Energy Market Dynamics Hit The Rails

By Fred Norrell

In the midst of economic slow motion the energy market is extremely active. Coal shipments are down, oil by rail is booming. Natural gas and oil exploration, drilling and production are experiencing explosive growth. How all this affects railroads and tie producers may be difficult to see at this early vantage point, but RTA forecasters are taking a stab at it. A few words on how the forecast is produced may help in understanding RTA's shifting focus on the sources of growth.

RTA predicts future tie purchases based on an in-house econometric model, supplemented by railroad survey results and by information from industry participants. The basic logic of the model is that economic growth results in increased railroad freight, which wears on infrastructure, thus increasing the need for tie purchases. This is maintenance-oriented thinking, yet new construction is beginning to play a bigger role in terms of materials supply. From the miles of track data reported by AAR, and from the tie purchases reported by RTA members, most new track appears to be constructed by small railroads, companies involved in energy projects, or others. This is somewhat at variance with prior RTA forecast assumptions. Thus, comparing this forecast with previous versions will reveal fewer Class 1 tie purchases and more "small market" tie purchases. Here, information from trade journals and industry contacts has been used to get a better grasp of the scale of new construction, which completes the RTA forecast.

The model gives coal shipments explicit treatment due to their importance in terms of freight volume. No doubt, coal is significant, but energy market dynamics are churning at a high speed. U.S. Class 1 railroads report that coal shipments declined by about 11 percent in 2012 and they continue down: 6 percent year-to-date as of week 21 reports. At the same time, petroleum products increased their presence on the U.S. Class 1 rails: up 46 percent in 2012, and still climbing.

To address these energy market changes, the econometric model has been revised or re-estimated to reflect these changes, and how they may impact the railroads and their suppliers. RTA wishes to caution that this forecast model is new, and it has not stood the test of time. The forecast results are summarized in the table below. ■

New Wood Crossties (in thousands)

Year approx.	Real GDP	Class 1 Purchases	Small Market Purchases	Total Purchases	Pct.
2008	-0.3%	16,761	3,907	20,668	0.2%
2009	-3.1%	16,216	3,432	19,648	-4.9%
2010	2.4%	16,379	3,200	19,579	-0.4%
2011	1.8%	16,525	5,363	21,888	11.8%
2012	2.2%	16,968	6,054	23,023	5.2%
2013	2.7%	16,831	6,039	22,870	-0.7%
2014	3.1%	17,138	6,196	23,334	2.0%
2015	2.9%	17,325	6,347	23,672	1.4%

Can Tie Suppliers Keep Up?

By Jim Gauntt

The good news is that the marketplace for crossties is churning along at a steady and high level of demand. The bad news is that log supplies are at their lowest levels in quite some time in many areas of the country.

Unusually wet weather, coupled with huge demand for crane mats and board road, has hit many tie producing regions hard. Recovery to normal log inventories at sawmills is not expected to occur for quite some time, according to mills that have reported.

On the recent RTA Field Trip (which will be covered in depth in the July/August issue of *Crossties),* one mill with a production capacity of 10,000 ties per week had only four days of logs left before they would have to shut down. And, they were only running at half capacity when the field trip attendees toured the facility. At another facility, the only thing being sawn and constructed were crane mats.

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At the risk of being too reactive, it could be that with other wood construction product markets such as flooring and pallets heating up, suppliers may be facing a perfect storm scenario. If this actually occurs, it could have marketplace impacts well into 2014, then even 2015, if demand remains as forecasted.

One way members can stay in close touch with the most current intelligence on the marketplace is to visit the RTA website's Members Only area. When they do, they can access detailed comments on the marketplace in the Procurement/Market Trends/Sawmills Circle. This is a forum where discussions take place on ongoing events and trends in the field regarding tie procurement.

Members can login, set up their profile and then join this circle where monthly trends reports submitted by tie buyers in the field are posted. If you don't know how to do this, there are two ways to get the right information on how to access this content.

One way is to view the just posted webinar on RTA's "Business Networking with a Purpose" found on the homepage, bottom right corner. Another way is to call RTA headquarters and let us walk you through the steps to do this. The more members participate, the more enriched the content will be. So, help us increase the value of this powerful networking and current events tool by getting started within our online community as soon as possible.

Another invaluable resource for members is the Purchases Report and Interactive Scenario Planner found at http://www.rta.org/monthly-trends. In the latter spreadsheet, members can postulate several different scenarios and see the results on production and inventory-to-sales ratios over the next 18 months.

Now, back to the question: Can tie suppliers keep up with demand? The short answer is yes. At some point in the future, tie suppliers will exhibit the resilience this industry has become famous for and "catch up." In the meantime, however, it remains to be seen at what cost, how long supply may be less than optimal, and when equilibrium will return.

Savvy market analysts suggest that tie supply could be as much as 1.4-1.8 million ties shy of fundamental demand by the end of 2013. Crosstie users are thus encouraged to use all the RTA tools available and communicate with suppliers with increased frequency as they navigate the next 18-24 months of tie supply. ■