

CAI International, Inc.
Form 10-Q
May 03, 2019

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the quarterly period ended March 31, 2019

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

For the transition period from to

Commission file number: 001-33388

CAI International, Inc.

(Exact name of registrant as specified in its charter)

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Delaware 94-3109229
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification No.)

Steuart Tower, 1 Market Plaza, Suite 900
San Francisco, California 94105
(Address of principal executive offices) (Zip Code)

415-788-0100

(Registrant's telephone number, including area code)

None

(Former name, former address and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	Accelerated filer
Non-accelerated filer	Smaller reporting company
	Emerging growth company

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If an emerging growth company, indicate by check mark of the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading symbols	Name of exchange on which registered
Common Stock, par value \$0.0001 per share	CAI	New York Stock Exchange
8.50% Series A Fixed-to-Floating Rate Cumulative Redeemable Perpetual Preferred Stock, par value \$0.0001 per share	CAI-PA	New York Stock Exchange
8.50% Series B Fixed-to-Floating Rate Cumulative Redeemable Perpetual Preferred Stock, par value \$0.0001 per share	CAI-PB	New York Stock Exchange

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock	April 30, 2019
Common Stock, \$0.0001 par value per share	17,934,992 shares

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SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains certain forward-looking statements, including, without limitation, statements concerning the conditions in our industry, our operations, our economic performance and financial condition, including, in particular, statements relating to our business, operations, growth strategy and service development efforts. The Private Securities Litigation Reform Act of 1995 provides a “safe harbor” for certain forward-looking statements so long as such information is identified as forward-looking and is accompanied by meaningful cautionary statements identifying important factors that could cause actual results to differ materially from those projected in the information. When used in this Quarterly Report on Form 10-Q, the words “may,” “might,” “should,” “estimate,” “project,” “plan,” “anticipate,” “expect,” “intend,” “outlook,” “believe” and other similar expressions are intended to identify forward-looking statements and information. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their dates. These forward-looking statements are based on estimates and assumptions by our management that, although we believe to be reasonable, are inherently uncertain and subject to a number of risks and uncertainties. These risks and uncertainties include, without limitation, those in our Annual Report on Form 10-K for the year ended December 31, 2018 filed with the Securities and Exchange Commission (SEC) on March 5, 2019 and our other reports filed with the SEC. We undertake no obligation to publicly update or revise any forward-looking statement as a result of new information, future events or otherwise, except as otherwise required by law. Reference is also made to such risks and uncertainties detailed from time to time in our other filings with the SEC.

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PART I — FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CAI INTERNATIONAL, INC.

CONSOLIDATED BALANCE SHEETS

(In thousands, except share information)

(UNAUDITED)

	March 31, 2019	December 31, 2018
Assets		
Current assets		
Cash	\$ 20,128	\$ 20,104
Cash held by variable interest entities	27,058	25,211
Accounts receivable, net of allowance for doubtful accounts of \$2,839 and \$2,042 at March 31, 2019 and December 31, 2018, respectively	94,729	95,942
Current portion of net investment in sales-type and direct finance leases	74,895	75,975
Prepaid expenses and other current assets	4,422	2,789
Total current assets	221,232	220,021
Restricted cash	29,703	30,668
Rental equipment, net of accumulated depreciation of \$613,838 and \$599,443 at March 31, 2019 and December 31, 2018, respectively	2,176,376	2,265,260
Net investment in sales-type and direct finance leases	465,041	473,792
Goodwill	15,794	15,794
Intangible assets, net of accumulated amortization of \$5,799 and \$5,397 at March 31, 2019 and December 31, 2018, respectively	5,331	5,733
Operating lease right-of-use assets	3,181	-
Furniture, fixtures and equipment, net of accumulated depreciation of \$2,657 and \$2,635 at March 31, 2019 and December 31, 2018, respectively	960	964
Other non-current assets	297	385
Total assets (1)	\$ 2,917,915	\$ 3,012,617
Liabilities and Stockholders' Equity		
Current liabilities		
Accounts payable	\$ 7,361	\$ 7,371
Accrued expenses and other current liabilities	19,869	22,460
Due to container investors	670	2,609
Unearned revenue	5,216	7,573

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Current portion of debt	318,664	311,381
Rental equipment payable	56,221	74,139
Total current liabilities	408,001	425,533
Debt	1,764,695	1,847,633
Deferred income tax liability	38,949	38,319
Operating lease liabilities	1,961	-
Total liabilities (2)	2,213,606	2,311,485
Stockholders' equity		
Preferred stock, par value \$0.0001 per share; authorized 10,000,000		
8.50% Series A fixed-to-floating rate cumulative redeemable perpetual preferred stock, issued and outstanding 2,199,610 shares, at liquidation preference, at March 31, 2019 and December 31, 2018	54,990	54,990
8.50% Series B fixed-to-floating rate cumulative redeemable perpetual preferred stock, issued and outstanding 1,955,000 shares, at liquidation preference, at March 31, 2019 and December 31, 2018	48,875	48,875
Common stock, par value \$0.0001 per share; authorized 84,000,000 shares; issued and outstanding 18,207,676 and 18,764,459 shares at March 31, 2019 and December 31, 2018, respectively	2	2
Additional paid-in capital	119,557	132,666
Accumulated other comprehensive loss	(6,594)	(6,513)
Retained earnings	487,479	471,112
Total stockholders' equity	704,309	701,132
Total liabilities and stockholders' equity	\$ 2,917,915	\$ 3,012,617

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- (1) Total assets at March 31, 2019 and December 31, 2018 include the following assets of certain variable interest entities (VIEs) that can only be used to settle the liabilities of those VIEs: Cash, \$27,058 and \$25,211; Net investment in direct finance leases, \$13,486 and \$13,862; and Rental equipment, net of accumulated depreciation, \$126,305, and \$71,958, respectively.
- (2) Total liabilities at March 31, 2019 and December 31, 2018 include the following VIE liabilities for which the VIE creditors do not have recourse to CAI International, Inc.: Current portion of debt, \$47,816 and \$41,066; Debt, \$117,625 and \$67,615, respectively.

