

# “Life is Good” Equipment Trends & Outlook

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**Barbara W. Wilson**  
**President**

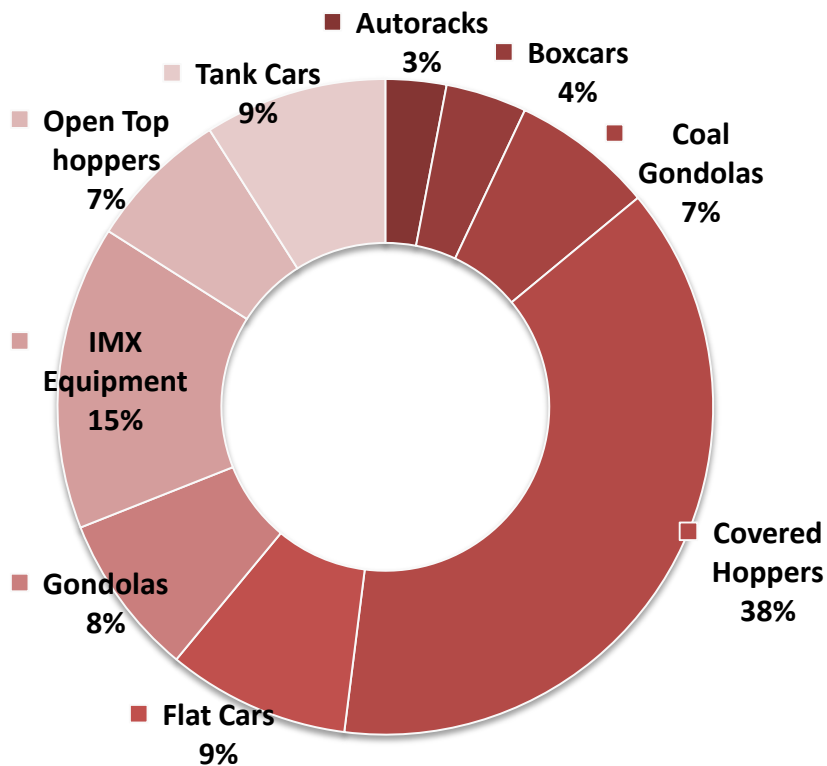
Midwest Rail Shippers Association  
January 2015

***Opinions  
expressed and  
topics discussed  
are my personal  
opinions and not  
that of  
First Union Rail  
or Wells Fargo***

- Who is First Union Rail?
- **What's new at First Union Rail?**
- Rail Equipment Orders and Backlog
- Railcar Demand: 2015
  - Energy, Intermodal, Grain, Housing
- Lease Market Conclusions

## FIRST UNION RAIL

*First Union Rail's key competitive advantage is a low cost of capital; when combined with our expertise, products and services we seek to meet our clients' equipment needs*



### Who is First Union Rail today?

- **Fleet:** Very large and diverse equipment fleet:
  - Over **100,000** railcars and **800** locomotives
  - Focused on general service equipment
- **Business Model:** Full service, in-house management of all railcars and locomotives
- **Location:** Offices in U.S. and Canada allow for domestic transactions in both countries; based in Rosemont, IL
- **People:** Seasoned team of >150 employees
- **Products:** Operating railcar & locomotive leases; railcar lease management services
- **Owner:** Wells Fargo Bank

**First Union Has a Broad perspective on the market for railcars and locomotives**

# What's Happening now at First Union Rail

- Aggressive Fleet Growth, both Railcars and Locomotives
  - **Buying Brand New Railcars** – Diverse commodities
  - **Buying in Secondary market:** fleets and individual deals:
  - January 2015: Macquarie Rail's North American Railcar fleet
  - April 2014: Helm Financial Corporation
  - Numerous individual lease transactions with equipment both on and off lease
  - **Investment programs** - Ongoing in owned equipment
- Personnel, added over 25 permanent team members in 2014
- Focused on Quality Customer service
- **GOAL:** Have a large diverse fleet to meet our clients' needs while deploying Wells Fargo's capital for a satisfactory return

