GATX | GATX Corporation

2016 First Quarter Conference Call **April 21, 2016**

Operator:

Good day, everyone and welcome to the GATX First-Quarter Conference Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Mr. Chris LaHurd. Please go ahead, sir.

Chris LaHurd:

Good morning, everyone, and thank you for attending GATX's First-Quarter 2016 Earnings Conference Call. With me today are Brian Kenney, President and Chief Executive Officer; and Bob Lyons, Executive Vice President and Chief Financial Officer.

As a reminder, any forward-looking statement made on this call represents our best judgment as to what may occur in the future. We have-based these forward-looking statements on information currently available, and disclaim any intention or obligation to update or revise these statements to reflect subsequent events or circumstances. The Company's actual results will depend on a number of competitive and economic factors, some of which may be outside the control of the Company. For more information, refer to our Form 10-K for a discussion of these factors. You can find this report, as well as other information about the Company, on our website, www.gatx.com.

Before I get into the numbers and provide brief commentary on the quarter, I'd like to remind everyone that our annual shareholders meeting will be held tomorrow, and will be in downtown Chicago at the Northern Trust building at the corner of LaSalle and Monroe. The meeting begins at 9:00 a.m. Central Time, and slides from Brian Kenney's presentation will be posted to our website.

Earlier today, GATX reported 2016 first-quarter net income of $69.3 million or $1.66 per diluted share. This compares to 2015 first-quarter net income of $62.2 million or $1.39 per diluted share. 2016 first-quarter results include a net gain of approximately $1.5 million or $0.04 per diluted share from the exit of Portfolio Management's marine investments.

Rail North America's fleet utilization was 98.9% at the end of the first quarter. During the quarter, the renewal rate change of GATX's Lease Price Index was 6.4% and our renewal success rate was 67.5%. The average renewal term for cars in the Lease Price Index was 34 months. While demand held up for most car types, lease renewals and new car placements are increasingly competitive and lease rates trended down. Although energy-related car types had a very negative impact on LPI and renewal term, railcar oversupply and a more efficient railroad resulted in even broader-based lease rate pressure.

You all likely noted an increase in Rail North America's Other Income in the first quarter of 2016 versus the first quarter of 2015. This increase was related to a $10 million fee GATX received for allowing one customer to return 200 crude cars prior to the contractual lease termination date. The secondary market for railcars in North America remained active, albeit down from 2014 and '15 highs, and Rail North America's asset remarketing income was $17.9 million during the quarter.

Within Rail International, the European tank car leasing market remained stable. GATX Rail Europe is seeing steady demand across the fleet with utilization at 95.1%. Rail International's investment volume was $22 million during the first quarter. 2016 first-quarter segment profit was down materially from 2015 first quarter, but this was primarily due to two factors. First, we had approximately $4 million of remarketing income in the first quarter of last year, which we did not repeat this quarter; and in 2016, we purchased and expensed a larger number of wheel sets than normal in anticipation of a change-out program that we have underway. It's worth noting, market conditions in Europe are consistent with our expectations entering this year.

American Steamship Company expects to continue to face a challenging market with low iron ore demand on the Great Lakes throughout 2016. And they are currently operating 11 vessels.

Portfolio Management's results were driven primarily by the solid performance of the Rolls-Royce and Partners Finance affiliates.

And finally, GATX was active under our share repurchase authorization during the quarter, buying back nearly 1.12 million shares for a total of $50 million.

Those are the prepared remarks. I'll hand it back to the operator so we can open it up for questions.

QUESTION AND ANSWER

Operator:

(Operator Instructions) We'll take our first call from Justin Long [Stephens, Inc.] -- please go ahead.

Justin Long:

Thanks and good morning. So, my first question was on the 2016 guidance. I know you didn't change the overall EPS range, but I was wondering if you could speak to the underlying assumptions within that? Did anything change by segment since the start of the year? Just want to understand that -- the different moving pieces and how they could have changed.

Brian Kenney:

Yeah, Justin -- it's Brian. The biggest change from our guidance in January is around lease rates. We said it would be flat-to-slightly positive for the year. And due to the combination of the existing oversupply -- competitors' new cars delivering into the industry without a home -- you have increased railroad velocity and mediocre demand; so competition for new car placement and existing car placement is fierce. And lease rates are decreasing faster than we predicted.

Don't have great visibility into exactly how bad that will get, but we currently expect the LPI will go negative in 2016, and will probably end up negative for the year. It's hard to tell how much, because we don't really know what competitors' actual deliveries will be in 2016 versus what the backlog suggests. But having said that, we don't think that the pricing degradation will be severe enough to negatively impact our revenue to the point where we have to change our guidance. And apart from that, pretty much everything is the same as we said in January.

Bob Lyons:

Yeah, Justin, I would just add, too, I think we did provide, back in the fourth quarter, kind of a segment-by-segment, at least directionally, where we felt things would go by each segment. And as Brian said, no -- no change from that today.

Justin Long:

Okay, great. That's really helpful. And you mentioned the lease rate environment being a little bit worse than you initially expected in January. Is there anything you can share that would kind of give us an order of magnitude or put some context around that? I know lease rates vary by car type, but maybe something on the sequential change you've seen in lease rates in the first quarter by your major car types.

