GATX | GATX Corporation

2015 Fourth Quarter Conference Call — January 21, 2016

Operator:

Good day, everyone, and welcome to the GATX Fourth-Quarter Conference Call. Today's call is being recorded. And at this time, I'd like to turn the Conference over to Chris LaHurd. Please go ahead.

Chris LaHurd:

Thank you. Good morning, everyone, and thank you for joining us for our fourth-quarter and 2015 year-end conference call. With me today are Brian Kenney, President and Chief Executive Officer; Bob Lyons, Executive Vice President and Chief Financial Officer; and Tom Ellman, Executive Vice President and President of Rail North America. I'll provide a very brief overview of the numbers, and then Brian will discuss 2015 as well as the year ahead. Following Brian's comments, we will open it up for Q&A.

Now before we begin, 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 2014 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.

Today, GATX reported 2015 fourth-quarter net income of $58.2 million or $1.37 per diluted share. This compares to 2014 fourth-quarter net income of $58.5 million or $1.30 per diluted share. 2015 fourth-quarter results include net negative impacts from the exit of Portfolio Management's Marine investments, which we outlined at the end of the third quarter, and Other Items of $3 million or $0.07 per diluted share.

We reported net income of $205.3 million or $4.69 per diluted share for the full-year 2015. This compares to net income of $205 million or $4.48 per diluted share for 2014. 2015 full-year results, including net negative impact from the exit of Portfolio Management's Marine investments and Other Items of $29.6 million or $0.68 per diluted share.

So, rather than me go through a deeper 2015 review, we thought it'd be more beneficial, more valuable, for Brian to discuss 2015, and the challenges and opportunities we anticipate in 2016. So, with that, I'll turn it over to Brian.

Brian Kenney:

Yeah, thanks, Chris. So what I want to do is provide color on our 2016 earnings outlook. Now, obviously these are very volatile times. Among other things, we have a slowing Chinese economy; we have falling commodity prices; we have oil prices below $30 a barrel; we're facing an industry with an oversupply of railcars; and you have the worst start to the year in the history of the U.S. financial markets.

But despite all that, we're entering the year in great condition. As Chris outlined, as you saw in the press release, our worldwide rail business had another record year in 2015, and we're sitting here today with North American fleet utilization over 99%; we have almost all of our 2016 new car deliveries placed; we have a much lower number of existing cars scheduled for renewal in 2016 compared to prior years. So I think we've positioned the fleet very well to withstand this weaker market.

So let's go into some detail on the outlook for North American Rail. In today's market, absolute lease rates for most car types are declining. So obviously, you can't expect to realize the record lease rate increases that we produced over the last two years.

But having said that, because of the way we structured our fleet and our lease term over these last few years, we still expect to see many instances of lease rates increasing over expiring rates when cars renew in 2016. And sitting here today, we expect our Lease Price Index to show a flat-to-slightly positive renewal rate change in 2016.

On the fleet utilization side -- again, we are sitting here today at 99.1% utilization -- that's full utilization of our fleet. We do expect utilization pressure, given 2016's weaker market. And obviously, it's hard to predict with certainty, but we currently anticipate utilization will trend down, but remain in the high 90s throughout 2016.

On the investment side, we expect a similar level of railcar investment this year compared to 2015. Again, almost all of those new cars are already placed with customers. So a younger and larger fleet will contribute to revenue in 2016. The net effect on revenue in North American Rail, if you combine the placement of new cars delivering with flat-to-positive renewal rates on the existing fleet, and then somewhat lower fleet utilization, it will result -- or expected result in 2016 revenue that is slightly higher than 2015.

The next driver worth mentioning is net maintenance expense in 2015. And again, this year, we'll continue our strategy to move more maintenance into our own network and away from certain third-party providers, particularly true for tank car maintenance. We find that safety and quality is much higher when we perform the maintenance internally, and with the strides in efficiency we've made over the last few years, we performed that maintenance more cost-effectively internally as well. So we'll continue that strategy.

Looking at tank car qualifications that are due this year -- and that's a major maintenance cost driver -- it's a few-hundred cars lower than in 2015. So, offsetting that maintenance decrease from lower compliance work, we'll have more cars entering the network for commercial reasons. So, primarily lower renewal success, more assignment of cars to other customers. Thus, on a net basis, maintenance expense in 2016 will be flat-to-slightly higher than it was last year.

And the last factor worth mentioning for North American Rail is remarketing income. We'll continue to optimize our fleet -- we always do -- through secondary market sales of railcars. We did it every year through the last downturn. We'll do it again in 2016. But given where the market's going, we don't expect to see the values nearly as high as what we realized last year. And thus, remarketing income will be down materially in 2016.

So the net effect of slightly higher revenue, increased ownership costs from new car investments; flat-to-slightly higher maintenance; and then much lower remarketing income, results in North American Rail segment profit that we expect to be down in 2016 in the range of 10% to 15% from last year.