# Rail Equipment: “Life is Good”

Rail Equipment Market in 2015



### ***Five broad industry trends are driving railcar demand:***

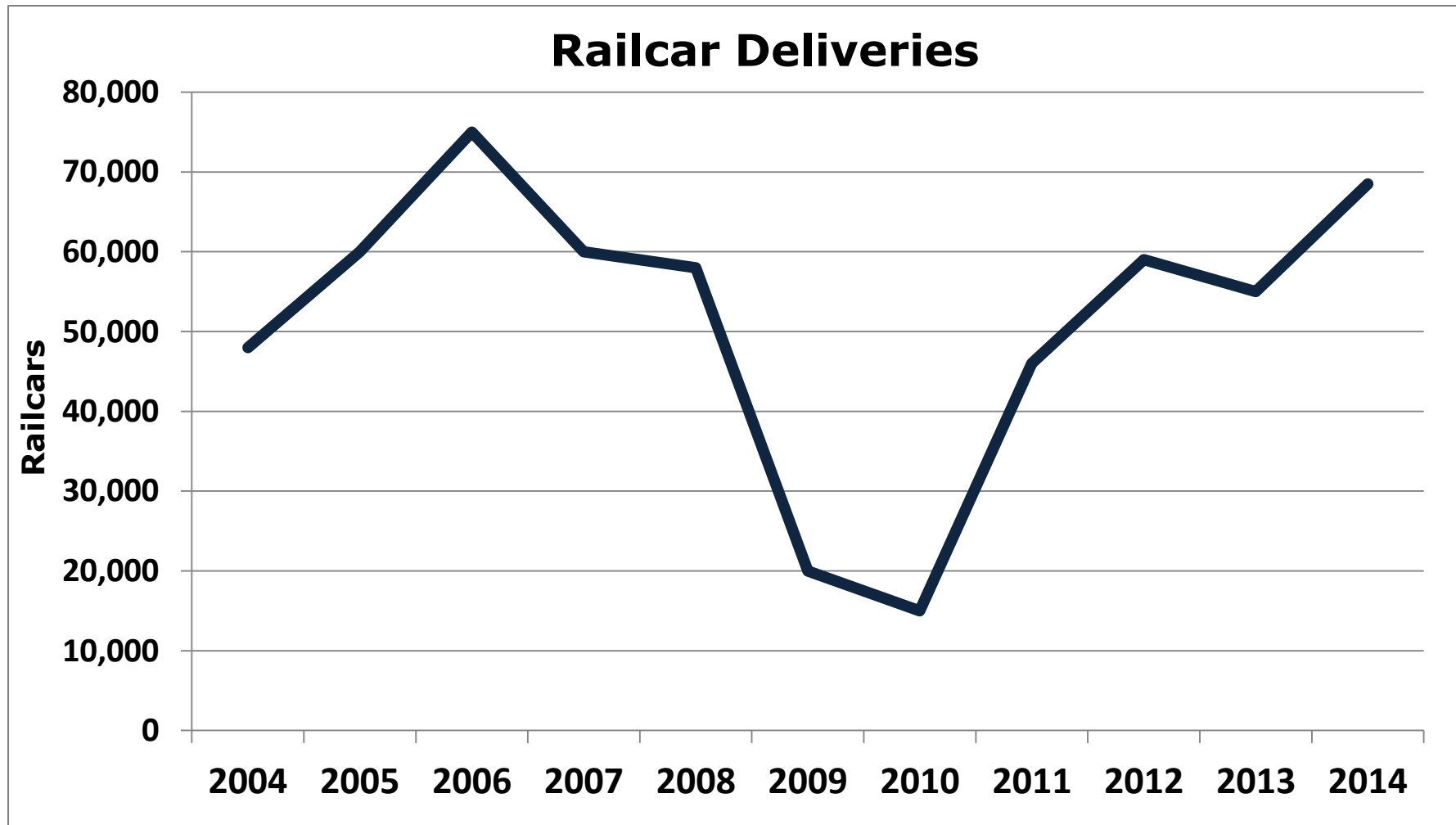
- 1. Energy** - Shale/Oil; tank car & sand car demand continues at this time; tank car regulations will require replacement cars;
- 2. Energy** - Coal car demand is stable, virtually no new cars;
- 3. Intermodal** - domestic growth continues, this fleet is growing;
- 4. Grain** - 2<sup>nd</sup> consecutive record harvest with an aging fleet;
- 5. Housing** - gradual rebound is occurring with strong 2015 forecast

### **Today's market:**

Demand is strong across the board: very few, if any, sand, tank, grain, or intermodal railcars or any low or high horsepower locomotives are available for lease.