See accompanying notes to unaudited consolidated financial statements.

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CAI INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF INCOME

(In thousands, except per share data)

(UNAUDITED)

	Three Months Ended March 31,	
	2019	2018
Revenue		
Container lease revenue	\$ 75,511	\$ 64,634
Rail lease revenue	7,881	9,104
Logistics revenue	27,716	21,636
Total revenue	111,108	95,374
Operating expenses		
Depreciation of rental equipment	31,784	28,847
Storage, handling and other expenses	5,120	4,100
Logistics transportation costs	24,519	18,665
Gain on sale of used rental equipment	(8,832)	(2,195)
Administrative expenses	14,396	11,241
Total operating expenses	66,987	60,658
Operating income	44,121	34,716
Other expenses		
Net interest expense	23,850	16,899
Other expense (income)	38	(35)
Total other expenses	23,888	16,864
Income before income taxes	20,233	17,852
Income tax expense	1,659	714
Net income	18,574	17,138
Preferred stock dividends	2,207	21
Net income attributable to CAI common stockholders	\$ 16,367	\$ 17,117
Net income per share attributable to CAI common stockholders		
Basic	\$ 0.88	\$ 0.84
Diluted	\$ 0.87	\$ 0.83
Weighted average shares outstanding		
Basic	18,555	20,414

Diluted	18,870	20,672
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See accompanying notes to unaudited consolidated financial statements.

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CAI INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(UNAUDITED)

	Three Months Ended March 31,	
	2019	2018
Net income	\$ 18,574	\$ 17,138
Other comprehensive (loss) income, net of tax:		
Foreign currency translation adjustments	(81)	310
Comprehensive income before preferred stock dividends	18,493	17,448
Dividends on preferred stock	(2,207)	(21)
Comprehensive income available to CAI common stockholders	\$ 16,286	\$ 17,427

See accompanying notes to unaudited consolidated financial statements.

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CAI INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

(In thousands)

(UNAUDITED)

	Preferred Stock		Common Stock		Additional	Accumulated Other Comprehensive	Retained	Total
	Shares	Amount	Shares	Amount	Paid-In Capital	Loss	Earnings	Equity
Balances as of December 31, 2018	4,155	\$ 103,865	18,764	\$ 2	\$ 132,666	\$ (6,513)	\$ 471,112	\$ 701,132
Net income	-	-	-	-	-	-	18,574	18,574
Preferred stock dividends, \$0.53125/share	-	-	-	-	-	-	(2,207)	(2,207)
Foreign currency translation adjustment	-	-	-	-	-	(81)	-	(81)
Repurchase of common stock	-	-	(595)	-	(13,946)	-	-	(13,946)
Exercise of stock options	-	-	27	-	107	-	-	107
Stock based compensation - options	-	-	-	-	221	-	-	221
Stock based compensation - restricted stock	-	-	14	-	618	-	-	618
Payment of income tax withheld on vested restricted stock	-	-	(2)	-	(109)	-	-	(109)
Balances as of March 31, 2019	4,155	\$ 103,865	18,208	\$ 2	\$ 119,557	\$ (6,594)	\$ 487,479	\$ 704,309

	Preferred Stock		Common Stock		Additional	Accumulated Other	Retained	Total
	Shares	Amount	Shares	Amount	Paid-In Capital	Comprehensive Loss	Earnings	Equity
Balances as of								
December 31, 2017	-	\$ -	20,391	\$ 2	\$ 172,325	\$ (6,122)	\$ 397,640	\$ 563,845
Net income	-	-	-	-	-	-	17,138	17,138
Preferred stock dividends, \$0.01181/share	-	-	-	-	-	-	(21)	(21)
Foreign currency translation adjustment	-	-	-	-	-	310	-	310
Issuance of common and preferred stock, net of offering costs	1,600	40,000	100	-	956	-	-	40,956
Exercise of stock options	-	-	2	-	24	-	-	24
Stock based compensation - options	-	-	-	-	416	-	-	416
Stock based compensation - restricted stock	-	-	2	-	188	-	-	188
Payment of income tax withheld on vested restricted stock	-	-	(2)	-	(36)	-	-	(36)
Balances as of								
March 31, 2018	1,600	\$ 40,000	20,493	\$ 2	\$ 173,873	\$ (5,812)	\$ 414,757	\$ 622,820

See accompanying notes to unaudited consolidated financial statements.

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CAI INTERNATIONAL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(UNAUDITED)

	Three Months Ended March 31, 2019	2018
Cash flows from operating activities		
Net income	\$ 18,574	\$ 17,138
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	31,839	28,879
Amortization of debt issuance costs	1,202	945
Amortization of intangible assets	403	544
Stock-based compensation expense	839	604
Unrealized (gain) loss on foreign exchange	26	(80)
Gain on sale of used rental equipment	(8,832)	(2,195)
Deferred income taxes	630	752
Bad debt expense	738	124
Changes in other operating assets and liabilities:		
Accounts receivable	1,158	671
Prepaid expenses and other assets	(1,132)	(27)
Net investment in sales-type and direct financing leases	16,442	-
Accounts payable, accrued expenses and other liabilities	(3,580)	(6,288)
	(1,940)	(1,458)