Brian Kenney:

Sure. I can try to give some color there. As we've indicated over the last year on the calls, absolute lease rates have been falling across the fleet, except for a few car types -- but that pace of decline absolutely accelerated in the first quarter. And I don't want to get too granular by car type for competitive reasons, but I'd say absolute market rates, as we see them, declined for freight cars in the quarter by an average of around 15%, and declined for tank cars over 20%.

So, pretty serious degradation in the quarter. Strong performers in there were anything consumer-related, such as auto or intermodal, and aggregate cars did okay. Weak performers were pretty widespread. Once again from a sequential absolute rate perspective, small-cube covered hoppers, as we predicted, have had a rough go here. And certain tank cars are now struggling as well, from an absolute rate perspective. High-pressure cars, for instance, came down significantly in the quarter. But once again, that's off of record highs that we saw as recently as last year.

And just to clarify, remember that the changes in the absolute market rates are not necessarily reflective of what happens to our revenue in a given quarter. And that's because of that term structure of rates, which we pushed out pretty dramatically over the last few years. So, high-pressure cars being a great example, once again had a nice decline in the quarter, but we are still renewing them above the expiring rate, so they're actually a positive contributor to the LPI. And probably the best data point for where we are in rates at this point is we're not trying to reduce the length of our lease terms, so we don't lock in these rates for too long a term.

Justin Long:

Okay, great. And last question I have. Obviously, it's a tough demand environment. I think you guys took the prudent strategy of locking in peak lease car rates at the peak and pushing term. But after doing that -- and, I guess, that kind of being completed -- going forward, what else can you do to manage the business to the demand environment we're seeing, whether it's something on the expense side, moving more maintenance in-house versus outsourcing? What strategic changes could you make in the next year or two in a pretty depressed demand environment?

Brian Kenney:

Yeah, well the first thing you do is you'll try to lock down utilization. We were actually pretty successful in the first quarter; actually did a little bit better on the utilization side than we anticipated. But, of course, lease pricing suffered in order to do that. But you want to lock down utilization, protect your installed position; be the price leader, not only on the way up but also on the way down. And I think we're demonstrating we're pretty successful with that.

And then you mentioned the other things -- on the expense side, we talked about an SG&A reduction of 3% to 5% over last year. On the maintenance side, you also mentioned that we are bringing more maintenance into our own network. We believe we do it less expensively -- we have higher quality, we're safer, and we actually have better delivery. So, it's all of the above. But it's really protecting your installed base -- is the number one motivation for our sales force right now.

Justin Long:

Okay, that's helpful. I'll leave it at that. Thanks so much for the time.

Operator:

And we'll go next to the site of Gordon Johnson [Barclays Capital] -- please go ahead.

Gordon Johnson:

Thanks for taking my questions.

Bob Lyons:

Sure.

Chris LaHurd:

Good morning.

Gordon Johnson:

So I guess -- just, I guess, with looking at the industry overall, we've done some recent checks, and looking at some of the oil companies that have recently filed for bankruptcies, have there been any cancellations -- maybe not necessarily for you -- or have you seen any cancellations of leases overall in the business?

Brian Kenney:

Well, we -- you can't cancel our leases. So, no for us. As far as what others are doing, I'm not aware of any. We have -- don't have a lot of renewals in this sector in 2016 -- for sand, very little; for crude, very little. So we're not that exposed.

As far as restructuring for requests, you always get those in any year. And there's no question they've gone up, given the current market environment. And those requests for restructuring or rental relief are primarily from energy and sand customers at this point. But that $10 million in Other Revenue you saw in the first quarter is a pretty good example of how we handle those relief requests, or early return requests. In that case, it was a large and valued customer that approached us about two years into their lease of 200 tank cars and asked to return them now, because they were surplus to their needs. Our strategy in this situation is that if we're approached for relief by a good customer, we will work to give them relief as long as our economics are not impacted. In fact, we look -- we actually try to improve our economics as a result. So, in that particular situation, we were able to negotiate a $10 million penalty fee that we felt would keep us whole from an economic perspective when they returned the cars. The customer also agreed to lease 100 new high-pressure cars that will be delivered later this year and in '17.

And it actually turned out to be a pretty big net positive from an economic perspective for GATX, because we received the fee, we placed the cars that the customer returned for a higher rate than we anticipated, and now we have a new car order at an excellent rate at a time when placing those new car deliveries is pretty challenging. So, that's what we strive for. There hasn't been a tremendous amount of requests. I'd say maybe around a dozen, including that one. And none of them -- looking at them at this point, even if we decide to act on them -- would have a material financial impact at all. So I think we're -- this is business as usual at this point.

Gordon Johnson:

That's extremely helpful. And just, I guess, a follow-on question on that. So I guess on the 200,000 cars that were canceled, the $10 million -- is that 100% margin revenue?

Brian Kenney:

It was 200 cars.

Bob Lyons:

It was 200 cars.

Gordon Johnson:

Sorry -- 200 --

Bob Lyons:

Then that – Yes, that $10 million all flow through Other Income, as Chris pointed out in his opening comments.

Brian Kenney:

Other Revenue?

Bob Lyons:

I'm sorry, Other Revenue. And it all went through in this quarter. Correct.

Gordon Johnson:

And there were no costs associated with that? And in addition, do you guys expect additional, I guess, fees associated with any potential cancellations?