# Rail Equipment Market in 2015

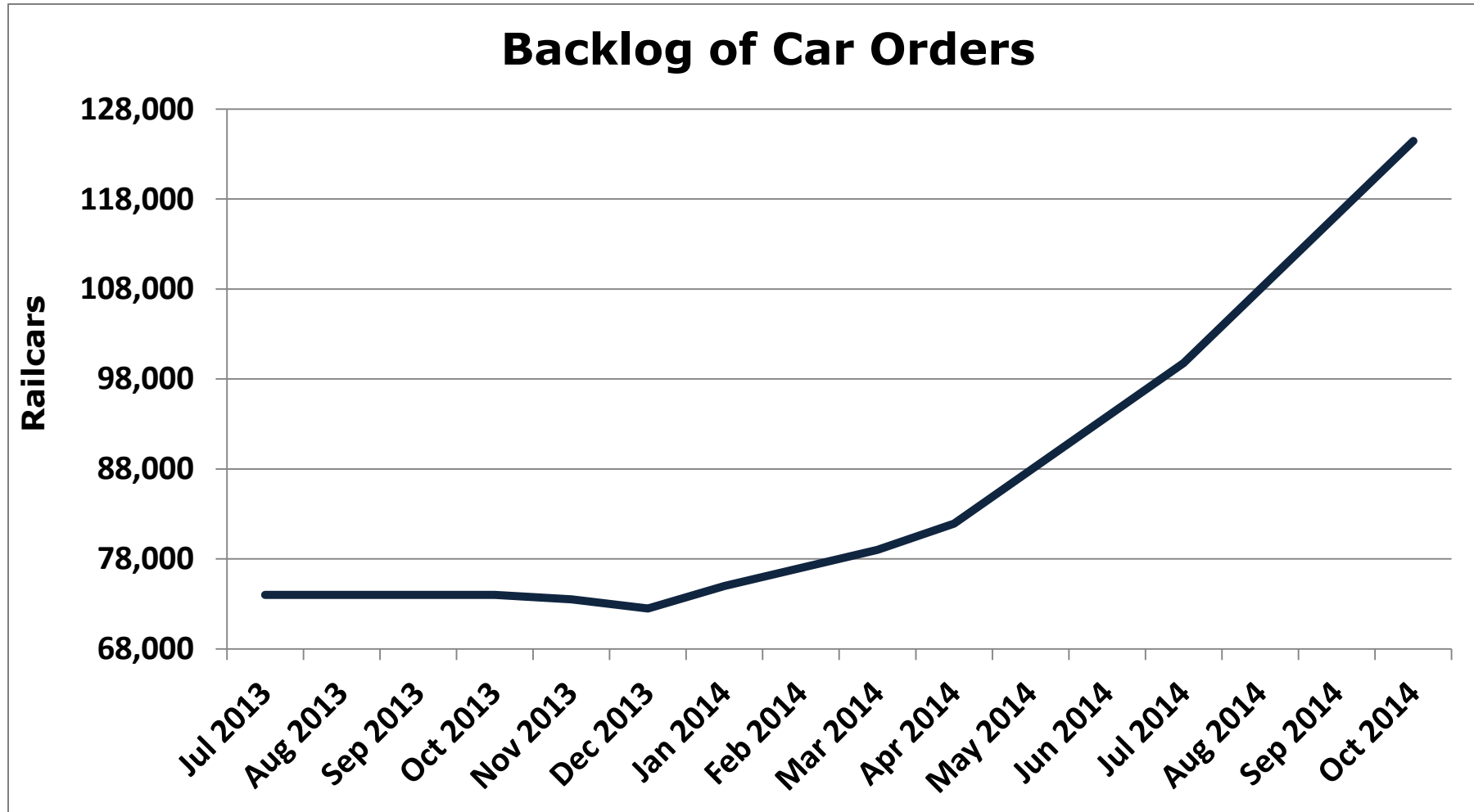
2014 Deliveries exceeded 67,000 cars  
2015 forecast is for > 80,000 car deliveries