Looking at International Rail, and specifically GATX Rail Europe, they've been performing very well financially in a difficult market for a number of years. And they've been modernizing their fleet in that process. Both those trends will continue in 2016. Their new car investment level will be down somewhat from last year, but we still expect fleet growth this year. And that fleet growth, along with small lease rate increases on the existing fleet, should result in higher revenue in 2016.

Now, that revenue increase will be offset somewhat by higher ownership costs from growing the fleet as well as higher maintenance expense, really due to scheduled car revisions. Offsetting the operational improvement in International Rail will be the effect of the stronger dollar. And so the net effect of all these factors is that Rail International segment profit is expected to be relatively flat in 2016.

Moving on to Portfolio Management, our experience in leasing partnerships with Rolls-Royce performed very well in 2015. They also had robust investment volume as well. They added over $300 million of engines to the portfolio last year, and they also recognized attractive gains in disposing of older engines from the portfolio. We expect a similar year financially for the Rolls-Royce partnerships this year.

Also within Portfolio Management, this year, we're going to complete the strategic sale of the Marine assets. Once again, keep in mind that those assets are different than the ones we're exiting -- or the ones we are exiting are different than the American Steamship segment -- it's unrelated.

So, apart from the gains on the sale from completing the strategic exit from Marine in 2016 -- so the Marine assets will no longer contribute to Portfolio Management earnings going forward. And the net effect is that we expect Portfolio Management to show a flat segment profit in 2016 on a normalized basis.

At American Steamship, they had a very tough year financially in 2015. Their iron ore volume that they carry dropped 4.5 million tons from the prior year. That was driven by declining domestic steel production, obviously. Average capacity utilization for domestic steel mills was 60% in 2015 as compared to 75% the prior year. And if you look at the primary drivers, you had global excess steel manufacturing capacity; increased imports; the stronger dollar. We don't think those conditions are going to improve in 2016, and thus, we're expecting that ASC will carry similar volume this year as they did last.

However, we expect that this tonnage will be carried in 11 vessels as opposed to the 13 that sailed in 2015. And that will result in significant savings from -- you avoid substantial costs that you would ordinarily incur to fit-out those two additional vessels for the sailing season. And thus, we expect American Steamship profit to be up. It could be up 20% or more in 2016, but that's off a pretty low base from 2015.

And then moving to Corporate -- on the SG&A side, we expect SG&A to drop in 2016 by about 3% to 5%. That's due in part to the savings from that early retirement program that we implemented in the fourth quarter of 2015. That program alone should generate $3 million plus savings per year for the foreseeable future. But we also have -- we have a tight control on SG&A. And general tighter cost control across the organization will allow us to decrease that in 2016 as well.

And then, lastly, we took on less debt to finance our growth in 2015 by using those sales proceeds from exiting the Marine business within Portfolio Management. And since we maintain a target leverage for our business segments, that will result in less interest expense allocated to the Corporate segment in 2016. And that will mean about a $10 million difference, positive, year-over-year.

So if you consolidate all that segment guidance, you result in a 2016 total net income for GATX that we currently expect to be somewhat lower than last year, but an EPS that is essentially flat with 2015. And that's how we arrive at that annual guidance of $5.25 to $5.45 per diluted share.

So that's a little more color on the guidance. As I said to lead off, these are difficult economic times. But sitting here today, we started discussing at the beginning of this downward trend in the railcar leasing market on these calls back in mid-2014, and then we produced record earnings in 2014, record earnings in 2015. We're projecting to be close again in 2016. So I think that's a good indication of how we've used the up-market to protect our fleet as the market turns down.

I'd also address quickly the issue of capital allocation. I think everyone on the call is aware of GATX's commitment to return capital to its shareholders, both consistently and in various forms. 2016 will mark the 97th consecutive year of dividend payments by GATX, and that's a record that few companies can match. And in addition, if you look over the last 10 years, we've also repurchased almost 17 million shares of GATX stock. So that returned another $750 million to shareholders by that method.

Now, we have repeatedly explained to investors that the actions that we took in the strong market of the last few years in order to lock-in as much committed revenue as possible. As you saw in the press release, that committed revenue now amounts to over $4 billion. So that amount of committed revenue, combined with the record financial performance that we posted the last few years, that really helped solidify our commitment to continue to return capital to our shareholders in the coming years. And equally important, it allows us the flexibility to pursue attractively-priced assets. And they inevitably come up for sale in a weak rail market.

So I'll just close by assuring you that I am acutely focused on maintaining that right balance of growth and returning capital to shareholders. So let's go ahead and open it up to questions.

QUESTION AND ANSWER

Operator:

(Operator Instructions) And we will take our first question from Justin Long with Stephens. Please to ahead.