Brian Kenney:

You know, the way we think about, as I said is, you entertain them, especially from a large and a valued customer. For those requests that we do entertain, if the customer is otherwise healthy from a financial perspective, either propose a solution that benefits us economically or we politely decline them. So, a proposed solution could be like the one in this quarter where you have a penalty fee; they agree to take other deliveries. You might want to extend lease terms or agree to renew other cars, just to name a few examples.

But I think to the point you're getting to, if a customer is in financial distress, we will assess that situation, and we may decide to grant relief to get ahead of a worse scenario that may arise in bankruptcy. But if I look at the requests that we've received so far – like -- again, it's weighted towards sand and energy, some have been dismissed outright. We just -- they're not in distress and we are not going to give them any help. Some have been resolved, like the one in the first quarter, and some are being considered. But, again, at this point, it's relatively small for less than 1% of the cars in our fleet, and there's nothing that I would say would impact us -- outside of this one in the first quarter. Positively -- there's nothing that would impact us financially in a material way.

Gordon Johnson:

Okay and then just one last one. What was the EPS, excluding that $10 million of fees?

Bob Lyons:

That would have been -- it's about a $0.14 increase in EPS for that fee.

Gordon Johnson:

Excellent. Hey, thanks a lot guys for the questions.

Bob Lyons:

Okay. Thank you.

Operator:

We'll take our next question from Mike Baudendistel [Stifel Nicolaus] -- please go ahead.

Mike Baudendistel:

Thank you. Can you talk a little bit about the trajectory of operating costs and how those should progress during the year? It looks like you did a nice job with cost containment, both in SG&A, operating lease expenses, even marine expenses. Were any of those things sort of unusually low in the first quarter, and maybe there's some timing impacts later in the year? Or just any comments there?

Bob Lyons:

Yeah, not so much with marine operating -- marine operating expense, obviously, is impacted by when ASC goes into operation during the course of the year. You'll see that pick up, along with marine revenue, as the year progresses. Operating lease expense is really -- it shouldn't change much from where it was in the first quarter, given the fact that we've been refinancing some of those lease-ins at a much lower rate. So that will continue at the level that it was in the first quarter.

The big one, though, Mike, to your question, is really SG&A. And we came into the year -- last year on a normalized basis, our SG&A was about $183 million. Brian indicated earlier that we expected this year we'd see a 3% to 5% decrease in that number. And we are still expecting that on a full-year basis. So, in the first quarter, I would not normal -- I would not annualize the first-quarter SG&A number. It will actually pick up as the year progresses, as we incur some costs related to IT and some other projects that we have underway.

Brian Kenney:

Yeah, and let me pile on. In railcar maintenance, that did decrease from the prior-year quarter. I wouldn't read too much into that. I still expect it to be flat-to-up for the year. We do have lower compliance maintenance this year, but we do expect more commercially-driven maintenance, because we think our utilization will come down somewhat -- even though we did better than we thought in the first quarter.

Also, on the marine side, Bob was right. It really hasn't gotten started. They just got it sailing in the first quarter at ASC. But we do expect lower operating expenses at ASC in 2016. We're going to carry the same amount of tonnage in our forecast but we're going to do it with two fewer vessels. So we would expect operating costs to be the main driver of their increased earnings in '16.

Mike Baudendistel:

Great. That's really helpful detail. I also wanted to ask you -- your average renewal term of 34 months is the shortest it's been in some time. And I know you said that some of that was, on your part -- sort of part of your objective there. I wanted to ask, is it concentrated -- is the shortening term concentrated in certain car types that were extraordinarily short? Or has it really come down sort of across the board?

Chris LaHurd:

Yeah, I'll touch on both LPI and term there. They were both heavily influenced by energy-related cars. More specifically, coal and the larger general service 30,000-gallon tank cars. To give you an example on the term, if you strip out or exclude coal cars, that renewal term goes from 34 months north of 45 months. So, yes, energy cars had a large impact.

Mike Baudendistel:

Great. That's all for me. Thank you.

Operator:

And we'll take our next question from the site of Matt Brooklier [Longbow Research] -- please go ahead.

Matt Brooklier:

Hey, thanks. So I guess my first question, you talked about your -- the renewal success rate at, I think, 67.5 for the quarter. How does that compare to fourth quarter, if you have that number? And then what are your thoughts on renewal success rate for the remainder of the year? Do we level out here? Or do you think that there's potentially further pressure?

Bob Lyons:

Sure. It's Bob Lyons. We had -- 81 months was the term in the fourth quarter.

Chris LaHurd:

81%.

Bob Lyons:

I'm sorry, 81 months would be nice -- 81% was the term in the -- renewal success rate in the fourth quarter. Looking through the balance of the year, we kind of -- obviously, we came in anticipating that that number would come down for sure into that probably 70% range. We're below that a little bit in the first quarter. Again, some of that is driven by some unique activity in the first quarter. But it's going to be down in this range for the balance of the year. And as Brian indicated earlier, it's an extremely competitive market out there. Our commercial team is working very hard to get renewals and we're being aggressive to do so. But it's a competitive landscape for sure.