Railway Supply Institute Inc. data, Economic Planning Associates

# Rail Equipment Market in 2015

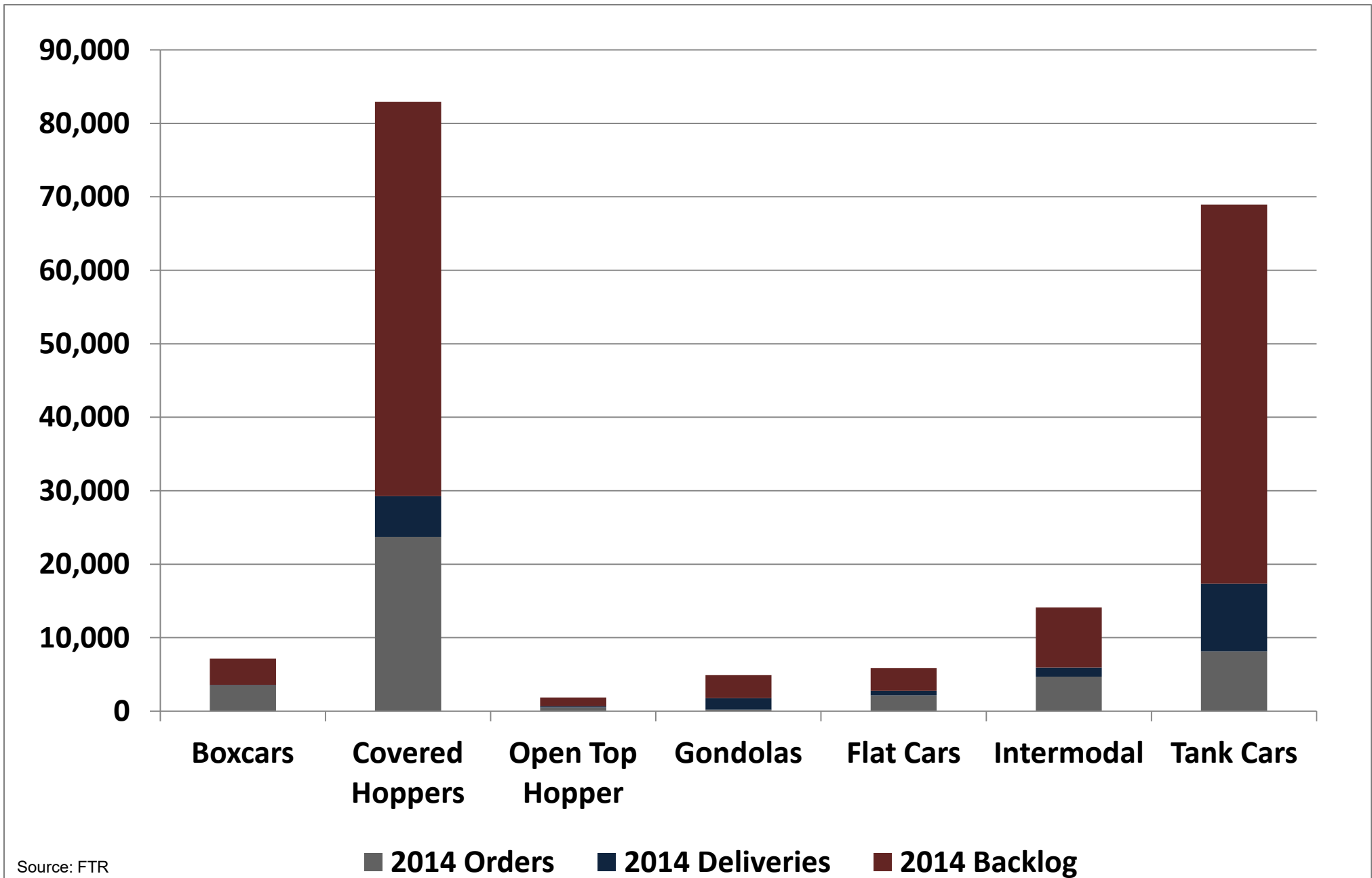
Backlog at 124,437 cars as of October 2014, up 69% y/y;  
Largest backlog since October 1979 backlog of 127,887 cars





# Rail Equipment Market in 2015

## 2014 Orders, Deliveries and Backlog by Car Type



Source: FTR

A rail car order **boom** centered on **energy business** is in progress

**“HOT”** cars are:

- Frac sand: 34,334 cars on backlog (28% of total backlog)
- Tank cars: 51,582 cars on backlog (42% of total backlog)
- Orders of 20,000+ plastic pellet hoppers are expected in the next few years; cars will service chemical plants being built to use cheap natural gas
- Railcar prices are up across the **board on all car types ...**
- Manufacturers are taking orders for delivery in 2017 in most cases

**Yet, there are some things on the horizon that bear watching:**

- Government Regulation
  - Equipment: What regulations will pass for crude/ethanol car specs?
  - Railroads: Will regulations will impact crude/ethanol movement?
- Pipelines: Crude will move by pipeline if new ones are built
- <\$50 a barrel Oil – what does that mean for railcar demand?

