Tealinc

Touchbase

OCTOBER 2012

In This Issue

Visit us at:
www.tealinc.com

Railroad & Policy Updates

Rail industry's cost of capital rose in 2011, STB says

September 13, 2012 the Surface Transportation Board (STB) announced it calculated the rail industry's after-tax cost of capital for 2011 at 11.57 percent compared with 11.03 percent in 2010 and 10.43 percent in 2009.

Each year, the board calculates the industry's cost of capital, which represents the STB's estimate of the average rate of return needed to persuade investors to provide capital to the freight-rail industry.

"The board uses the cost of capital figure in evaluating the adequacy of individual railroads' revenues each year," STB members said in a prepared statement, adding that the board also uses the figure when determining the reasonableness of a challenged rail rate, considering a rail line abandonment proposal or valuing a particular railroad's operation.

The STB also determined that, in 2011, the cost of railroad long-term debt was 3.97 percent; the cost of common equity was 13.57 percent; and railroad's capital structure mix was 20.83 percent for long-term debt and 79.17 percent for common equity.

Learn more at:
http://www.progressiverailroading.com/federal_legislation_regulation/news/Rail-industrys-cost-of-capital-rose-in-2011-STB-says--32465#

Mechanical Brief with Steve Christian

Overlooked truck inspection item

A recent railcar inspection I completed reminded me of a very simple but often overlooked item to inspect on every railcar that you should look at. Whether you're inspecting cars to buy, lease or completing a routine inspection on cars you have in service, here are a few things to keep in mind.

Whether you're inspecting cars to buy, lease or completing a routine inspection on cars you have in service, here are a few things to keep in mind

Normal railcar truck inspections include:

- Friction casting wear and condition
- Wedge rise
- Springs (broken, missing and signs of spring bind)
- Column guide and gib clearance
- Column wear plates
- Column wear plate securements
- Side frame pairing
- Etc., etc., etc.

The item that is often overlooked is the position of the roller bearing in the side frame pedestal. Every time your brakes are applied on a railcar, the brake shoes press against the wheel treads outward from the centerline of the side frame. This action ultimately causes the roller bearing adapter into the outside thrust lugs of the side frames. As the result, wear occurs on the thrust lugs and the corresponding surface of the roller bearing

Excessive adapter and or thrust lug wear results in truck hunting, premature wear on all truck components and premature wheel wear

Once you train yourself to look for this it will jump out at you as you look at railcars

AAR reports mixed weekly rail traffic for August

Commodity carloads of petroleum and petroleum products, motor vehicles and parts, crushed stone, sand and gravel up for August 2012

adapter causing the roller bearing to shift away from the springs. If the roller bearing looks like it is getting close to the outside leg of the side frame, the roller bearing adapter and/or the thrust lugs are worn.

This is a very wordy explanation of what is a very simple phenomenon. When the side frames are new or recently rebuilt under AAR specification M-214 and new roller bearing adapters are applied, the roller bearing should ride in the side frame at the center line of the pedestal.

Sometimes the fix is as simple as rotating the roller bearing adapter. Rotating the adapter means that you rotate the worn portion towards the springs. Applying a new adapter is a better fix.

If neither the rotation nor the replacement of the adapter gets the roller bearing centered in the pedestal, the only solution is to perform a rebuild of the side frame in a shop certified to perform AAR M-214 truck rebuilds.

Why does this matter? Excessive adapter and or thrust lug wear results in truck hunting, premature wear on all truck components and premature wheel wear.

Once you train yourself to look for this it will jump out at you as you look at railcars. I would recommend that you include this in your inspection regime.