Matt Brooklier:

Okay. And then, I guess, I'm just trying to get my arms around your commentary that the change that you saw in lease rates, the deterioration, that that's, I guess, the biggest component of what had changed versus your expectations maybe a couple months ago. I'm just trying to get a sense for what -- I guess, what was the offset? Because it just seems like there was a huge change in your lease rate expectations over a couple of months, yet you're still able to put up a pretty healthy earnings number. I'm just curious if maybe some of the cost saving initiatives that you had talked about and had planned were potentially maybe brought forward or accelerated? I'm just trying to line things up here.

Bob Lyons:

Sure. Well, keep in mind that the LPI and what happens to lease rates in any given quarter doesn't have a significant impact in near-term revenue, because our cars are renewing ratably over the course of a given year. This year, we had about 12,500 cars coming into the year that were scheduled for renewal, so they would occur evenly throughout the course of the year. So what happens, really, in any one given quarter or one given year doesn't have a significant impact on revenue in that particular year. So, yeah, there's been some revenue degradation from what we anticipated coming into the year, but we're able to -- certainly able to see that picked up other areas as well.

Matt Brooklier:

Okay, just the function of the model and the -- I guess cars up for renewal --

Bob Lyons:

Yeah, and if you think about it coming into any given year, given the term structure of our rates, 80% to 85% of our lease revenue coming into the year is already set, given how we set up lease terms over the course of the last couple of years.

Matt Brooklier:

Okay. And just my last question. You talked to the tank car market, where obviously you're seeing incremental pressure for flammable service tank cars, just given demand, is down pretty significantly. And I think you also mentioned that you're starting to see some pressure in non-flammable tank cars and rates are being impacted. Could you, I guess, kind of benchmark where rates are currently for non-flammable tanks, maybe relative to the cycle if you look at where rates are right now? How does that compare to maybe the past five years?

Brian Kenney:

I can give that a shot. So, I'd say for tank cars, and honestly, freight cars at this point, off their respective peaks of a couple of years ago -- which were both unprecedented historically and incredibly high -- both tank and freight rates are probably off 40% or more from that peak. For flammable cars, like a 30,000 gallon tank car, it's done more than 40%.

Matt Brooklier:

Um-hmm.

Brian Kenney:

For non-flammables, it's down less.

Matt Brooklier:

Okay. That's good color. Appreciate the time.

Operator:

We'll go next to the site of Art Hatfield [Raymond James] -- please go ahead, your line is open.

Art Hatfield:

Hey, thanks for taking the time this morning. Hey, quick question on the Portfolio Management segment income. As we look at that, what you reported in the quarter, is that pretty representative of how we should think about it as it trends forward after you've divested of some of the assets there?

Bob Lyons:

Yes. That is reasonably where it's -- call it $19 million of segment profit for the quarter last year, on a normalized basis, when you strip out the noise with regards to some of the charges that were taken last year in anticipation of exiting the marine portfolio – there, kind of normalized segment profit would be in the mid-$70 million range.

Art Hatfield:

Okay

Bob Lyons:

That's what we indicated we would expect coming into this year. Nothing occurred during the quarter to change that view.

Art Hatfield:

Okay. Thanks for that. Broader question, going back to the North American rail business. As you kind of look out and you -- obviously, you see the pressure on rates that you're seeing right now, and you look at where the industry backlog is for new car builds and the expected delivery cadence over the next few quarters. Do you see any light at the end of the tunnel when this pressure -- or can you see when the light at the end of the tunnel is going to develop with regards to lease rates maybe finding a bottom?

Brian Kenney:

That's the big question, Art. I think we see a lot of forecasts out there that says deliveries will kind of slide back to 50,000 a year normalized level.

Art Hatfield:

Um-hmm

Brian Kenney:

We don't understand the rationale behind that forecast. In fact, I don't even think it's a forecast. I think it's more of a hope by some that industry deliveries will just land softly. If you look at the history of deliveries and cycles, it's been incredibly volatile. You had boom times of 70,000 deliveries or more in both 1999 and 2006.

Art Hatfield:

Right.

Brian Kenney

And that was followed thereafter in the downturn by 17,000 deliveries in 2002 and I think 16,000 in 2010. And the fact is, the market has to adjust from these peaks to get back into equilibrium with actual demand. And historically, it does so by going way below any long-term average. So, in the current cycle, you saw a peak last year of 82,000 deliveries. And that's the highest on record. And that was driven to a large extent by orders for crude and sand cars. And then, you look at today's environment, and you have a sharp decline in coal traffic, a sharp decline in crude prices and traffic, a small drop in other car loadings. You have increased railroad velocity.

And then you hear us talk about lease demand and rate trends that we're seeing today. We don't see how the delivery cycle will be much different than the prior ones, really. And others will argue that it will be propped up by massive newer car orders to replace the legacy DOT-111s. But, honestly, they are the same people that are forecasting huge quantity of retrofits. So, you can't have both.

Art Hatfield:

Yeah.

Brian Kenney:

And you add that to the GATX perspective, that even the current number of cars in the crude service is not sustainable, we just can't get to a slide back to only 50,000 a year. So, I mean, actually I'm a lousy economist, but we do look hard at the data and what customers are saying. And we keep coming back to 50,000 cars per year is way too many cars chasing too little traffic. And we think deliveries will have to trend much lower and will repeat history. So, honestly, I don't know where it goes, but I don't think it will be 50,000. I think it has to come much lower. And we don't know how fast that will happen. Because, if you look at the backlog, it looks spectacular; I don't know how much of that is real at this point.