Justin Long:

Good morning, guys. I wanted to start with a question on the guidance. You mentioned the expectation for remarketing income in North America, in North American Rail, to be down materially in 2016. But could you talk about the order of magnitude you expect?

And also, as we think about a railcar demand environment that is progressing more towards replacement levels, what would you view as a normalized level of remarketing income for your business?

Bob Lyons:

Justin, its Bob Lyons. Thanks for your time this morning. So this past year, as you know from the results in the financials, we did about $67 million of remarketing income at Rail. In North America, we told you coming into the year it was going to be a strong year, and it was.

As we look out into 2016, yeah, I think right now it looks to be somewhere in the range of $40 million versus the $66 million or $67 million from last year. That's still a very healthy number, and reflective of the fact that, even with packages we are putting out in the marketplace today, we continue to see interest in our assets. And we'll see how that progresses during the course of the year.

I also think, unlike last year where it was more heavily weighted to the beginning of the year, it'll be evenly spaced during the course of the year. And even in the -- if you go far enough back and look at 2009 and 2010, to that period in the marketplace when it was extremely stressed, and the financial markets were extremely stressed, we still did $20 million, $30 million of remarketing income in those years. So, $40 million is a very reasonable number.

Justin Long:

Okay, great. That's really helpful. And second question -- I wanted to focus on some of the things Brian said on capital allocation. Given the prior buyback program is wrapped up, I thought there was a chance we could see another authorization on the quarter. Should we read into that that maybe there's more opportunity in terms of the acquisitions that you're seeing in the market? Or are you still contemplating another buyback program?

Bob Lyons:

That's really more due to timing than anything else, Justin. Our Board meeting is next week. Our regularly scheduled January meeting is next Friday, so that's when our Board will contemplate both the dividend, and we typically look at dividend increases at this time of the year, and the stock buyback.

And I can tell you we'll contemplate an authorization. The last authorization we had was for $250 million. We completed that this past year, as we noted in the press release. We will contemplate another authorization in that same level. And I could like -- I could see that being completed in a similar pattern to what we did with the last authorization, over a two-year period. Again, I have to reiterate that granting an authorization is a Board decision, but it is our expectation we will present the Board with a proposal.

Justin Long:

Okay, great. And I would assume, since nothing has been announced, that's not included in the guidance number, the EPS guidance you gave?

Bob Lyons:

No, we are assuming in the guidance that we gave that there would be some authorization and action under that authorization in 2016.

Justin Long:

Okay. And does that assume a similar program, that $250 million program, like you mentioned over two years?

Bob Lyons:

Yes, correct. Somewhere in that range. And again, it's the Board's discretion. But yes, that has been contemplated already. And obviously, given where the stock price is at, we have been buying the stock back at levels higher than this, and I'm comfortable with that. We like to buy rail assets, as you know. And given where the stock's trading today, we will be -- we'll look at all alternatives for capital allocation. But that one looks very attractive.

Justin Long:

Okay. Thanks, Bob. And last question, if I could sneak one more in. Given some of the demand, uncertainty and macro fears, and you alluded to some of that in your remarks, but I wanted to ask about your comfort with the balance sheet. When you stress test the model, do you feel comfortable with the amount of leverage on the business today, even if we were to slip into a recessionary period in the broader economy?

Bob Lyons:

Absolutely. Given where our leverage is today -- you know, it's interesting. We normally get questions about trying to turn -- take leverage up a little bit. We manage that conservatively. We have a solid investment grade rating. That matters a lot to us, particularly in markets where the financial markets get a little bit more stressed. But I'm very comfortable with where the balance sheet is today -- where leverage is today.

In addition to using this up market to extend term in our railcar portfolio, we've done the same thing on the balance sheet side. The average life on our debt today is about 7-1/2 years. That was about 3-1/2 years going into 2008. And our weighted average cost of debt today is under 4%. So I feel we're in an excellent position, particularly given, as Brian noted, the committed lease revenue of north of $4 billion.

Justin Long:

Okay, great. I'll leave it at that. Thanks for the time and congrats on the execution in the tough environment.

Bob Lyons:

Thanks.

Operator:

And we'll take the next question from Matt Brooklier with Longbow Research. Please go ahead.

Matt Brooklier:

So you mentioned in the release your lease rate expirations being at a lower level in '16. But could you give a little bit more color in terms of the number, if you have it, how that compares to '15? And maybe, on a historical basis, what the average lease rate expiration has been?

Chris LaHurd:

Yeah, Matt. I'll -- let me hit on both exposure and expiration. So, 2016 renewal exposure is -- it's only 12,500 cars. 15,000 cars were to expire in 2016, but we early-renewed about 2,500 of those. So, obviously, this reduces the actual exposure for the year. And just for comparison purposes, we saw that number around 17,000 for 2015.

Matt Brooklier:

Okay. And if we look out to '17, are we anticipating expirations are still at kind of this lower-end level? Or are you able to look out that far?