*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

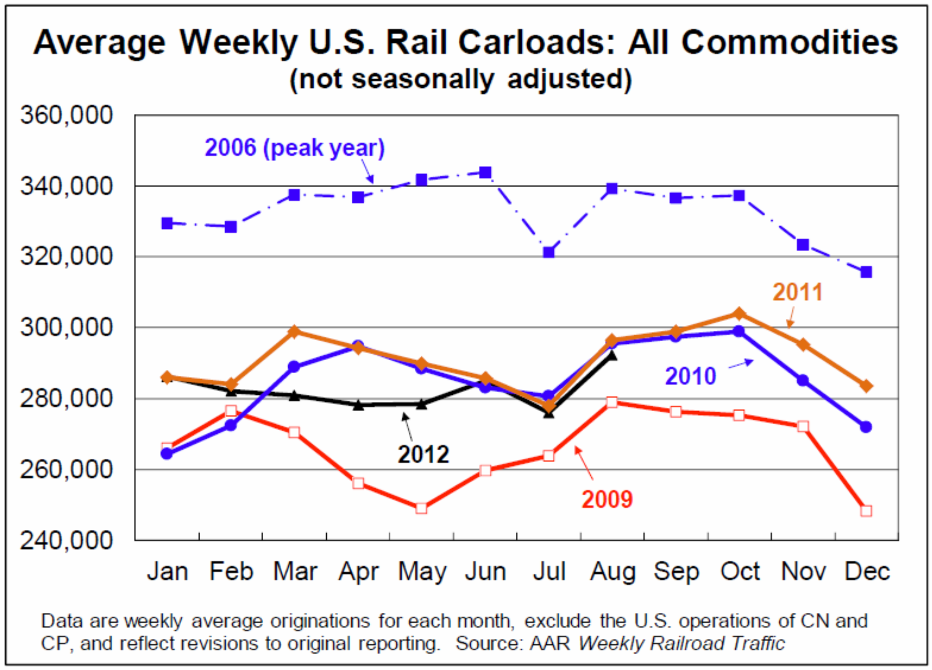
The Association of American Railroads (AAR) reported on September 6, 2012 that U.S. rail carloads originated in August 2012 totaled 1,461,680, down 1.4 percent compared with August 2011. Intermodal traffic in August 2012 totaled 1,230,992 containers and trailers, up 51,145 units or 4.3 percent compared with August 2011. The August 2012 average weekly intermodal volume of 246,198 units is the second highest average for any August on record.

Commodity groups that saw carload gains in August 2012 compared with August 2011 included: petroleum and petroleum products, up 49 percent or 18,007 carloads; motor vehicles and parts, up 13 percent or 8,966 carloads; and crushed stone, sand, and gravel, up 7.3 percent or 6,905 carloads.

Commodities with carload declines in August 2012 were led by coal, down 7.3 percent or 48,493 carloads; metallic ores, down 18.7 percent or 8,757 carloads; and waste and nonferrous scrap, down 15 percent or 2,652 carloads.

Carloads excluding coal were up 3.3 percent or 27,443 carloads in August 2012 compared with August 2011. Carloads excluding coal and grain were up 3.5 percent or 25,889 carloads in August 2012 compared with August

2011.



Carloads of coal, metallic ores, waste and nonferrous scrap down August 2012

As of September 1, 2012, 311,226 freight cars were in storage, a decrease of 3,745 cars from August 1, 2012, and equal to 20.3 percent of the North American fleet.

As of September 1, 20.3 percent of the North American fleet was in storage; down 3,745 cars from August

"U.S rail traffic in August was pretty much same song, different verse," said AAR Senior Vice President John T. Gray. "Weakness in coal carloadings was largely but not entirely offset by increases in carloads of petroleum and petroleum products, autos, lumber, and several other commodities, with intermodal showing continued strength."

AAR today also announced mixed weekly rail traffic for the week ending September 1, 2012, with U.S. railroads originating 292,732 carloads, down 3.4 percent compared with the same week last year. Intermodal volume for the week totaled 249,113 trailers and containers, up 6.5 percent compared with the same week last year.