Art Hatfield:

Yeah, that's kind of where my next question was going. And this is kind of a -- having been through so many of these cycles, this one is so unique with the size, or at least the stated size of the backlog. And I guess the question -- and maybe you've not seen this in prior cycles, maybe this is something that can occur, I would guess, from my opinion that maybe a lot of the next upcycle is already in the backlog. With that premise understood, have you -- have shippers, or people who have ordered cars, reached out to you in an effort to sell you their production slots over the next couple of years?

Brian Kenney:

I'm not aware of any of that, Art.

Art Hatfield:

Okay. Is that something that you think could happen?

Brian Kenney:

It's an interesting question. I'm sure it could happen. I would guess that it wouldn't be that attractive to us.

Art Hatfield:

Fair enough. Fair enough. I was kind of wondering on -- more on the other side than --

Brian Kenney:

Yeah.

Art Hatfield:

-- whether or not you'd do something stupid.

Brian Kenney:

Well, I mean the slight slide in utilization we saw in the first quarter, we're not losing deals to competitors. As I said, we'll try to be the price leader on the way down as well. It's just people don't need the cars at this point.

Art Hatfield:

Sure.

Brian Kenney:

And we're seeing -- that's what I think is going to happen through 2016. That's going to be the ongoing battle. That's why you see rates sliding even more than we thought they would. And I know you're looking for a light at the end of the tunnel, and honestly, so are we, but I think it has to happen for -- the only way it happens for delivery is to come off dramatically from where people are saying they're going to be, and where they have been historically.

Art Hatfield:

Yeah. No, I understand that and I agree with that. I guess I just wanted to get your thoughts and your take on that. Actually it was extremely helpful. One last question then on this -- a little different take.

Have things gotten bad enough -- forget about people selling production slots, but have things gotten bad enough where people are trying to get out of equipment at this point? You -- from your perspective, your customers, you mentioned that; but I'm talking about other leasing entities who want to move away from what they've done.

Brian Kenney:

You know, not yet. But speaking solely from prior experience in past downturns, we usually see more attractively-priced assets hit the market either in bankruptcy situations, or in those situations where people that came into the market when it was hot –

Art Hatfield:

Right.

Brian Kenney:

-- finally realized the rail business is more cyclical and challenging than they thought. So both of those examples involve companies experiencing some financial pain first. And so, by that metric, we'll probably have to wait a while here, but I think it's coming.

Art Hatfield:

Sure.

Bob Lyons:

And I think we -- when we talked about this back in the January call, Art, we indicated, based on if you looked at 2008 and 2009, it took 12 to 18 months before people really started to feel it, and before you started to see assets loosen up in the marketplace.

Art Hatfield:

And that's extremely helpful. Just one last comment on that then. If we get to that point, what's your balance sheet situation or kind of size appetite, assuming if anything big were to come to the market?

Bob Lyons:

Sure. Balance sheet is in incredibly strong shape today still, with leverage in the 3.5 or less range. We have a lot of capacity. Our debt maturity schedule is very balanced over the course of the coming years. Obviously, we have a large revolving credit facility that we never touch. We have access to the capital markets. Currently, as we sit here today, and if you think about where we are compared to back in 2007, we've also used this very strong market over the course of the last year to extend our debt maturities.

Art Hatfield:

Um-hmm

Bob Lyons:

Back in 2007, our average debt maturity was about 3.5 years; today it's about 7.5.

Art Hatfield:

Okay

Bob Lyons:

And our average debt cost back then was about 6.5%; today it's less than 4%. So we've lowered rates, stretched maturities, kept the balance sheet in great shape. And we're in a very good position to do transactions of any size, should they present themselves.

Art Hatfield:

Right. Hey, that's very helpful. Thanks, Brian. Thanks, Bob. Appreciate the time.

Operator:

We'll take our next question from the site of Justin Bergner [Gabelli & Co.] -- please go ahead.

Justin Bergner:

Good morning.

Bob Lyons/Chris LaHurd:

Good morning.

Justin Bergner:

I have a couple quick questions, so I'll try and run through them. On the renewal rate, I think you mentioned at the start of the call that the 67.5% was a bit better than your expectations for the quarter. Is that right? And therefore, should I see the renewal rates coming down closer to 60% for the rest of the year?

Brian Kenney:

No. It was actually a little less than we would have said. What did we say for the year, Chris? Low 70s? There were a couple of transactions that pushed it a little lower. We think, for the year, we're not going to back off that number. What it's going to take to get there, though, is the rates. And that's why we're saying that's a little worse than expected.

Justin Bergner:

Okay. Thanks for that clarification. With respect to the lease rates on freight cars and tank cars, I think the down 15% and down 20% numbers, are those on a sequential basis or on a year-over-year basis?

Brian Kenney:

That is during the quarter. So, from the fourth quarter.

Justin Bergner:

Okay, that's helpful. Another question I had was in regards to the share repurchase program. I guess during the quarter, you repurchased shares at a slightly faster pace than might be inferred from the recent share repurchase program. And I was just curious if I should read anything into that.

Bob Lyons:

No, we have an authorization that the Board granted back in January, a $300 million share repurchase authorization. We indicated that for 2016, we would probably repurchase somewhere in the same range of what we repurchased in '15, which was about $125 million -- somewhere in that ballpark. So, it's really just a function of activity in the marketplace, trading volume, a number of different things. So I wouldn't read too much into that. My expectation on a full-year basis is unchanged.