Brian Kenney:

Yeah, I think you've got to be careful projecting beyond a year, because it really depends on this year's activity. And for instance, if certain car types that we do renew are at a rate that we don't really like for the long term that much, we're going to go shorter on there. So it's very hard to start projecting out more than a year, because it depends on this year's commercial activity.

Matt Brooklier:

Okay, that's helpful. I guess, can you talk to some of the other potential cost levers that you can pull as we're going into a moderating environment? You talked to the early retirement program that you've offered in fourth quarter. But I'm just curious to hear if there's any more offsetting potential factors as things potentially continue to moderate --

Brian Kenney:

Well, SG&A is the main cost lever that we can control. I think a lot of people expect us to say maintenance as well, but a lot of that is commercially driven and just driven by the structure of your fleet. Now, it happens to be a light year for compliance in 2016. It's projected to be kind of light again in 2017.

But if commercial activity is such that there's a lower renewal success rate and a lot of assignments to new customers, you could see the maintenance go up beyond where we project. So, that's a risk factor. So really, it's SG&A, as far as what you can impact directly and quickly on the cost side.

And I -- again, I think if you normalize 2015 by pulling out that $9 million charge -- because that really doesn't -- you know, it's going to have a big decrease in SG&A in 2016. But you have to pull that charge out. And I think that gets you to about $183 million normalized SG&A. And I think we can hit that by 3% to 5% in 2016.

Matt Brooklier:

Okay. And your comments regarding pulling more of your maintenance and specifically for tank cars in-house, is that just -- is that something that you were planning on already? Or is that a reflection of, I guess, outsourced maintenance costs starting to rise as kind of the North American network is getting tighter? I'm just curious to hear kind of the thought process in terms of the drivers with taking more of your maintenance cost in-house.

Brian Kenney:

We've been doing it a lot. We did it in 2015, to a great extent. We're going to do it again over the next -- continue that over the next year. It's really a strategy because we believe our quality and our delivery is much higher internally. That's been our experience, versus third-party providers or at least most third-party providers. And we've worked very hard getting more efficient within our own network. And now we are to the point where we're lower cost than our external providers as well. So yes, that's a strategy, to continue to pull inside.

Matt Brooklier:

Okay. Helpful. Appreciate the time.

Operator:

Our next question is from Mike Baudendistel with Stifel. Please go ahead.

Mike Baudendistel:

I wanted to ask you -- on your agreement with Trinity, I think you said that you have commitments from customers to take a lease of the equipment in 2016. Do you have much visibility beyond 2016, since that's a multi-year agreement?

Tom Ellman:

Yes, and actually there's two agreements. So the 2011 agreement is coming to the end. We've placed practically all cars from that. We just have a little over 100 cars left. And then we had a second agreement that we did in 2014 for 8,950 cars. That agreement, the deliveries pick up starting in August of 2016. And on that agreement, we have placed between 10% and 15% of the cars. So we mentioned on the call we've placed pretty much all the cars through 2016 deliveries and we've placed a handful into 2017.

Mike Baudendistel:

Great. That's helpful. And then another question on your press release, you -- I just want to make sure I'm interpreting this correctly -- it sounds like, in 2016, you may or may not be purchasing equipment in the secondary market, sort of depending on the trajectory of the prices of that equipment. But maybe you have to see prices come down a little bit more, further, until you invest more heavily. Am I interpreting that correctly?

Tom Ellman:

Well, we're always looking for investment opportunities both in the new and secondary market. In 2015, we were a net seller because we found the prices attractive in that market. And we were less of a net buyer. As the market changes, we'll have to continue to monitor that, but it's something that we look for in every market.

Mike Baudendistel:

Okay, thanks. That's all for me this morning. Thank you.

Operator:

We'll go to Art Hatfield with Raymond James.

Art Hatfield:

Hey, morning. Thanks for taking the time this morning. Brian, I kind of hope -- I don't know if I'm going to ask this right, but I kind of want to get your feel for how you see a potential downturn? It seems to me that as we enter this period, we've got a difficult economic backdrop, as you noted, but we also enter it with an obscenely high new railcar backlog. And we know that some of that's been pushed out into later years.

And we could -- you know, you could almost make the argument that the beginnings or a good portion of the next upcycle is already in the book, and we may see an extended period of very weak new car orders. Would you characterize kind of those dynamics, as we enter this period, as something that could bring about much worse carnage in the industry than we saw in the '08/'09 recession?

Brian Kenney:

Yeah. I would say it's certainly possible. Because, remember, we've been talking, before demand started to drop and you started to have these economic uncertainties that you're seeing in today's market -- we've been talking about the oversupply, especially in the energy portion of our market, for a year and a half. So this, to us, was a supply-driven downturn. And now it's been exacerbated a little bit by potential economic weakness out there.