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Due to container investors		
Unearned revenue	(2,038)	(362)
Net cash provided by operating activities	54,329	39,247
Cash flows from investing activities		
Purchase of rental equipment	(141,212)	(112,763)
Proceeds from sale of used rental equipment	180,331	9,671
Purchase of furniture, fixtures and equipment	(50)	(58)
Receipt of principal payments from sales-type and direct financing leases	-	8,336
Net cash provided by (used in) investing activities	39,069	(94,814)
Cash flows from financing activities		
Proceeds from debt	306,582	477,600
Principal payments on debt	(382,847)	(441,884)
Debt issuance costs	(419)	(3,485)
Proceeds from issuance of common and preferred stock	-	42,076
Repurchase of common stock	(13,946)	-
Dividends paid to preferred stockholders	(2,207)	-
Exercise of stock options	107	24
Net cash (used in) provided by financing activities	(92,730)	74,331
Effect on cash of foreign currency translation	238	98
Net increase in cash and restricted cash	906	18,862
Cash and restricted cash at beginning of the period (1)	75,983	47,209
Cash and restricted cash at end of the period (2)	\$ 76,889	\$ 66,071

Supplemental disclosure of cash flow

information

Cash paid during the
period for:

Income taxes	\$	91	\$	174
Interest		22,544		16,654

Supplemental disclosure
of non-cash investing
and financing activity

Transfer of rental equipment to direct finance lease	\$	8,349	\$	15,956
Rental equipment payable		56,221		133,714

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- (1) Includes cash of \$20,104 and \$14,735, cash held by variable interest entities of \$25,211 and \$20,685, and restricted cash of \$30,668 and \$11,789 at December 31, 2018 and 2017, respectively.
- (2) Includes cash of \$20,128 and \$21,564, cash held by variable interest entities of \$27,058 and \$22,765, and restricted cash of \$29,703 and \$21,742 at March 31, 2019 and 2018, respectively.

See accompanying notes to unaudited consolidated financial statements.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(1) The Company and Nature of Operations

Organization

CAI International, Inc., together with its subsidiaries (collectively, CAI or the Company), is a transportation finance and logistics company. The Company purchases equipment, primarily intermodal shipping containers and railcars, which it leases to its customers. The Company also manages equipment for third-party investors. In operating its fleet, the Company leases, re-leases and disposes of equipment and contracts for the repair, repositioning and storage of equipment. The Company also provides domestic and international logistics services.

The Company's common stock, 8.50% Series A Fixed-to-Floating Rate Cumulative Redeemable Perpetual Stock and 8.50% Series B Fixed-to-Floating Rate Cumulative Redeemable Perpetual Stock are traded on the New York Stock Exchange under the symbols "CAI," "CAI-PA" and "CAI-PB," respectively. The Company's corporate headquarters are located in San Francisco, California.

Basis of Presentation

The accompanying unaudited consolidated financial statements include the financial statements of CAI International, Inc. and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

In the opinion of management, the accompanying unaudited consolidated financial statements contain all normal, recurring adjustments necessary to present fairly the Company's financial position as of March 31, 2019 and December 31, 2018, the Company's results of operations for the three months ended March 31, 2019 and 2018, and the Company's cash flows for the three months ended March 31, 2019 and 2018. The results of operations and cash flows for the periods presented are not necessarily indicative of the results of operations or cash flows which may be reported for the remainder of 2019 or in any future period. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) have been condensed or omitted. The accompanying unaudited interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto for the year ended December 31, 2018, included in the Company's Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on March 5, 2019.

(2) Accounting Policies and Recent Accounting Pronouncements

Recent Accounting Pronouncements

In February 2016, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2016-02, Leases (Topic 842) (ASU 2016-02), and subsequently issued amendments thereto, that replaced existing

lease accounting guidance. The new standard requires lessors to classify leases as a sales-type, direct financing, or operating lease. A lease is a sales-type lease if any of five criteria are met, each of which indicate that the lease, in effect, transfers control of the underlying asset to the lessee. If none of those five criteria are met, but two additional criteria are both met, indicating that the lessor has transferred substantially all of the risks and benefits of the underlying asset to the lessee and a third-party, the lease is a direct financing lease. All leases that are not sales-type or direct financing leases are operating leases. The new standard also established a right-of-use model (ROU) that requires lessees to recognize an ROU asset and lease liability on the balance sheet for all leases with a term longer than twelve months.

The Company adopted ASU 2016-02, as amended, effective January 1, 2019, using the modified retrospective approach and the effective date as the date of initial application. Consequently, financial information will not be updated and the disclosures required under the new standard will not be provided for dates and periods before January 1, 2019. In addition, the Company elected the following practical expedients permitted under the transition guidance within the new standard: (1) the “package of practical expedients,” which does not require the Company to reassess under the new standard its prior conclusions about lease identification, lease classification, and initial direct costs, (2) the short-term lease recognition exemption for its office space leases of twelve months or less, which resulted in the Company not recognizing an ROU asset or lease liability for these leases, and (3) the practical expedient to not separate lease and non-lease components for leases that qualify for the practical expedient.

Adoption of the new standard resulted in the recognition of operating lease ROU assets of \$3.7 million and operating lease liabilities of \$4.1 million as of January 1, 2019. Adoption did not have an impact on the Company’s consolidated statements of income or cash flows.

Except as described above, there were no changes to the Company’s accounting policies during the three months ended March 31, 2019. See Note 2 to the audited consolidated financial statements in the Company’s Annual Report on Form 10-K for the year ended December 31, 2018, filed with the SEC on March 5, 2019, for a description of the Company’s significant accounting policies.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Accounting Policies

(a) Container and Rail Lease Revenue

The Company recognizes revenue from operating leases of its equipment as earned over the term of the lease. Where minimum lease payments vary over the lease term, revenue is recognized on a straight-line basis over the term of the lease. The Company recognizes revenue on a cash basis for certain railcar leases that are billed on an hourly or mileage basis through a third-party railcar manager. Early termination of the rental contracts subjects the lessee to a penalty, which is included in lease revenue upon such termination. Sales-type and finance lease income is recognized using the effective interest method, which generates a constant rate of interest over the period of the lease.