Justin Bergner:

Okay. And just one more. It looks like the affiliate earnings for your Portfolio Management segment was down quarter -- year-on-year for the first time in a while. Is there actually a small decline in the Rolls-Royce joint venture? Or is that decline a function of sort of other sort of secondary JVs?

Bob Lyons:

Two things. One is we sold our joint venture interests in a shipping joint venture here during the course of the quarter. So those vessels are no longer part of the equation. That was a small contributor. But yeah, Rolls-Royce, their contribution was a little bit less than it was last year, but I'm not concerned about that. They also have remarketing activity within Rolls-Royce, so their numbers can bump around a little bit quarter-to-quarter. Last year, they did about our share, about $65 million in total contribution. I'd expect that to be in the same range again this year.

Justin Bergner:

Okay, great. Thanks.

Bob Lyons:

Sure.

Operator:

We'll take our next question from Steve O'Hara – please go ahead, your line is open.

Steve O'Hara:

Hi, good morning.

Bob Lyons:

Good morning.

Steve O'Hara:

Could you just talk just a little more about the term change? And so that the average renewal term came down quite a bit, and it sounds like that was you guys keeping rates or looking at the current rates and wanting to keep terms short. Is that pretty much the way it played out? Or was it customers, like you said, aren't too interested, so you've got to make it a little more palatable for them with a shorter term? Or both?

Brian Kenney:

Well, coal -- as Chris said, was a big contributor to that decrease. It was -- what, 12 months longer with that coal? (multiple speakers) And in general, a lot of our car types, if you look at the rates on them, they're at the point where we are trying to reduce term, so there's a little of that. And customers make it a little bit easier. They're not generally willing to commit as long, due to less visibility in their business. And then, of course, there's the customers that are very sophisticated that are trying to do the opposite. But yes, we're proactively trying to push term down.

Steve O'Hara:

Okay, thank you. And then just on the backlog, I mean, there was no reading, I guess, yet. But it has been coming down, but obviously not as much as it needs to. I mean, I guess I'm just wondering what your feeling is on the possibility that all of these cars that are kind of in that backlog get delivered, and maybe what the worst-case scenario might be for the industry if that did happen. I mean, it would seem unlikely. But I'm just wondering how you might position yourself if maybe more of those cars get delivered than you might expect?

Brian Kenney:

Yeah. I mean, that's -- it really doesn't change your tactics whether they do or not. As I said, you're just trying to protect your installed base by being as aggressive as you can to keep those cars in place. So whether they deliver or not, it's the same tactics. I share your skepticism that they will, but it doesn't change our tactics.

Steve O'Hara:

Okay. And then I'm just wondering, is there -- do you know any of your competitors that may be -- I know you guys have kind of a less-than-average renewal scenario for 2016. And I'm wondering if, based on where rates are today, would you be more aggressive in maybe early renewing cars so they don't come up in 2017?

Or would you be more apt to let them come up in 2017 when you have kind of a heavier year?

Brian Kenney:

Yeah. That's a great question, and it's one that we took advantage of. Because, you know, we've been talking about the market turning down for quite some time, really, in late 2014. So we did as many early renewals on '15 and '16 as we could. Right now, trying to do early renewals for 2017 and beyond when the market is declining like this, that's not gonna happen. Customers would rather wait and see how low rates will go. So, great thought, but that -- the time when you could get away with that is pretty much done already.

Steve O'Hara:

Okay. All right, thank you very much.

Operator:

And we'll take our next question from the site of Kristine Kubacki [Avondale Partners] -- please go ahead.

Kristine Kubacki:

Good morning, guys. One question. On -- in terms of utilization -- or in terms of the renewals, I know you guys had talked in the past about a lower exposure of renewals in 2017. Can you remind us how many cars are up for renewal in 2017?

Chris LaHurd:

Yes. Hey, Kristine. I'd say it's a bit difficult to provide '17 renewals at this point. As Brian said, it's heavily influenced by leases that we execute this year. Give you an example -- if we put a coal car on a 12-month lease this year versus a 24-month lease, that's going to change renewal exposure, as well as early renewals. So, the other thing might be worth noting. Lease expirations tend to be in the range of 15,000 to 20,000 cars for us. And as a result of our commercial strategy, we're at the low-end of that range this year, but I think we have to wait and see a little bit longer for '17.

Kristine Kubacki:

Okay, that's fair. And then I want to ask a little bit different question, maybe on the remarketing income side. Obviously, it sounds like things are still relatively hot in the secondary market -- or not maybe hot but still doing well. Can you comment a little bit on your kind of guidance for remarketing income? I know you touched on that in the fourth quarter. Has anything changed there?

Bob Lyons:

Sure. What I indicated at the fourth-quarter conference call was that Rail North America remarketing income would be somewhere in the $35 million to $40 million range. And we had about $18 million in the first quarter. So, a very good start on that. We're still seeing interest and good demand for quality assets that we're putting out into the secondary market. So, I would still expect the full-year estimate to be right in that range.

Kristine Kubacki:

Okay, that's good. And I was just wondering, in terms of the early termination fee, was that included in your guide in January?

Bob Lyons:

No, that was not.