So, yes, it seems that, going into this period of weakness, there's a lot more in the way of oversupply than there was going into the last one. The last one seemed to be more demand-driven. But, Tom, do you --

Tom Ellman:

Oh, no, I would absolutely agree with that. The one thing I'd point out, though, from a GATX perspective, is because the upturn that came before was even stronger than the last upturn; we were able to put out even more cars at higher rates for longer terms. So despite the -- I agree with Brian on the economic situation -- GATX is entering it a little better prepared.

Art Hatfield:

And to that question -- and I agree with your assessment; you guys have done a great job of prepping yourself for this. When do you get -- I want to ask this the right way, because I know you don't want to get too far out. But when does it get -- when does the length of the downturn start to -- where you start to feel some significant pain? Is it something where we'd have to see this continue into mid-part of '17? Or does it take you all the way to '18? How should we think about that?

Brian Kenney:

Well, I think, given the -- well, it depends, Art. I don't know; it's very hard to have visibility. It's a very volatile market out there in terms of where lease rates are going, for instance. I think if we can protect our utilization, we'll be in very good shape for a number of years. And that's going to -- to a large extent, it's going to depend on how exacerbated this oversupply situation is and where demand is going.

On the rate side, given current trends, it's going to be much more difficult. But that works its way through the fleet much slower.

Art Hatfield:

Right

Brian Kenney:

So really, the big -- and it's true for 2016 as well. The biggest factor, swing factor, both up and down, is North American rail fleet utilization.

Art Hatfield:

Okay

Brian Kenney:

We say – we're projecting it's going to trend down a little bit, but it's going to stay in the high 90s. If we can maintain it where it is today, that's an upside to this earnings guidance. If we can't and situations are tougher, that immediately hits us quicker and that's downside to our earnings guidance.

And the second-order effect of that -- we've already referred to it as the maintenance side -- if utilization drops, maintenance is going to go up as well because -- it depends on the type of car return to some extent. But generally, there's more fleet activity, there's more cars entering the maintenance network, there's more cars going to different customers. That drives higher maintenance expense. If it's higher-than-expected utilization, we'll have lower maintenance expense.

So utilization is the big risk factor for 2016 and really for any rail business at all. On the rate side, things are trending down. We're projecting a positive, slightly positive LPI this year. 2017? You can do the math. If rates continue down, it's not going to be positive any more.

Art Hatfield:

Right. Right.

Brian Kenney:

So it's hard to look out and see how bad it's going to be and how -- and when it's going to finally hit us. But eventually, our long terms expire as well --

Art Hatfield:

Right

Brian Kenney:

-- and this thing starts to get to us.

Art Hatfield:

Right. Okay. That's actually -- that's helpful. I appreciate that. A couple other questions. First, are you starting to see any pressure on new car prices?

Tom Ellman:

Yes. Okay. So, the answer is yes, and it comes from two different areas. One, the component costs -- the steel prices that go into the cost for the builders, are coming down. And then obviously in this environment, that's more people chasing fewer deals, the pricing power of the builders is not where it had been.

Art Hatfield:

Okay. And is that moving down fast or just kind of a steady decline? Or is it car-type specific?

Tom Ellman:

Yes, you know, like every question, it varies by car type. But I would say that, in totality, market rates for the cars are coming down at a good pace.

Art Hatfield:

This -- and this is my final question; again, I appreciate the time. And this may be way too early to have a clue or have an answer to, but are you starting to see or sense that some competitors out there that got real aggressive with the energy upturn are starting to feel some real pain?

Brian Kenney:

It's too early -- too early to tell, Art. And, you know, a lot of people ask me about that, especially in terms of acquisitions or when can you pick up assets in the secondary market?

And when will they be at the right price? And as I think about that, generally, when we've been successful there, it's been out of bankruptcy or troubled financial situations. So, I don't see that yet. And so I would imagine we're just going to have to wait a while and wait for some pain to develop.

Bob Lyons:

If you go back -- Art, if you go back to 2008, we started talking about a slowdown in early 2007.

Art Hatfield:

Right

Bob Lyons:

Put up record earnings in 2007/2008, and really didn't see robust activity from distressed sellers really until late 2009/2010, was really when it started to kick in.

Art Hatfield:

And was some of that selling, though, related to more the bank crisis and people not being -- people going into bankruptcy because of other things? Do you need that type of scenario this downturn? Or do you just think that you're going to see distressed assets because of the investment decisions people have made over the last few years?

Brian Kenney:

You know, that's a good question. I think, if you look at the two fleets that we either added to our owned and managed fleet, I think one was more rail distress and the other was a combination of what you're talking about.

Art Hatfield:

Okay, that's helpful. Hey, thanks for the time this morning. Appreciate it.

Operator:

We'll go to Steve O'Hara with Sidoti & Company. Please go ahead.