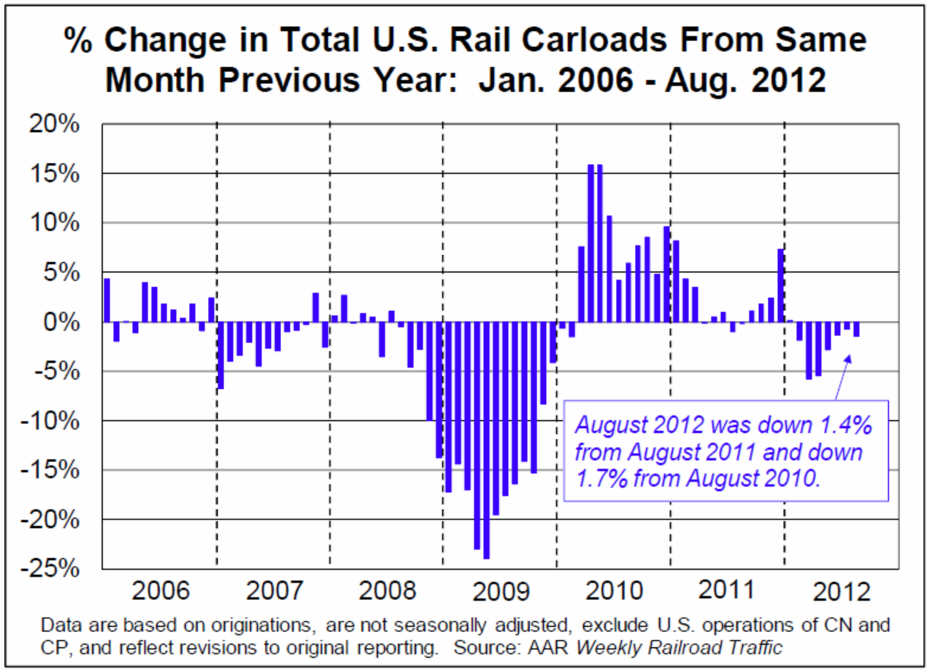
Ten of the 20 carload commodity groups posted increases compared with the same week in 2011, with petroleum products, up 44.1 percent; farm products excluding grain, up 22 percent, and lumber and wood products, up 20.7 percent. The groups showing a decrease in weekly traffic included metallic ores, down 17.2 percent, and waste and nonferrous scrap, down 16.6 percent.

Weekly carload volume on Eastern railroads was down 7.1 percent compared with the same week last year. In the West, weekly carload volume was down 1.1 percent compared with the same week in 2011.

U.S. Traffic for the year down 2.4 percent from the

For the first 35 weeks of 2012, U.S. railroads reported cumulative volume of 9,890,231 carloads, down 2.4 percent from the same point last year, and 8,226,793 trailers and containers, up 3.7 percent from last year.

same point last year with trailers and containers up 3.7 percent from last year



Canadian railroads reported 79,510 carloads for the week, up .1 percent compared with the same week last year, and 54,839 trailers and containers, up 3.9 percent compared with 2011. For the first 35 weeks of 2012, Canadian railroads reported cumulative volume of 2,683,533 carloads, up 2.8 percent from the same point last year, and 1,788,902 trailers and containers, up 6.9 percent from last year.

Combined North American rail volume for the year down 1.3 percent from the same point last year with trailers and containers up 4.7 percent from last year

Mexican railroads reported 14,722 carloads for the week, up 2.3 percent compared with the same week last year, and 11,230 trailers and containers, up 12.6 percent. Cumulative volume on Mexican railroads for the first 35 weeks of 2012 is 499,977 carloads, down .5 percent compared with the same point last year, and 338,901 trailers and containers, up 18.5 percent from last year.

Combined North American rail volume for the first 35 weeks of 2012 on 13 reporting U.S., Canadian and Mexican railroads totaled 13,073,741 carloads, down 1.3 percent compared with the same point last year, and 10,354,596 trailers and containers, up 4.7 percent compared with last year.