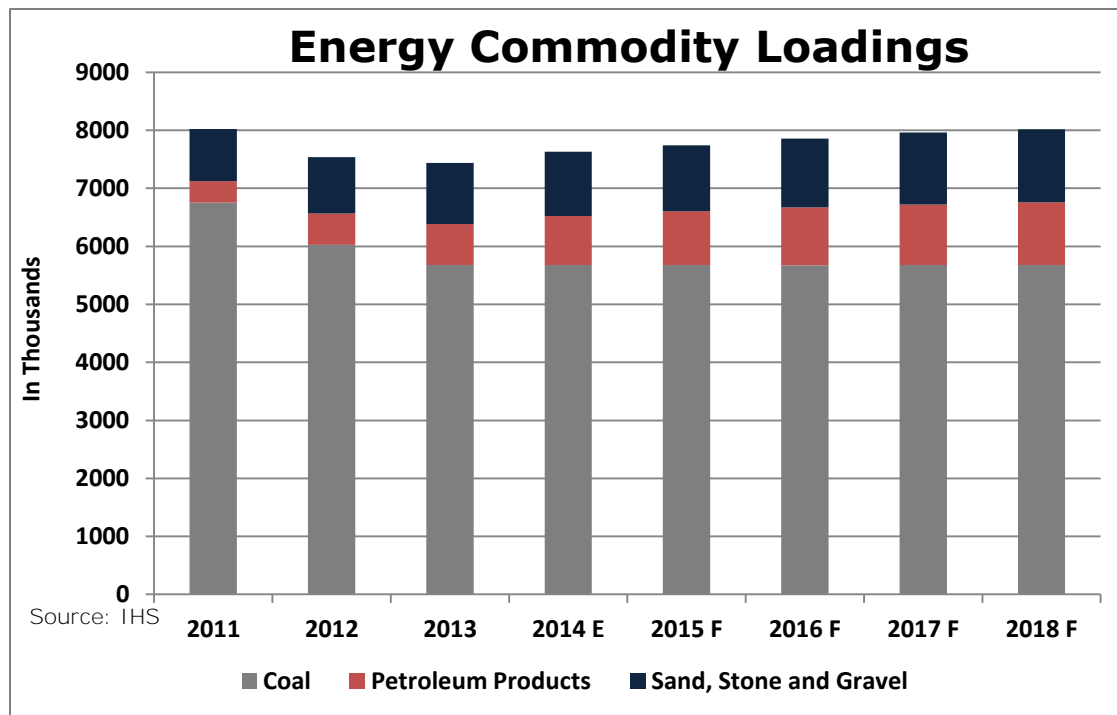
# Rail and Falling Oil Prices

- A decline in drilling should be expected which will impact CBR, frac sand demand, chemicals, pipe and other materials used for extraction
  - Given large backlog of sand cars there is potential for oversupply
  - Given pending new tank car regs, many tanks will not be retrofitted, thus large numbers of existing cars will be exiting the market reducing the risk of an oversupply of crude tanks
- However, crude shipments are **less than 2%** of all North American carloads and only 4% of all volume came from CBR related traffic
- Near term, relatively minimal risk to railcar supply
- Large U.S. oil and gas fields will continue exploration and production
- **The big picture of <\$50/barrel oil**
- Intermodal benefits from increased consumer spending
- Growth in other commodities may offset the loss of crude shipments
  - Falling energy prices make the U.S. more globally competitive in markets for chemicals and finished goods
  - **Equivalent to a "tax credit" for both consumers and business =** increased demand for shipping inbound commodities and outbound finish product

## Railcar Demand: Energy

**Tank car and sand car** equipment demand is very strong:

- Backlog of 34,333 small cube covered hoppers on order largely for frac sand: **QUESTION: are we overbuilding this car type?**
- Large Backlog of 51,582 tank cars, 70%+ crude oil; yet there are likely 40,000 crude cars that will be uneconomical to retrofit to new regulations



**Coal cars:** Traffic is flat YoY with little excess car capacity due to utility stockpile rebuilding in 2014; but reducing demand is a secular theme until export markets rebound

