slump (look up sub-prime mortgage industry write down / write off on the internet) looks to continue affecting lumber, lumber products and related commodities such as stone, clay, glass, and, to a lesser degree, aggregates. In many cases. large capital investment return requirements will require continue churning out of products but probably not at the same pace as we saw a year ago.

What's bright on the horizon? Intermodal appears to be holding up as we continue to consume as a nation.

M&A Activity. On the Mergers and Acquisitions front we've seen a couple of bold steps. CN-EJE and CP-DM&E both appear to be leading the pack. They appear to have made these steps for different reasons, one for operating efficiency and the other for market share. Each are logical fits, though, and should provide Shippers with more alternatives than they presently have available.

STB. The legislative front has also had recent developments challenging STB authority on transfer stations running under pre-emption status. Better known as the Pallone-Murphy Amendment to H.R. 2095 changing the requirements of the federal railroad pre-emption under 49 USC 10501 (b). Basically, the amendment supports that federal railroad pre-emption for operation of transfer stations has been often abused and should be revised to a tighter standard under a different governing body.

Fourth Quarter Planning. While you're developing your plans for 2008, don't ignore the fact that in the railroad industry the fourth quarter happens. Two of the three slowest periods from a railroad service perspective are in November (Thanksgiving week) and December (Christmas week). Plan ahead.

Enjoy your Thanksgiving holiday.

We look forward to earning your business!