Kristine Kubacki:

Okay. And then just a last question on scrap cars, I noticed that stepped up in the quarter. Anything going on there? Or -- I know scrap rates have come up off the bottom, but was it just a one-off? Or should we expect that trend to lift up here as we're kind of going into -- downward in the marketplace?

Bob Lyons:

Really no change to our expectation on full-year scrap volume. Obviously, as you know, given the sheer size of our fleet, there's going to be just a base load of scrapping activity that takes place every year. We have seen some uptick in scrap rates, but still nowhere near the level they had been in prior years.

Brian Kenney:

But I think it's a good question. If rates continue to march up, you will see more cars than fail their economic repair limit when they come in for maintenance. And, so if that persists, you could see higher scrapping than we anticipated.

Kristine Kubacki:

Okay, very good. I appreciate the time. Thank you.

Operator:

And we'll take our next question from the site of Michael Cohen [SuNOVA Capital] -- please go ahead, your line is open.

Michael Cohen:

Thanks for taking my question. Just wondering if you could talk about the lease rates on new cars that are being delivered versus renewals, and kind of the relationship that you're seeing between those now and how they affect one another?

Brian Kenney:

They are related. Remember that we have placed virtually all of our deliveries in '16. We're currently working in the second quarter of 2017. So, to a big -- to a large extent, we locked all that in before we entered the year, as far as ours. But new car rates -- it doesn't matter. A car is a car right now, and you'll get it placed, and so rates are converging.

Michael Cohen:

Is that -- is the natural impact of that -- is that more -- let me phrase this differently. Is that more detrimental to the new car that's being delivered that costs more to buy? Or is it harder to re-lease the used car because it's used?

Brian Kenney:

It's a good question. For the most part, it depends on the car type. A lot of these cars, whether it's new or 10 years old, have the same utility. So, if there's a lot of new cars available -- and we are seeing new cars, not ours, since we placed all of ours, but new cars that don't have a home compete with our renewals in the market, and they're offering new cars at rates that we would generally put our older cars out at. And so, it depends on the customer and the car type, but generally the utility is the same, given the lowest rate at this point in the market.

Michael Cohen:

Understood. And how much of that is driven by supply and demand dynamics? And how much of it is driven by sort of just the price of the raw material to build the car? In other words, has the price of steel, which is obviously higher than it was at the end of the year but lower than it's been in recent years, how does that affect the price of a new car and the price of a renewal?

Brian Kenney:

Yeah. So the price of a new car last year came down between 5% and 15% because of lower steel prices. And you're right, it has reversed in the first few months of 2016. But it's only added, at this point, around $500. So it's pretty small at this point. And remember, new car cost is completely unrelated to any -- to lease rates. It has nothing to do with it. It's the market that sets the lease rates.

Bob Lyons:

And I would just add too, I think for a large number of the car types that we provide, the demand equation is stable. The challenge is the supply of cars, the sheer supply of cars in the marketplace. And that's what's really driving that rate challenge.

Michael Cohen:

Okay. And then, as it relates to American Steamship in terms of volume, I know you guys are planning to handle sort of the same amount of volume with two fewer cars -- I mean two fewer vessels. Do you -- are you starting to hear any sort of color commentary on the amount of volume of iron ore for the year this year, versus last year?

Bob Lyons:

We would expect the same mix as last year. Iron ore was quite challenged last year -- that's historically been the most lucrative commodity on the Great Lakes. And it moves typically in our largest vessels, the 1,000-footers. So, commodity mix we're not anticipating is going to change or has been down. We're not anticipating any significant recovery there. Overall still planning to move somewhere around 26 million to 27 million tons this year total.

Michael Cohen:

Great. Thanks for taking my questions.

Bob Lyons:

Sure. Thank you.

Operator:

We'll take our next question from the site of Steve Barger [KeyBanc Capital] -- please go ahead.

Steve Barger:

Thanks for the time. Brian, you said protecting the installed base is the number one thing for the sales force to do in a tough environment. I just want to circle back to that. Other than the price lever, is there anything that you have in the commercial playbook for getting a customer to stay with you or to choose you if it's a new relationship?

Brian Kenney:

If it's a new relationship?

Steve Barger:

Yes. If someone's coming to you for the first time, and they have multiple people to shop from, of course.

Brian Kenney:

Well, I think the main thing with GATX beyond relationship is service. And as I've mentioned, for instance, the strategic imperative of bringing more maintenance into our own network, we believe we're quicker, have higher quality, are safer. So, yes, we have the service component as well.

Steve Barger:

Got it. But that's clearly overshadowed in the near-term just by too much supply for railcars.

Brian Kenney:

Yes, I would say -- well, it depends -- once again, it depends on the car. Everything -- every answer at GATX, we slide out by saying it depends on the car type, but you're right. In this kind of market, right now price is the king.

Steve Barger:

Got it. And Bob, when you sign a lease renewal at a lower rate, what can you do to offset the revenue decline on the cost side? Other than the focus on controlling SG&A that you've talked about, are there other levers to pull?

Bob Lyons:

Well, obviously, in terms of -- and Brian has alluded to it as well, is trying to run our maintenance facilities as efficiently as we can. We are -- you know, 3% to 5% reduction in SG&A is a pretty significant number for us, and we're continuing to focus very tightly on that. And there's other ancillary costs across the Company that we try to button-down as tightly as we can. But when that lease rate pressure occurs, to be quite honest, there aren't a lot of levers to offset just a pure change in lease rate.