**Regulatory Front:** awaiting word on new car regulation/modification requirements:

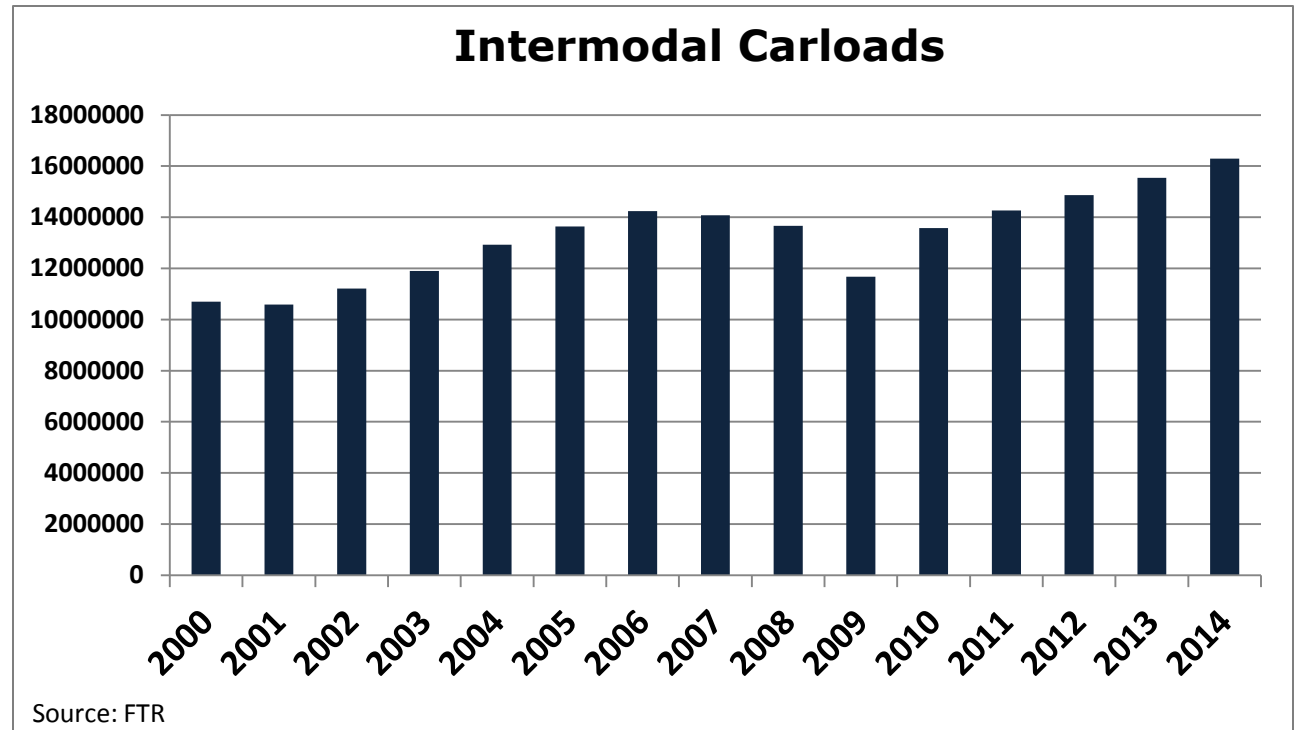
- **Today's crude tank Standard is CPC - 1232:** includes coiled & insulated, jacketed, normalized steel, top /bottom protections, high-capacity relief valves
- Retrofits will occur when economical, many older cars will be retired

### Forecast:

New tank car orders will surge to replace retirements

## Railcar Demand: Domestic Intermodal

- Increased Flat Car and domestic box demand for domestic intermodal
- Over 8,000 intermodal cars ordered in the third quarter of 2014