Certain leases include one or more options to renew or purchase the leased rental equipment. The exercise of lease renewal or equipment purchase options is at the sole discretion of the customer.

Included in lease revenue is revenue consisting primarily of fees charged to the lessee for handling, delivery, and repairs. These activities are considered non-lease components of the contract, which are generally accounted for separately from the lease component, and revenue is recognized as earned in accordance with Accounting Standards Codification (ASC) Topic 606, Revenue Recognition. For certain leases of railcar equipment, the Company is responsible for the repair and maintenance of the railcars throughout the lease term. For such leases, the lease and non-lease component are combined as a single lease component, and revenue is recognized as earned in accordance with ASC Topic 842, Leases.

Also included in lease revenue is revenue from management fees earned under equipment management agreements. Management fees are generally calculated as a percentage of the monthly net operating income for an investor's portfolio and recognized as revenue in the month of service.

(b) Leases

The Company leases office space under operating leases with expiration dates through 2024. The Company determines whether an arrangement constitutes a lease and records lease liabilities and ROU assets on its consolidated balance sheets at lease commencement. Operating leases under ASC 842 are included in operating lease right-of-use assets, accrued expenses and other current liabilities, and operating lease liabilities in the Company's consolidated balance sheets.

Operating lease ROU assets and liabilities are recognized at commencement date based on the present value of lease payments over the lease term. As most of the Company's leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. The operating lease ROU assets also include any lease pre-payments made and exclude lease incentives. Certain of the Company's leases include one or more options to renew, which are included in the lease term only when it is reasonably certain that the Company will exercise that option. The Company's office space leases often include lease and non-lease components, which are combined and accounted for as a single lease component.

For short-term leases, the Company records rent expense in its consolidated statements of income on a straight-line basis over the lease term and records variable lease payments as incurred.

(3) Consolidation of Variable Interest Entities

The Company regularly performs a review of its container fund arrangements with investors to determine whether or not it has a variable interest in the fund and if the fund is a variable interest entity (VIE). If it is determined that the Company does not have a variable interest in the fund, further analysis is not required and the Company does not consolidate the fund. If it is determined that the Company does have a variable interest in the fund and the fund is a VIE, a further analysis is performed to determine if the Company is a primary beneficiary of the VIE and meets both of the following criteria under FASB ASC Topic 810, Consolidation:

- it has power to direct the activities of a VIE that most significantly impact the VIE's economic performance; and
- it has the obligation to absorb losses of the VIE that could be potentially significant to the VIE or the right to receive benefits from the VIE that could potentially be significant to the VIE.

If in the Company's judgment both of the above criteria are met, the VIE's financial statements are included in the Company's consolidated financial statements as required under FASB ASC Topic 810, Consolidation.

The Company currently enters into two types of container fund arrangements with investors which are reviewed under FASB ASC Topic 810, Consolidation. These arrangements include container funds that the Company manages for investors and container funds that have entered into financing arrangements with investors. All of the funds under financing arrangements are Japanese container funds that were established under separate investment agreements allowed under Japanese commercial laws. Each of the funds is financed by unrelated Japanese third-party investors.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Managed Container Funds

The fees earned by the Company for arranging, managing and establishing container funds are commensurate with the level of effort required to provide those services, and the arrangements include only terms and conditions that are customarily present in arrangements for similar services. As such, the Company does not have a variable interest in the managed containers funds, and does not consolidate those funds. No container portfolios were sold to the funds during the three months ended March 31, 2019 and 2018.

Collateralized Financing Obligations

The Company has transferred containers to Japanese investor funds while concurrently entering into lease agreements for the same containers, under which the Company leases the containers back from the Japanese investors. The Company concluded these were financing transactions under which sale-leaseback accounting was not applicable.

The terms of the transactions with container funds under financing arrangements include options for the Company to purchase the containers from the funds at a fixed price. As a result of the residual interest resulting from the fixed price call option, the Company concluded that it may absorb a significant amount of the variability associated with the funds' anticipated economic performance and, as a result, the Company has a variable interest in the funds. The funds are considered VIEs under FASB ASC Topic 810, Consolidation, because, as lessee of the funds, the Company has the power to direct the activities that most significantly impact each entity's economic performance, including the leasing and managing of containers owned by the funds. As the Company has the power to direct the activities that most significantly impact the economic performance of the VIEs and the variable interest provides the Company with the right to receive benefits from the entity that could potentially be significant to the funds, the Company determined that it is the primary beneficiary of these VIEs and included the VIEs' assets and liabilities as of March 31, 2019 and December 31, 2018, and the results of the VIEs' operations and cash flows for the three months ended March 31, 2019 and 2018, in the Company's consolidated financial statements.

The containers that were transferred to the Japanese investor funds had a net book value of \$139.8 million as of March 31, 2019. The container equipment, together with \$27.1 million of cash held by the investor funds that can only be used to settle the liabilities of the VIEs, has been included on the Company's consolidated balance sheets with the related liability presented in the debt section of the Company's consolidated balance sheets as collateralized financing obligations of \$124.2 million and term loans held by VIE of \$41.3 million. No gain or loss was recognized by the Company on the initial consolidation of the VIEs. Containers sold to the Japanese investor funds during the three months ended March 31, 2019 and 2018, had a net book value of \$65.0 million and \$7.9 million, respectively.