Steve O'Hara:

Good morning. I was wondering if you could just quickly talk about, in terms of the -- maybe the cars that come off in 2016, is it -- would you say it's more favorable than the average in terms of where the market sits today than maybe it normally would be? Or is it less favorable? Or kind of just normal or average?

And then just on the opportunity for investment, I mean, are there areas that -- are you really strictly looking in North America or other geographies? And then are there, let's say, pools of car types or something like that you may avoid or wait a little longer on? Thank you.

Tom Ellman:

So I'll start with the North American situation and let others address other geographies. I think your question maybe was in terms of mix of what is expiring in 2016 versus other years.

Our fleet is large enough, and we focus enough on diversity, that, in general, the year 2016 is not much different than any other year, with one big exception. And that's anything related to the oil boom. We really went out of our way to have less overall exposure in the near term to small cube-covered hoppers which carry the sand, and some of the tank car types that carry the crude oil. So it's a relatively lighter year there.

Conversely, in coal, that market has been challenged for a while. So we've been going relatively shorter term on coal cars. So that's maybe a little bit heavier.

Steve O'Hara:

Okay. Thank you.

Brian Kenney:

And as far as acquisitions beyond North America, Europe being the primary place we look and we poke, there's really just been one fleet that has changed hands over the last couple years -- and it has been an unsettled market in Europe for a number of years. And that was the Nacco fleet, which I think was around 10,000 cars that CIT picked up.

So we constantly search and we poke. But honestly, we're looking more at organic growth in Europe from -- what we've been doing with existing customers, upgrading and modernizing their fleets. We are looking at new geographies, so Eastern Europe is big for us. We already have a strong presence. And the fleet is much older and in need of replacement there.

There are certain freight car types where the commodity flows are very stable and the fleet of incumbents are aging. So, I look at more organic growth right now being higher potential in Europe than an acquisition opportunity.

Steve O'Hara:

Okay. And then just -- could you just -- have you talked about the plans for the proceeds from the sale in Portfolio Management from the Marine assets? Is that -- do you expect that to fund the share repurchase agreement? Or what -- just debt paydown or what?

Bob Lyons:

Yes. It's -- you know, dollars are really fungible, so I look at those coming in the door the same as other -- cash from operations or other portfolio proceeds. So it really kind of co-mingled into the total mix of cash inflows, very strong cash inflows that we see in 2016. And we'll use those as we normally do, to fund our hopefully continued growth in the fleet and looking for opportunities on that front, dividend buyback, et cetera.

Steve O'Hara:

Okay. And then lastly, on the boxcar fleet, can you just talk about what utilization was in the quarter and maybe your outlook on that portion of the fleet?

Tom Ellman:

Yeah. So the boxcar fleet continues to perform extremely well. We were over 97% for the year for the boxcar fleet. And going forward, we expect that to perform well. It's an area that I don't think you'll see a lot of incremental investment, but the assets that we have are continuing to do well.

Steve O'Hara:

Okay. Thank you very much.

Operator:

We'll now go to Justin Bergner with Gabelli & Co.

Justin Bergner:

Good morning, everyone.

Bob Lyons:

Good morning

Justin Bergner:

I have a couple questions here. I guess, first, to clarify an earlier comment on or question in regards to the number of railcars that are up for renewal -- was that meant to be a North American number? And was it inclusive of boxcars or just ex-boxcars?

Chris LaHurd:

Yeah, that's a wholly owned North American number, and that excludes boxcars for comparative purposes to prior years.

Justin Bergner:

Okay, great. Thanks, that's helpful. Second question was a more big-picture question, which is, what is the impact of sort of ongoing trends in rail utilization and perhaps weaker scrappage due to low steel prices? How is that sort of affecting the outlook for your business?

Bob Lyons:

I don't think it's really affecting the outlook for the business, per se. You can see the impact it's had on the scrap income that we generate. We break that out for you on the segment tables in the income statement. And you can see that in 2015, scrap income was down quite significantly. Fortunately, it's not a significant driver of our overall segment profit. But definitely the numbers there were lower.

I don't know, Tom, if you have anything else you want to add on that?

Tom Ellman:

Yeah. No, the one thing on the scrap prices, it does come into play when we look -- a car comes in the shop and you have to make a decision on whether to repair it or to scrap it. You look at the economics of what the car is going to continue to earn over its life and compare that to the scrap proceeds. So when scrap prices are down, it makes it relatively more likely that you would repair a car than scrap it.

Justin Bergner:

Okay, great. Thank you. And on the rail sort of utilization trend, I mean, is that still -- is improving rail utilization still a headwind for the tank car and railcar demand? Or is that sort of stabilizing?

Tom Ellman:

Yes. So I think maybe you are talking about improved railroad performance?

Justin Bergner:

Yes.

Tom Ellman:

Yeah. So -- okay. So, railroad performance -- when it performs well, car types that move relatively more miles are more impacted than the ones that move relatively less. So the core historical part of GATX's fleet -- tank cars, specialty covered hoppers -- are impacted relatively less. Car types like intermodal and coal that move more miles are impacted relatively more.