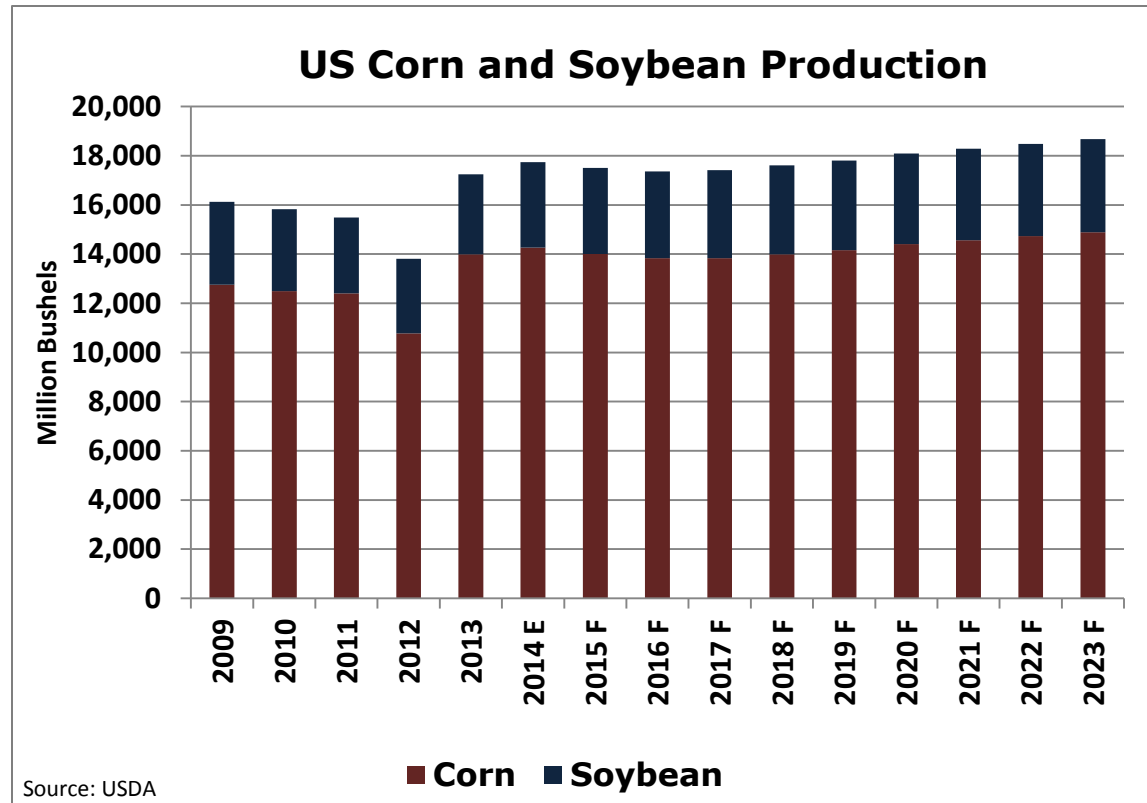


### *Drivers of Growth:*

- CSX, Norfolk Southern and Burlington Northern have invested millions of \$'s into:
  - New Facilities
  - New Services
- **Intermodal is 40% of CSX's system freight volume**
- Conversion of Freight from Highway to Rail will continue to fuel the growth of Domestic Intermodal

## Railcar Demand: Grain

- Backlog of over 9,000 large cube covered hoppers on order; these cars will serve as replacement cars as older cars fall out
- Grain Volumes (2013/14 harvests) are strong and car demand is very strong
- **2014 harvest exceeded 2013's** record harvest with new highs established in corn and soybeans

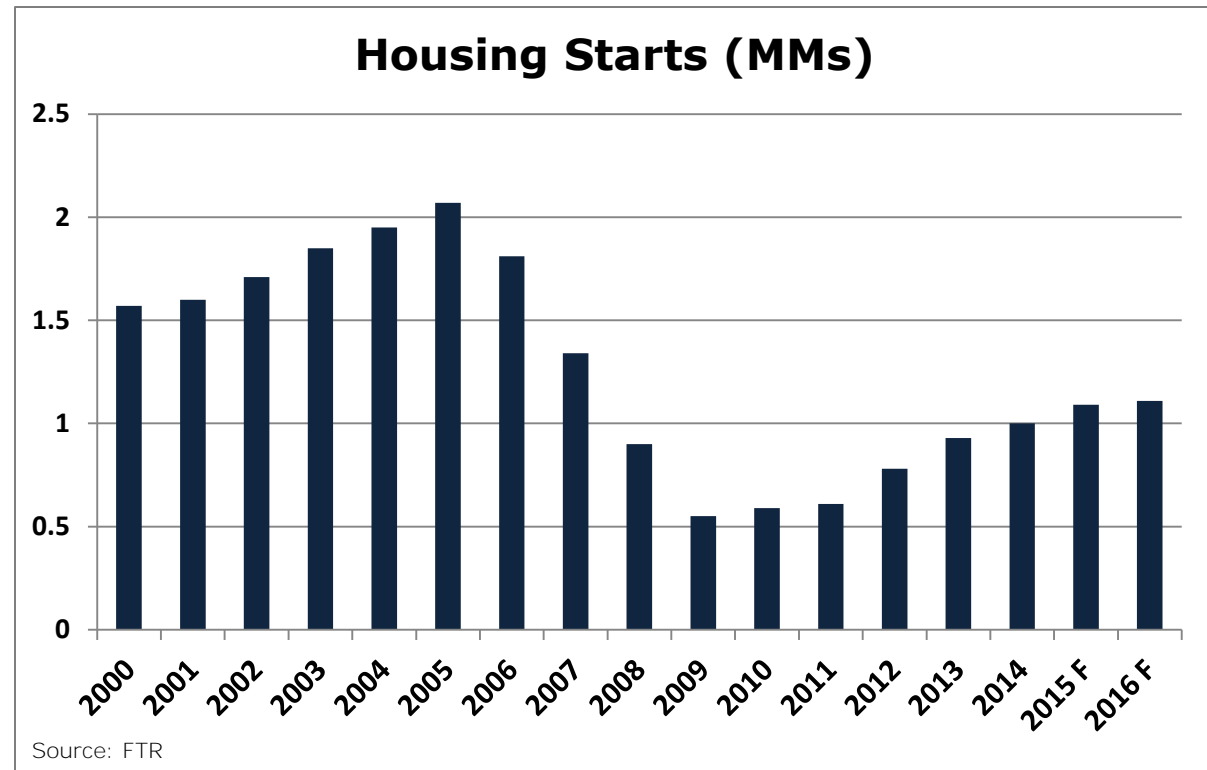


- Few available cars in the market today; expected fleet attrition of the lower capacity cars over the next few years will continue to keep car supply tight
- Virtually all old 4750 cube covered hopper cars are still in service