(4) Rental Equipment

The following table provides a summary of the Company's rental equipment (in thousands):

	March 31, 2019	December 31, 2018
Dry containers	\$ 1,885,018	\$ 1,840,304
Refrigerated containers	340,495	341,983
Other specialized equipment	206,282	192,035
Railcars	358,419	490,381
	2,790,214	2,864,703
Accumulated depreciation	(613,838)	(599,443)
Rental equipment, net of accumulated depreciation	\$ 2,176,376	\$ 2,265,260

On February 26, 2019, the Company entered into an agreement to sell 2,146 railcars. The sale of 1,946 railcars for consideration of \$165.3 million was completed in February 2019, which resulted in a \$7.0 million gain on sale of rental equipment. The sale of the remaining 200 railcars is expected to complete in the second quarter of 2019.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(5) Net Investment in Sales-Type and Direct Finance Leases

The following table represents the components of the Company's net investment in sales-type and direct finance leases (in thousands):

	March 31, 2019	December 31, 2018
Gross sales-type and finance lease receivables (1)	\$ 785,149	\$ 804,511
Unearned income (2)	(245,213)	(254,744)
Net investment in sales-type and direct finance leases	\$ 539,936	\$ 549,767

(1) At the inception of the lease, the Company records the total minimum lease payments, executory costs, if any, and unguaranteed residual value as gross sales-type and finance lease receivables. The gross sales-type and finance lease receivables are reduced as customer payments are received. There was \$74.4 million unguaranteed residual value at March 31, 2019 and December 31, 2018, included in gross sales-type and finance lease receivables. There were no executory costs included in gross sales-type and finance lease receivables as of March 31, 2019 and December 31, 2018.

(2) The difference between the gross sales-type and finance lease receivables and the cost of the equipment or carrying amount at the lease inception is recorded as unearned income. Unearned income, together with initial direct costs, are amortized to income over the lease term so as to produce a constant periodic rate of return. There were no unamortized initial direct costs as of March 31, 2019 and December 31, 2018.

In order to estimate the allowance for losses contained in gross sales-type and finance lease receivables, the Company reviews the credit worthiness of its customers on an ongoing basis. The review includes monitoring credit quality indicators, the aging of customer receivables and general economic conditions.

The categories of gross finance lease receivables based on the Company's internal customer credit ratings can be described as follows:

Tier 1— These customers are typically large international shipping lines that have been in business for many years and have world-class operating capabilities and significant financial resources. In most cases, the Company has had a long commercial relationship with these customers and currently maintains regular communication with them at several levels of management, which provides the Company with insight into the customer's current operating and financial performance. In the Company's view, these customers have the greatest ability to withstand cyclical down turns and would likely have greater access to needed capital than lower-rated customers. The Company views the risk of default for Tier 1 customers to range from minimal to moderate.

Tier 2— These customers are typically either smaller shipping lines or freight forwarders with less operating scale or with a high degree of financial leverage, and accordingly the Company views these customers as subject to higher volatility in financial performance over the business cycle. The Company generally expects these customers to have less access to capital markets or other sources of financing during cyclical down turns. The Company views the risk of default for Tier 2 customers as moderate.

Tier 3— Customers in this category exhibit volatility in payments on a regular basis.

Based on the above categories, the Company's gross sales-type and finance lease receivables were as follows (in thousands):

	March 31, 2019	December 31, 2018
Tier 1	\$ 677,220	\$ 698,014
Tier 2	107,929	106,497
Tier 3	-	-
	\$ 785,149	\$ 804,511

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

Contractual maturities of the Company's gross sales-type and finance lease receivables subsequent to March 31, 2019 for the years ending March 31 are as follows (in thousands):

2020	\$ 115,179
2021	91,343
2022	83,364
2023	77,814
2024	69,955
2025 and thereafter	347,494
	\$ 785,149

(6) Intangible Assets

The Company amortizes intangible assets on a straight line-basis over their estimated useful lives as follows:

Trademarks and tradenames	2-3 years
Customer relationships	5-8 years

The Company's intangible assets as of March 31, 2019 and December 31, 2018 were as follows (in thousands):

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	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
March 31, 2019			
Trademarks and tradenames	\$ 1,786	\$ (1,786)	\$ -
Customer relationships	9,344	(4,013)	5,331
	\$ 11,130	\$ (5,799)	\$ 5,331
December 31, 2018			
Trademarks and tradenames	\$ 1,786	\$ (1,786)	\$ -
Customer relationships	9,344	(3,611)	5,733
	\$ 11,130	\$ (5,397)	\$ 5,733

Amortization expense was \$0.4 million and \$0.5 million for the three months ended March 31, 2019 and 2018, respectively, and was included in administrative expenses in the consolidated statements of income.

As of March 31, 2019, estimated future amortization expenses are as follows (in thousands):

2020	\$ 1,609
2021	1,609
2022	1,232
2023	474
2024	407
	\$ 5,331

(7) Leases

Lessee

The Company has entered into various non-cancelable office space leases with original lease periods expiring between 2019 and 2024. The components of lease expense for the three months ended March 31, 2019 were as follows (in thousands):

Operating lease cost	\$ 600
Short-term lease cost	15
Variable lease cost	73
Total lease cost	\$ 688

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The weighted-average remaining term of the Company's operating leases was 3.2 years and the weighted-average discount rate used to measure the present value of the Company's operating lease liabilities was 4.2% as of March 31, 2019.