Learn more:
http://www.aar.org/NewsAndEvents/Freight-Rail-Traffic/2012/09/06-railtraffic.aspx

Graphs adapted from:
http://www.aar.org/NewsAndEvents/~/media/aar/railtimeindicators/2012-09-rti.ashx

Industrial Inside

Second quarter aggregate production up considerably

Preliminary numbers from the U.S. Geological Survey (USGS) suggest aggregate production rose sharply in the second quarter. Increases in domestic production for crushed stone, sand and gravel were substantial compared to production in the first quarter of 2012, primarily owing to seasonal variations.

USGS says crushed stone production was up 47 percent over the first quarter, and construction sand and gravel was up 63 percent

Cement consumption expected to exceed earlier expectations

“If Congress fails to address the fiscal cliff issue during the first or second quarter of 2013, there is the potential for severe adverse economic consequences that could slow the recovery process, potentially leading to a severe decline in 2013 cement consumption”

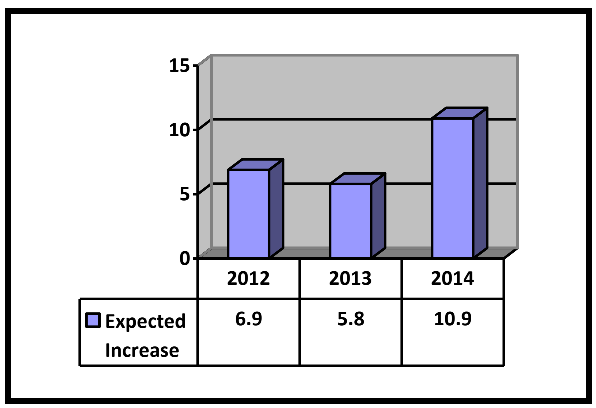
USGS says crushed stone production was up 47 percent over the first quarter, and construction sand and gravel was up 63 percent. Construction materials showed much more modest increases when compared to the second quarter of last year, with crushed stone and construction sand and gravel each up 5 percent.

The increase in construction materials production compared to production in the second quarter of 2011 could be the continuing effects of the unusually warm winter weather in the eastern half of the United States. The increase may also reflect specific increases in construction after several years of decline.

Total construction spending during the first half of 2012 was up 9 percent over the corresponding period of 2011.

Meanwhile, the Portland Cement Association (PCA) has nearly doubled its expected 2012 cement consumption figures in a revised forecast that reflects the favorable weather much of the United States has had, gains in residential and nonresidential construction activity and gains in cement intensities.

PCA revised its spring forecast upward, anticipating a 6.9 percent increase in 2012 from 2011 levels, followed by a 5.8 percent jump in 2013 and a 10.9 percent increase in 2014.



“In addition to great construction weather during the first half of the year, real put-in-place construction activity is up 4.2 percent compared to 2011 levels,” says Ed Sullivan, PCA chief economist. “We expect to see a 5.5 percent gain on real construction activity this year after seven consecutive years of decline.”

Beyond 2012, Sullivan says the near-term economic outlook is uncertain. The uncertainty will inhibit stronger growth conditions from materializing, he says.

“If Congress fails to address the fiscal cliff issue during the first or second quarter of 2013, there is the potential for severe adverse economic consequences that could slow the recovery process, potentially leading to a severe decline in 2013 cement consumption,” Sullivan says. “PCA’s baseline projections assume a rational Congress that will recognize these risks and take action to minimize restraints on economic growth.”

Articles adapted from:
http://www.pitandquarry.com/cement-consumption-expected-to-exceed-earlier-expectations/ and http://www.pitandquarry.com/second-quarter-aggregate-production-up-considerably/

Financial Focus

Federal Reserve Chairman Ben Bernanke takes on critics of QE3

On October 1, 2012, Federal Reserve Board Chairman Ben Bernanke attempted to answer some of the fierce criticism and public unease facing the Fed's third round of bond purchases, known as quantitative easing or QE3.