## Railcar Demand: Housing

### Rail Market Today:

- Limited availability of select boxcars;
- Demand for center beam cars has increased in 2014: Plenty of center beams still available; Lumber shipments are expected to increase 2.8% in 2015 with moderate growth through 2019
- Domestic Intermodal will benefit from consumer spending



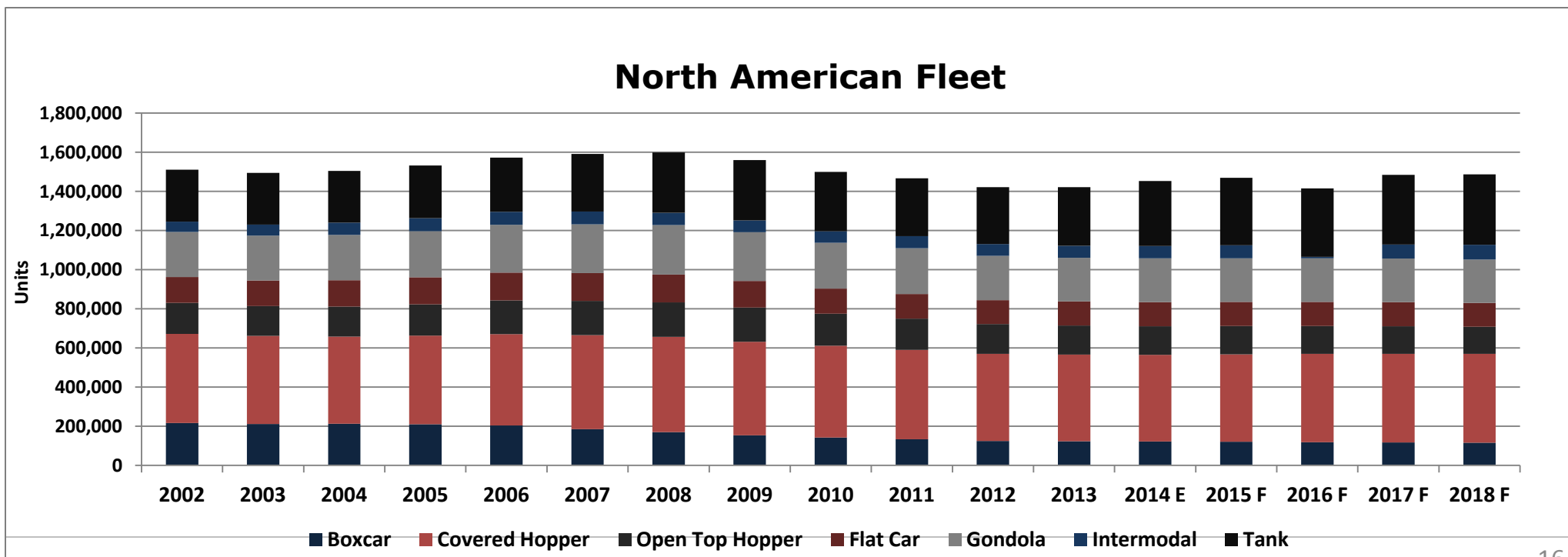
### Demand:

- In November 2014 Freddie Mac forecasted new home construction to increase by 20 percent in 2015; new home construction was up 5.5 percent year to date for the same period
- Lower fuel costs will translate into higher consumer spending

# Rail Equipment Market in 2015

## 2015 Forecast: Equipment demand will remain strong

- Lingering railroad congestion with lower Train speeds & longer dwell times will continue, resulting in strong demand for railcars and locomotives in 2015
- Economy is strong for commodities shipped by rail – strong equipment demand
- Growth opportunities exist in numerous segments for railcar assets
- North American fleet is aging and older cars will continue to fall out of the fleet
- New Car Production and backlogs will remain strong for next few years, fleet replacement pressures will continue to mount in select older fleets of cars
- North American fleet will not show significant overall growth in the next few years





# “Life is Good”

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