As long as railroad operations stay very fluid and very strong, you're going to see that as a headwind on those high-mileage car types. What that's going to mean going forward is difficult to say, because there's a lot of things that are out of the railroads' controls in that regard, the most important of which is weather. So the railroads certainly are going to try to maintain that performance, but we'll have to see what happens.

Justin Bergner:

Great. Thank you. I'll ask one more and then get back in the queue, which -- my final question for now is, your affiliate earnings within Portfolio Management were up strongly year-on-year. And I guess you are suggesting the Rolls-Royce joint venture can hold flat next year.

Why were the earnings up so strongly in the fourth quarter? And why is the engine leasing market looking better than the aircraft leasing market, where we've heard trends are rolling over fairly substantially?

Bob Lyons:

Yeah. Well, keep in mind, too, we are also in the -- we talk about aircraft engine leasing. It's a spare aircraft engine leasing business, so the dynamics there are a little bit different than those that are coming out with -- on wing with new airframe. Rolls did have another particularly strong year. It was up a little bit in the fourth quarter, as they had some remarketing events, too, in the fourth quarter. So that flowed through positively -- our share of that.

Looking out over the course of the next few years, we expect continued strong performance there operationally as well as some opportunities to remarket some engines. We have a very big installed base, north of 400 engines, almost 425 engines today, $3 billion asset base there of high-quality equipment with very high utilization.

Historically, what we've seen is airlines need their spares to run their airlines. And while they may be able to turn back aircraft from time to time, typically the spares that are in their network, they need to have in the network. And even in challenged times, they continue to make lease payments on those and need the spares to operate the airline in total.

Justin Bergner:

Thank you.

Operator:

And we'll now go to Steve Barger with KeyBanc Capital Markets. Please go ahead.

Ken Newman:

Hey, good morning. It's Ken Newman on for Steve. The first question is on free cash flow in 2016. You may have touched on this a little bit earlier in the call, but can you remind me -- how are you guys looking at CapEx as it relates to 2016? Is that going to be similar to 2015 levels? Or should we expect that to be higher or lower?

Bob Lyons:

In total, we had about a $700 million -- we had just under $715 million of total CapEx spread across all the business segments, obviously with the majority of that in Rail North America and Rail Europe. As we look out to 2016, we'd see a similar number. And obviously, we'll be opportunistic. If we see more attractive assets in the secondary market, we're certainly in a position we can capitalize on those. But what we're thinking today is we will be in the same range as 2015.

Ken Newman:

Got it. And then you talked a little bit about the headwinds for lease rates in terms for the entire portfolio. I was curious -- can you give a little bit more detail on what you are seeing in the environment for non-energy tank cars rather than just the energy?

Tom Ellman:

Yeah. So in looking at the demand drivers, there's a few different aspects, some of which impact the entire fleet, some of which impact just a portion of it. The overhang of excess builder capacity impacts every car type. And the non-energy car types are no exception.

What has held up pretty well there is demand. The railcar loadings are down across the board, but they're down pretty modestly in those non-energy tank car types. So those have been hanging in there pretty good, particularly on the existing car side.

We've talked before about how, if the customer has a car, switching it out is a tough situation. So they're switching costs and disruptive to their operations. So those we'd expect to hang in there pretty good on the existing car side. New car opportunities in that area are going to be really heavily competed for, because there's going to be relatively less places to put those new cars with a pretty big supply base.

Ken Newman:

Got it. And I guess just as a follow-up, can you tell us how many of those non-energy railcars or non-energy tank cars are existing in the fleet today? Specifically, break out the energy cars for us.

Tom Ellman:

Yeah. So, order of magnitude, we have a little under 60,000 total tank cars, and cars serving the energy market are maybe a quarter of that. So, three-quarters, give or take.

Ken Newman:

Perfect, thanks.

Operator:

And we'll now take the next question from Kristine Kubacki with Avondale Partners.

Kristine Kubacki:

Good morning. A question, something we used to talk about quite a bit. I was just thinking -- yes, I guess on a few conference calls ago, you talked about that you'd probably replace cars that were impacted by the regulations rather than retrofitting. I was wondering if you could just give us a little color on if that thought process has changed, and if you're accelerating any timing, given kind of the environment we're in at this point?

Tom Ellman:

Yeah. So first of all, when you talk about what's going on with the impacted cars, you've got to divide it up a little bit. So for legacy cars -- cars that were ordered before October 2011, we do not anticipate retrofitting any of those. That's what we said a few quarters ago. We continue to believe that. And as far as we know, there has been no, or tiny amounts, of activity in that regard in the industry as a whole.

For the CPC-1232, sometimes called the good-faith cars, cars ordered after October 2011, divide those into jacketed and non-jacketed cars. The jacketed cars, we will indeed retrofit because the cost to do that is just about $3,000 to $5,000 per car. That will happen over a very long period of time. It will happen as those cars come into shop for some other reason.