Maturities of the Company's operating lease liabilities, which do not include short-term leases, as of March 31, 2019 were as follows (in thousands):

2020	\$ 1,722
2021	727
2022	590
2023	452
2024	304
2025 and thereafter	26
Total lease payments	3,821
Less imputed interest	(248)
Total operating lease liabilities	\$ 3,573

Current operating lease liabilities of \$1.6 million were recorded in accrued expenses and other current liabilities on the Company's consolidated balance sheet as of March 31, 2019.

Cash payments included in the measurement of the Company's operating lease liabilities were \$0.6 million for the three months ended March 31, 2019.

As of March 31, 2019, the Company has \$5.6 million of undiscounted future payments under an additional operating lease that has not yet commenced, which is excluded from the table above. This operating lease will commence on October 1, 2019 with a lease term of 3.0 years.

Lessor

The Company leases its rental equipment on either short-term operating leases through master lease agreements, long-term non-cancelable operating leases, or finance leases. The components of lease revenue for the three months ended March 31, 2019 were as follows (in thousands):

Lease revenue - sales-type and direct financing leases	
Profit at lease commencement	\$ -
Interest income on lease receivable	11,390
	11,390
Lease revenue - operating leases	69,197
Variable lease revenue	2,805
Total lease revenue	\$ 83,392

The following represents future minimum rents receivable under long-term non-cancelable operating leases (in thousands):

	As of March 31, 2019
2020	\$ 138,561
2021	158,232
2022	135,738
2023	111,605
2024	72,494
2025 and thereafter	113,896
Total	\$ 730,526

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

	As of December 31, 2018
2019	\$ 184,978
2020	152,927
2021	129,361
2022	107,776
2023	71,762
2024 and thereafter	108,714
Total	\$ 755,518

See Note 5 for contractual maturities of the Company's gross sales-type and finance lease receivables.

(8) Debt

Details of the Company's debt as of March 31, 2019 and December 31, 2018 were as follows (dollars in thousands):

	March 31, 2019		Average Interest	December 31, 2018		Average Interest	Maturity
	Outstanding Current	Long-term		Outstanding Current	Long-term		
Revolving credit	\$ 7,000	\$ 288,000	4.2%	\$ 4,200	\$ 301,000	4.2%	June 2023
Revolving credit facility - Rail	-	193,500	4.2%	-	272,500	4.2%	October 2023
Revolving credit facility - Euro	-	19,074	2.0%	-	19,457	2.0%	September 2020
Term loan	1,800	26,850	4.7%	1,800	27,300	4.5%	April 2023
Term loan	109,500	-	4.1%	111,750	-	3.8%	October 2019
Term loan	7,000	73,750	4.3%	7,000	75,500	4.0%	June 2021

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Term loan	1,251	14,967	3.4%	1,240	15,284	3.4%	December 2020
Term loan	2,935	39,907	3.6%	2,909	40,651	3.6%	August 2021
Term loan	6,000	91,000	4.6%	6,000	92,500	4.6%	October 2023
Senior secured notes	6,110	49,720	4.9%	6,110	52,775	4.9%	September 2022
Asset-backed notes 2012-1	17,100	44,175	3.5%	17,100	48,450	3.5%	October 2027
Asset-backed notes 2013-1	22,900	68,700	3.4%	22,900	74,425	3.4%	March 2028
Asset-backed notes 2017-1	25,307	183,476	3.7%	25,307	189,802	3.7%	June 2042
Asset-backed notes 2018-1	34,890	276,213	4.0%	34,890	284,935	4.0%	February 2043
Asset-backed notes 2018-2	34,350	291,975	4.4%	34,350	300,563	4.4%	September 2043
Collateralized financing obligations	41,740	82,430	1.5%	39,610	67,615	1.2%	December 2021
Term loans held by VIE	6,076	35,195	4.1%	1,456	-	3.3%	June 2019
	323,959	1,778,932		316,622	1,862,757		
Debt issuance costs	(5,295)	(14,237)		(5,241)	(15,124)		
Total Debt	\$ 318,664	\$ 1,764,695		\$ 311,381	\$ 1,847,633		

The Company maintains its revolving credit facilities to finance the acquisition of rental equipment and for general working capital purposes. As of March 31, 2019, the Company had \$1,170.3 million in total availability under its revolving credit facilities (net of \$0.1 million in letters of credit), subject to the Company's ability to meet the collateral requirements under the agreements governing the facilities. Based on the borrowing base and collateral requirements at March 31, 2019, the borrowing availability under the Company's revolving credit facilities was \$140.4 million, assuming no additional contributions of assets.

On March 29, 2019, one of the Japanese investor funds that is consolidated by the Company as a VIE (see Note 3) entered into a term loan agreement with a bank. Under the terms of the term loan agreement, the Japanese investor fund entered into a seven-year, amortizing term loan of \$40.8 million at a fixed interest rate of 4.2%. The term loan is secured by assets of the Japanese investor fund, and is subject to certain borrowing conditions set out in the term loan agreement.

The agreements relating to all of the Company's debt contain various financial and other covenants. As of March 31, 2019, the Company was in compliance with all of its financial and other covenants.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

For further information on the Company's debt instruments, see Note 8 to the consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2018, filed with the SEC on March 5, 2019.

(9) Stock-Based Compensation Plan

Stock Options

The Company may grant stock options from time to time to certain employees and independent directors pursuant to its 2007 Equity Incentive Plan, as amended (Plan). Under the Plan, a maximum of 3,421,980 share awards may be granted.

Stock options granted to employees have a vesting period of four years from the grant date, with 25% vesting after one year, and 1/48th vesting each month thereafter until fully vested. Stock options granted to independent directors vest in one year. All of the stock options have a contractual term of ten years.