In a speech to the Economic Club of Indiana in Indianapolis, Bernanke tried to de-mystify the purchases, saying the basic monetary policy strategy "is the same as it has always been."

"The difference is that, with short-term interest rates nearly at zero, we have shifted to tools aimed at reducing longer-term interest rates more directly," he said.

Recognizing some of the public concern over the Fed's policy, Bernanke noted that even a star player of the Washington Nationals baseball team has asked him for the "scoop on quantitative easing."

"We expect inflation to remain low for the foreseeable future. The Federal Reserve's price stability record is excellent and we are fully committed to maintaining it"

Last month, the Fed moved to start open-ended buying of $40 billion of mortgage bonds per month until there is a sustained improvement in labor-market conditions.

Bernanke stressed the Fed has not abandoned its mission to keep inflation under control.

"We expect inflation to remain low for the foreseeable future," he said. "The Federal Reserve's price stability record is excellent and we are fully committed to maintaining it," he said.

Bernanke stressed that the Fed's pledge to keep rates low until mid-2015 was not a forecast of a weak economy over the next three years.

Instead, the message is "as long as price stability is preserved, we will take care not to raise rates prematurely," he said.

"If the economy is growing at trend or below trend, that is just enough to help provide jobs for new people coming into the labor force... It does nothing to eat into the backlog of the unemployed. Our unemployment rate of 8.1% currently is really about the same it was in January. We

"We hope that, by clarifying our expectations about future policy, we can provide individuals, families, businesses, and financial markets greater confidence about the Fed's commitment to promoting a sustainable recovery and that, as a result, they will become more willing to invest, hire and spend," he said.

Following up on those comments, Bernanke stressed in response to a question that he is not expecting a recession and that the central bank's actions are in response to concerns that growth will continue at a pace that is insufficient to put people back to work.

"If the economy is growing at trend or below trend, that is just enough to help provide jobs for new people coming into the labor force," Bernanke

are not really making progress. At least not this year."

said. "It does nothing to eat into the backlog of the unemployed. Our unemployment rate of 8.1% currently is really about the same it was in January. We are not really making progress. At least not this year."

The Fed chairman stressed that the Fed "has the policy tools to tighten monetary conditions at the appropriate time so as to prevent the emergence of inflationary pressures down the road."

Learn more at:
http://www.marketwatch.com/story/bernanke-takes-on-critics-of-qe3-2012-10-01-121033349

The Edge

Happy Halloween!   If you still have kids at home you're probably already aware that October is a "spooky" month.   Here in about 30 days we'll see all sorts of ghosts, goblins and spooks running around collecting treats!

Those of us in the rail transportation arena have been seeing our share of ghosts, goblins and spooks in the bulk commodity mining, manufacturing and processing community for the past several months (or years in some cases).   However it appears that some of the spooks are rising to the surface and are slowly being dealt with providing some stability to rail transport shipments. You'll note in this issue most commodities shipped by rail, sans coal, are steady to growing.   Since rail transportation originated carloads is a leading indicator of economic health we'd need to say the sickness in the US economy has at least stabilized and is on the road to recovery.

Another indicator is stagflation. This is where the economy is recovering but costs go up and values don't. It's a natural evolution in economic recovery to pay more dollars for a good, service or product to make up for increased costs of inputs. Generally in my limited economic theory department stagflation occurs and it feels like a continuation of the poor economy but really it's a stage of recovery. After which there is some additional economic health indicators where interest rates earned on invested capital are more than menial. And then there's a threat of interest rate run up which could cause undue inflationary pressure. The good point is that it appears the Federal Reserve Board is paying attention and working hard to control inflation. Wearing the mask is the outcome of the Presidential, senate and house elections. We'll see if those elected officials take off their masks and go to work for the economy and working folks or continue to spook us!

We look forward to earning your business!