The challenging one to think about are the non-jacketed CPC-1232 cars. The retrofit is expensive. It's probably on the -- order of magnitude, $30,000-$40,000. And so there could be opportunities where that makes sense, but it'll be case-by-case and, at least from a GATX perspective, unclear what we will do in that regard.

Kristine Kubacki:

Okay. That's fair. And then just -- I think we've nitpicked over almost every portion here. But just -- could you talk a little bit about your locomotive (technical difficulty) you're seeing there, in North America, in terms of utilization or how you're thinking about that fleet?

Tom Ellman:

I'm sorry; you cut out. But I think you asked about locomotive utilization. Is that correct?

Kristine Kubacki:

That's correct. Sorry about that.

Brian Kenney:

Okay. Yeah, so our locomotive fleet, which is -- a vast majority is lower-horsepower, four-axle equipment, has held up pretty well. Utilization has been fairly consistent over time. Where we've seen cars not utilized, it's almost exclusively getting them through the shop. Shop space is pretty constrained in that -- for that asset type. And so, when we see dips, it's primarily a result of getting cars through -- I mean, getting locomotives through; I'm sorry.

What you're seeing more broadly, not with these locomotive types that GATX participates in, the high-horsepower, six-axle locomotives, there aren't a big excess in that market.

Kristine Kubacki:

Okay. Very good. Thank you very much for the time.

Tom Ellman:

Yes.

Operator:

And the next question will come from Art Hatfield with Raymond James.

Art Hatfield:

Actually, just a couple follow-ups. And one just came -- comes on the heels of Kristine's question about retrofits. Is it possible that if you retrofit some of those non-jacketed CPC-1232s, that it may extend the life of those cars?

Tom Ellman:

You mean beyond its statutory life?

Art Hatfield:

Yeah.

Tom Ellman:

No.

Art Hatfield:

Okay. Okay. Actually, the other question I was more curious about was, we understand that the definition of utilization is cars under a lease agreement. Do you ever get a feel for kind of what the real underlying utilization level is, i.e., how many of those cars are not being used by your customers that are currently on lease?

Tom Ellman:

Yeah, that's pretty anecdotal, unfortunately.

Art Hatfield:

Okay

Tom Ellman:

If you will recall, during the last downturn, the AAR started providing statistics about cars that haven't moved in 60 days -- that was actually helpful. That helped us get at some of that, but it's hard to do without that statistic.

Art Hatfield:

Okay, fair enough.

Bob Lyons:

They disbanded reporting that number a while ago.

Art Hatfield:

Right. No, I know, I know. And my question was going to be -- if, in fact, you had a good idea, what this looked like relative to prior peaks as we're heading into a downturn? But can't answer it. So, thank you very much.

Operator:

And we'll now go to Justin Bergner with Gabelli & Co.

Justin Bergner:

Just a couple quick follow-up questions. The early retirement program costs -- are those all in the fourth quarter of '15? Or will we see lingering costs into '16?

Bob Lyons:

Sure -- Justin, they are all in the fourth quarter of 2015, in the SG&A line; roughly $9 million pretax.

Justin Bergner:

Okay, that's helpful. And then you mentioned that the Corporate interest will go down because of proceeds on the Marine side. Does that flow through just the Portfolio Management segment? Or does it flow through all the segments?

Bob Lyons:

The interest costs that had historically been borne in that -- at that in the Corporate line item there would get re-allocated essentially back up to the other segments, ratably.

Justin Bergner:

Okay. So we'll see interest expense come down across the segments, not just Portfolio Management?

Bob Lyons:

It would come down at Corporate and up a little bit at the other segments.

Justin Bergner:

Oh, okay.

Bob Lyons:

It's just a redistribution of that interest expense. From a consolidated standpoint, it doesn't have an impact -- it's just geography.

Justin Bergner:

Okay. And then, finally, I noticed that the other revenue line item in Rail North America was up sharply year on year. Could you maybe talk a little bit more about that? And is that something that's going to continue going forward?

Bob Lyons:

It was up more in 2015 over 2014. Some of that is -- the bigger driver on that number is the maintenance revenue line item. We also had some situations where cars are returned at the end of the lease or returned in a condition such that we can make a claim on those cars, and it flows through that line. I wouldn't expect it to be as strong in 2016.

Justin Bergner:

Great. Thanks.

Operator:

And that's all the time we have for questions. So that will conclude our Q&A session for today. And I'll turn it back to Chris LaHurd for any additional or closing remarks.

Chris LaHurd:

Yeah, thanks, everyone. I appreciate the time. And please contact me if you have any questions. Thank you.

Operator:

Thank you very much. And that does conclude our conference call for today. I'd like to thank everyone for your participation, and have a great day.