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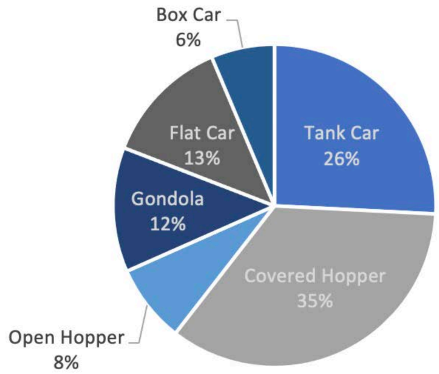
Rail-Car Leases

In recent years, Preserver has increased its exposure to income-generating infrastructure assets. Income-generating infrastructure assets include real estate, cell towers, billboards, pipelines, and inland marine vessels. These strategies are attractive due to the stability of the cash flows, hard asset collateral, lease rate escalators, and income generation.

Another investment strategy that fits within our infrastructure income thesis is rail-car leasing. Railroads and other rail-car asset owners lease their rail-cars to shippers under long-term leases. The global market for rail-cars remains fragmented with the top ten lessors owning 55% of the 1.6 million rail-car market. The table below shows a breakdown of the top ten lessors, which include TTX, Wells Fargo Rail, UTLX, and GATX.

LESSOR	OWNERSHIP ENTITY	FLEET SIZE	%
TTX	Railroad	170,000	10.1%
Wells Fargo Rail	Bank	165,000	9.8%
UTLX	Public Co.	125,000	7.4%
GATX	Public Co.	120,000	7.1%
CIT Rail	Bank	116,000	6.9%
Trinity Rail	Public Co.	103,000	6.1%
SMBC Railcar	Japanese Bank	53,000	3.2%
ITE Management	Investment Fund	35,000	2.1%
The Andersons	Public	23,000	1.4%
PNC Rail	Bank	17,000	1.0%
All Others		755,208	45.0%

Source: ITE Management Presentation June 2021; Drewry Maritime Research - Annual Report , AAR 2019 Rail Equipment Data, Public Filings.



Source: ITE Management Presentation June 2021; Drewry Maritime Research - Annual Report , AAR 2019 Rail Equipment Data, Public Filings.

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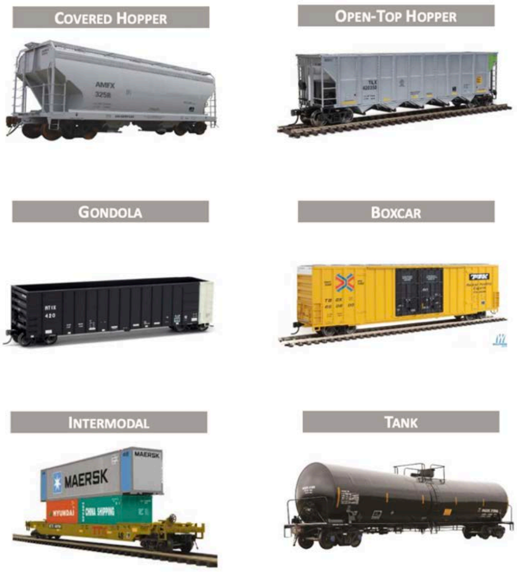

The types of freight rail-cars are autoracks, gondolas, hoppers, tank cars, pine cars, boxcars and flatcars. Rail-cars are considered essential to shippers; thus, it is rare that a shipper will return rail-cars at lease expiration. In addition, the lease payments are a small, but essential expense in the cost of doing business for shippers.

Through stable cash flows, rail-car leasing can generate un-levered cash yields near 6-8%. With moderate leverage, levered pre-tax cash yields can reach 9-10%. Leases are typically 2-10 years with annual escalators, and are typically full-service, which means the lessees are responsible for maintenance and operating costs. Rail-cars depreciate to a scrap value on a straight-line basis over 35-50 years, but they are eligible for accelerated depreciation, which can add 200-300 bps of additional returns to taxable investors. The favorable tax treatment makes rail-car leases one of the few investments where after-tax returns are higher than pre-tax returns.

Diversification across rail-car types, lessees and lease expiration is important to maintaining a resilient portfolio as economic cyclicality in shipped goods can have varying impacts on the lease rates for different rail-car types. 2020 was a down year for railroad volumes and lease rates, while 2021 has witnessed a rebound in both. According to Freight Movers, U.S. carloads in 2021 are higher than 2020 but still on the lower end of the last five years as the Class I railroads seek to replace dwindling coal volumes.

The combination of its 11-12% after-tax yield, exposure to infrastructure assets, inflation hedging attributes, low correlation to financial assets, and stable cash flows make rail-car leases an attractive investment.