Steve Barger:

Got it. And you talked about, in past cycles, it taking 12 to 18 months to see distressed assets. When you think about when this really started, how far are we into this in terms of months or quarters?

Brian Kenney:

That's a good question. It really -- lease rates started taking the real dive over the last two quarters. So, I would say more six to nine months into it.

Steve Barger:

Got it. Okay, that's all I have. Thanks.

Bob Lyons:

Thank you.

Operator:

And we'll go next to the site of (inaudible)

Unidentified Analyst:

This is a little bit different than some of the other questions, but on the Rolls-Royce JVs, they've continued to grow over time. Over the last five years, they've been a much more significant contributor to earnings. Have -- can you kind of give us some more color in terms of where you think that business can go? How big can it get? How many engines do you think you can manage? And is it more correlated to what you're doing with Rolls-Royce? Or is it more related to build rates or something else?

Bob Lyons:

Sure. I'm happy to weigh in on that. It has been a very significant contributor to GATX for many years and continues to be today. Currently, the joint ventures themselves have roughly $3 billion of a net book value of assets spread across about 425 engines.

We started this joint venture back in 1998 with just a handful of engines and about $50 million in net book value. So, it's been a tremendous growth area for us. The growth in that business is really going to be driven by air traffic, long term. There are no unique activities between ourselves and Rolls-Royce where -- growth would be driven off of some strategic decision between ourselves and them.

They are an incredibly well-positioned and sophisticated operator in the spare engine market. But obviously, the big growth opportunities there are looking out over the course of the next 20 to 30 years is growth in air traffic overall. Number of engines in service, types of engines in service, and that's one of the reasons, given the projections -- which are pretty positive over a very long period of time for growth in air travel -- that we are optimistic we'll be able to continue to grow the portfolio long-term.

Unidentified Analyst:

Have you given outlook in terms of any engine count numbers going forward? It looks like we were somewhat flat 2014 and 2015, but prior to that, it was growing. Is that more a function of re-marketing activity? Or should we kind of think about inorganic growth?

Bob Lyons:

Yup, part of that is -- yup, part of that absolutely is driven by some remarketing activity, and just what we're seeing in the secondary market there as well as where certain engines within the portfolio are in their lifecycle. So, there's a remarketing element to it there. But we're looking at organic growth in terms of just trying to grow the base level of assets deployed there. I'm not envisioning any big stair-step or any unique opportunity out there that's really going to spike that growth. It's more steady, consistent growth, really dovetailing with the number of engines that Rolls-Royce is putting into the marketplace.

Unidentified Analyst:

Okay, thank you.

Bob Lyons:

Thank you.

Operator:

And we'll go next to the site of Justin Bergner -- please go ahead.

Justin Bergner:

Hi, guys. Thanks for the follow-up. Looking at the cars, the DOT-111s and the sort of non-jacketed CPC-1232s that need to be retrofitted or replaced. I mean, it seems like, over the next couple of years, we could potentially have sort of an opportunity on the order of 5,000 to 10,000 cars per year sort of offsetting the cyclical aspect. Is that sort of an appropriate way to think about things? Or is that too generous?

Bob Lyons:

I think at this point, it's very difficult to pinpoint that number, Justin. I can tell you requests for retrofits at GATX -- I can't think of any offhand. Brian, I don't know if you have any --?

Brian Kenney:

No. On legacy cars, it's literally zero. As far as CP-1232s, the jacketed car, GATX has 1,800 of them. And we will retrofit those. That's just replacing or reconfiguring the bottom outlet valve handle and then doing some stenciling, and it's a few-thousand-dollars. And it's -- they are very young cars. Lot of -- lots of economic life left. That makes sense. None of the other ones do, so we won't be retrofitting; we'll be scrapping.

So you’re getting to the replacement cycle for those. And our position has been the market is already served in the crude oil market, and therefore, we don't think a lot of that -- a lot of those orders are going to go anywhere, and we don't think that demand for retrofits is real. And so we are a little more skeptical than others in the industry that that will materialize this replacement cycle. It will, to some extent, but not to the extent that others are saying -- we don't think.

Justin Bergner:

Okay. But I mean could it make the trough a little bit more shallow than sort of the depth seen in prior recessions when you got sub-20,000?

Brian Kenney:

Sure.

Justin Bergner:

Okay. All right, thank you.

Bob Lyons:

Thank you.

Operator:

And we'll take a follow-up question from the site of Michael Cohen -- please go ahead.

Michael Cohen:

I'm sorry for the follow-up. But quick question, you had mentioned something about in your commentary about intermodal being strong based on consumer demand. Could you just provide a little more commentary on that, just given the fact that the intermodal shipping container seems to be under a bit of a challenged environment?

Brian Kenney:

No, you're right there. That's stronger relative to the rest of our fleet.

Michael Cohen:

Okay, great. Thank you.

Bob Lyons:

Yes. Thank you.

Operator:

And at this time, we have no further questions. I'd like to turn it back over to the speakers for any closing remarks.

Chris LaHurd:

Yes. I'd just like to thank everyone for their participation in the call. And you can give me a call if you have any follow-up questions. Thank you.

Operator:

We'd like to thank everybody for their participation on today's conference call. Please feel free to disconnect your line at any time.