The following table summarizes the Company's stock option activities for the three months ended March 31, 2019 and 2018:

	Three Months Ended March 31,			
	2019		2018	
	Number of	Weighted	Number of	Weighted
	Shares	Average	Shares	Average
		Exercise		Exercise
		Price		Price
Options outstanding at January 1	850,167	\$ 16.46	859,560	\$ 16.44
Options exercised	(46,917)	\$ 14.04	(1,893)	\$ 12.64
Options outstanding at March 31	803,250	\$ 16.60	857,667	\$ 16.45
Options exercisable	642,762	\$ 17.47	521,021	\$ 17.56

Weighted average remaining term	5.5 years	6.1 years
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The aggregate intrinsic value of stock options exercised during the three months ended March 31, 2019 and 2018 was \$0.5 million and less than \$0.1 million, respectively. The aggregate intrinsic value of all options outstanding as of March 31, 2019 was \$5.5 million based on the closing price of the Company's common stock of \$23.20 per share on March 29, 2019, the last trading day of the quarter.

The Company recognized stock-based compensation expense relating to stock options of \$0.2 million and \$0.4 million for the three months ended March 31, 2019 and 2018, respectively. As of March 31, 2019, the remaining unamortized stock-based compensation cost relating to stock options granted to the Company's employees and independent directors was approximately \$1.0 million, which is to be recognized over the remaining weighted average vesting period of approximately 1.5 years.

The Company did not grant any stock options during the three months ended March 31, 2019 and 2018.

Restricted Stock and Performance Stock

The Company grants restricted stock units and restricted stock awards from time to time to certain employees and independent directors pursuant to the Plan. Restricted stock granted to employees has a vesting period of four years; 25% vesting on each anniversary of the grant date. Restricted stock granted to independent directors vests in one year. The Company recognizes the compensation cost associated with restricted stock over the vesting period based on the closing price of the Company's common stock on the date of grant.

The Company grants performance stock to selected executives and other key employees. The performance stock vests at the end of a 3-year performance cycle if certain financial performance targets are met. The Company recognizes compensation cost associated with the performance stock ratably over the 3-year term when it is considered probable that performance targets will be met. Compensation cost is based on the closing price of the Company's common stock on the date of grant.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

The following table summarizes the activity of restricted stock and performance stock under the Plan:

	Number of	Weighted Average Grant Date Fair Value
	Shares	
Outstanding at December 31, 2018	204,730	\$ 20.45
Granted	131,494	\$ 25.67
Vested	(26,594)	\$ 20.30
Outstanding at March 31, 2019	309,630	\$ 22.68

The Company recognized stock-based compensation expense relating to restricted stock and performance stock awards of \$0.6 million and \$0.2 million for the three months ended March 31, 2019 and 2018, respectively. As of March 31, 2019, unamortized stock-based compensation expense relating to restricted stock and performance stock was \$5.5 million, which will be recognized over the remaining average vesting period of 2.4 years.

Stock-based compensation expense is recorded as a component of administrative expenses in the Company's consolidated statements of income with a corresponding credit to additional paid-in capital in the Company's consolidated balance sheets.

(10) Income Taxes

The consolidated income tax expense for the three months ended March 31, 2019 and 2018, was determined based upon estimates of the Company's consolidated annual effective income tax rate for the years ending December 31, 2019 and 2018, respectively. The difference between the consolidated annual effective income tax rate and the U.S. federal statutory rate is primarily attributable to foreign income taxes, state income taxes and the effect of certain permanent differences.

The Company's estimated effective tax rate was 8.2% at March 31, 2019, compared to 4.0% at March 31, 2018.

The Company accounts for uncertain tax positions based on an evaluation as to whether it is more likely than not that a position will be sustained on audit, including resolution of any related appeals or litigation processes. This evaluation is based on all available evidence and assumes that the appropriate tax authorities have full knowledge of

all relevant information concerning the tax position. Once it has been determined that a tax position is more likely than not to be sustained on its technical merits, the tax benefit recognized is based on the largest amount that is greater than 50% likely of being realized upon ultimate settlement. As of March 31, 2019, the Company had unrecognized tax benefits of \$0.3 million, which if recognized, would reduce the Company's effective tax rate. Total accrued interest relating to unrecognized tax benefits was less than \$0.1 million as of March 31, 2019. The Company does not believe the total amount of unrecognized tax benefits as of March 31, 2019 will change for the remainder of 2019.

(11) Fair Value of Financial Instruments

The carrying amounts of cash, restricted cash, accounts receivable and accounts payable reflected in the balance sheets as of March 31, 2019 and December 31, 2018, approximate their fair value due to the short-term nature of these financial assets and liabilities. The carrying value of variable rate debt in the balance sheets as of March 31, 2019 and December 31, 2018 approximates fair value as the changes in their associated interest rates reflect the current market and credit risk is similar to when the loans were originally obtained.

The principal balance of the Company's asset-backed notes and collateralized financing obligations was \$999.1 million and \$124.2 million as of March 31, 2019, with a fair value of approximately \$991.7 million and \$125.8 million, respectively, based on the fair value of estimated future payments calculated using prevailing interest rates. The fair value of these financial instruments would be categorized as Level 2 in the fair value hierarchy. The principal balance of the Company's asset-backed notes and collateralized financing obligations was \$1,032.7 million and \$107.2 million as of December 31, 2018, with a fair value of approximately \$1,024.7 million and \$108.9 million, respectively. Management believes that the balances of the Company's fixed-rate term loans of \$156.1 million and \$158.6 million, senior secured notes of \$55.8 million and \$58.9 million, and term loans held by VIE of \$41.3 million and \$1.5 million as of March 31, 2019 and December 31, 2018, respectively, approximate their fair values. The fair value of these financial instruments would be categorized as Level 2 in the fair value hierarchy.

(12) Commitments and Contingencies

In addition to its debt obligations described in Note 8 above, the Company had commitments to purchase approximately \$53.9 million of containers and \$27.3 million of railcars as of March 31, 2019, all in the twelve months ending March 31, 2020.

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CAI INTERNATIONAL, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

(13) Stockholders' Equity

Stock Repurchase Plan

In October 2018, the Company announced that the Board of Directors approved the repurchase of up to three million shares of its outstanding common stock. The number, price, structure and timing of the repurchases, if any, will be at the Company's sole discretion and will be evaluated by the Company depending on prevailing market conditions, corporate needs, and other factors. The stock repurchases may be made in the open market, block trades or privately negotiated transactions. This stock repurchase program replaces any available prior share repurchase authorization and may be discontinued at any time. In the first quarter of 2019, the Company repurchased 0.6 million shares of its common stock under this repurchase plan, at a cost of approximately \$13.9 million. As of March 31, 2019, approximately 1.9 million shares remained available for repurchase under this share repurchase program.

Common Stock At-the-Market (ATM) Offering Program

In October 2017, the Company commenced an ATM offering program with respect to its common stock, which allows the Company to issue and sell up to 2.0 million shares of its common stock. The Company did not issue any shares under this ATM offering program during the three months ended March 31, 2019. The Company has remaining capacity to issue and sell up to approximately 1.0 million of additional shares of common stock under this ATM offering program.

Series A Preferred Stock Underwritten Offering

In March 2018, the Company completed an underwritten public offering of 1,600,000 shares of its 8.5% Series A Fixed-to-Floating Rate Cumulative Redeemable Perpetual Preferred Stock, par value \$0.0001 per share and liquidation preference \$25.00 per share (Series A Preferred Stock), resulting in net proceeds to the Company of approximately \$38.3 million, after deducting the underwriting discount and other offering expenses. In April 2018, the Company sold an additional 170,900 shares of Series A Preferred Stock upon the partial exercise by the underwriters of their option to purchase additional Series A Preferred Stock, resulting in net proceeds to the Company of approximately \$4.1 million, after deducting the underwriting discount of \$0.1 million. The net proceeds were used for repayment of debt and general corporate purposes.

Series A Preferred Stock ATM Offering Program

In May 2018, the Company commenced an ATM offering program with respect to its Series A Preferred Stock, which allows the Company to issue and sell up to 2.2 million shares of its Series A Preferred Stock. The Company did not issue any shares under this ATM offering program during the three months ended March 31, 2019. The Company has remaining capacity to issue and sell up to approximately 1.8 million of additional shares of Series A Preferred Stock under this ATM offering program.

Series B Preferred Stock Underwritten Offering

In August 2018, the Company completed an underwritten public offering of 1,700,000 shares of its 8.5% Series B Fixed-to-Floating Rate Cumulative Redeemable Perpetual Preferred Stock, par value \$0.0001 per share and liquidation preference \$25.00 per share (Series B Preferred Stock), resulting in net proceeds to the Company of approximately \$41.2 million, after deducting the underwriting discount. The Company sold an additional 255,000 shares of Series B Preferred Stock upon the exercise by the underwriters of their option to purchase additional Series B Preferred Stock, resulting in net proceeds to the Company of approximately \$6.2 million, after deducting the underwriting discount of \$0.2 million. The net proceeds were used for repayment of debt and general corporate purposes.

For further information on the Company's shareholders' equity, see Note 14 to the consolidated financial statements in the Company's Annual Report on Form 10-K for the year ended December 31, 2018, filed with the SEC on March 5, 2019.

(14) Segment and Geographic Information

The Company organizes itself by the nature of the services it provides which includes equipment leasing (consisting of container leasing and rail leasing) and logistics.

The container leasing segment is aggregated with equipment management and derives its revenue from the ownership and leasing of containers and fees earned for managing container portfolios on behalf of third-party investors. The rail leasing segment derives its revenue from the ownership and leasing of railcars. The logistics segment derives its revenue from the provision of logistics services. There are no material inter-segment revenues.

With the exception of administrative expenses, operating expenses are directly attributable to each segment. Administrative expenses that are not directly attributable to a segment are allocated to the segments based upon relative asset values or revenue.

The following tables show condensed segment information for the three months ended March 31, 2019 and 2018, reconciled to the Company's income before income taxes as shown in its consolidated statements of income for such periods (in thousands):

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NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)

	Three Months Ended March 31, 2019			
	Container	Rail		
	Leasing	Leasing	Logistics	Total
Total revenue	\$ 75,511	\$ 7,881	\$ 27,716	\$ 111,108
Total operating expenses	38,409	(1,212)	29,790	66,987
Operating income (loss)	37,102	9,093	(2,074)	44,121
Net interest and other expenses (income)	19,947	3,945	(4)	23,888
Income (loss) before income taxes	\$ 17,155	\$ 5,148	\$ (2,070)	\$ 20,233
Goodwill	\$ -	\$ -	\$ 15,794	\$ 15,794
Total assets	\$ 2,534,976	\$ 337,406	\$ 45,533	\$ 2,917,915
Purchase of rental equipment (1)	\$ 108,090	\$ 33,122	\$ -	\$ 141,212

	Three Months Ended March 31, 2018			
	Container	Rail		
	Leasing	Leasing	Logistics	Total
Total revenue	\$ 64,634	\$ 9,104	\$ 21,636	\$ 95,374
Total operating expenses	31,349	6,906	22,403	60,658
Operating income (loss)	33,285	2,198	(767)	34,716
Net interest and other expenses	13,322	3,545	(3)	16,864
Income (loss) before income taxes	\$ 19,963	\$ (1,347)	\$ (764)	\$ 17,852
Goodwill	\$ -	\$ -	\$ 15,794	