

Dear Friends of IEWC, here is my account:

Industry News

Falling down, then climbing back throughout the last four weeks, the Wire Index managed to close perfectly flat from this time last month, closing at 44.5 on the 20th. This weekly-calculated index of publicly traded wire and cable manufacturers and distributors now stands at less than one-third of its peak value recorded in July of 2007. Click on the graph to the right for more information and historical data on the Wire Index.

US Economy

The US economy appears to be in a holding pattern, albeit a slightly downward-facing one. Economic indicators delayed by a month or two reveal continued declines in most sectors, though the rate of descent has slowed, implying a potential bottom to the economic freefall. Sore spots remain in unemployment, industrial production and consumer confidence, but retail sales, housing starts and consumer prices all show signs of improvement. The stimulus bill has passed, the Fed has (and continues to) flood the markets with liquidity, and we've survived a number of months without another crippling financial collapse. Market participants now seem to be waiting for more stable ground on which to build a recovery.

Although determining the timing of the economic bottom is nearly impossible, I still remain optimistic that the stabilization in demand and technical bottom will occur before the end of this year. As commodity prices recover slightly and the Consumer Price Index records two consecutive upticks, it is clear that a deflationary spiral has not taken hold. With prices no longer in decline, potential buyers lose purchase power holding on to their money, encouraging a fresh round of spending. As I explain below, the end of this recession will not necessarily prompt an immediate recovery in the demand for most wire and cable products, but it will mark the beginning of a new growth cycle.

The Fed

The US Federal Reserve Board has been extremely active in the markets throughout the current crisis, creating new "facilities" faster than most anyone can take the time to understand them. As recently as 2007, the Fed listed only Open Market Operations, The Discount Rate and Reserve Requirements in its policy arsenal, the same three tools appearing in economics textbooks for decades. Since the crisis, the Fed has expanded this toolset to include eight additional policy instruments, with an alphabet soup of auction, credit, liquidity, funding and loan facilities.

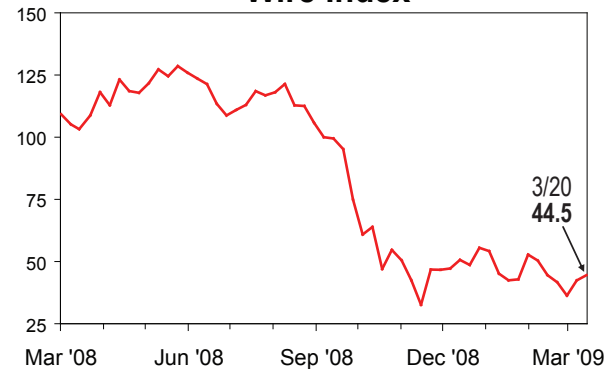
While all of these policy innovations are significant in some way, the Fed launched one of its most noteworthy crisis-fighting programs in its regular press release on March 18th without creating a new acronym. The central bank regularly buys short-term Treasury securities through Open Market Operations as its primary method of shaping the money supply and affecting market interest rates to narrow in on the stated Target Fed Funds Rate. With the latest announcement, however, the Fed will now purchase up to \$300 billion in longer-term Treasury securities. With the deep-pocketed Fed getting into the game, demands for these bonds increase, raising prices and driving down interest rates. By purchasing securities with longer maturity periods, the Fed more directly affects the lending market for longer-term consumer loans used to finance purchases like homes and cars. Lenders regularly calculate a risk premium for loans made to private borrowers, with risk-free Treasury securities as the benchmark. As this benchmark rate drops, the risk premium spread between Treasuries and private loan rates doesn't necessarily change, allowing market rates for mortgages and other consumer loans to fall as well. On the day of the announcement, yields on the 10-year Treasury note declined a full half percentage point, the largest single-day swing since 1987.

This latest Federal Reserve scheme, combined with the joint action to purchase additional billions in mortgage-backed securities, is clearly aimed at improving the housing market. Of course, this spending spree does not come without costs. Requiring a continued expansion of the money supply, these asset purchases increase the threat of inflation in the future. Investors sensed this risk after the Fed's mid-day announcement, sending gold prices up and hammering the dollar. Less tangibly, these actions can also foster a distorted market. US housing prices through the last decade were now clearly inflated, and the supply of homes had grown out of control. The only sustainable way to adjust for these excesses is to allow prices to fall and builders to idle. There is little political support for this hands-off approach, but subsidizing the housing industry again with artificially low rates has the potential to prop up the market before the necessary purging takes place, lending itself to another boom and bust cycle down the road.

Inventories

The timing of the economic recovery in the manufacturing sector will have much to do with inventory levels. Manufacturers, as lean as they have become in the last decade, typically still maintain some level of inventory of both materials and finished goods. Because of this, when new orders arrive, the benefits of increased demand do not cascade down the supply chain until inventory levels are low enough to warrant it. Inventory levels thus have a significant impact on the business cycle, both in severity and duration. Before

Wire Index



BY THE
NUMBERS
(US)

**Industrial
Production**
(Jan to Feb change)

-1.4%

**February
Unemployment**

8.1%

Retail Sales
(Jan to Feb change)

-0.1%

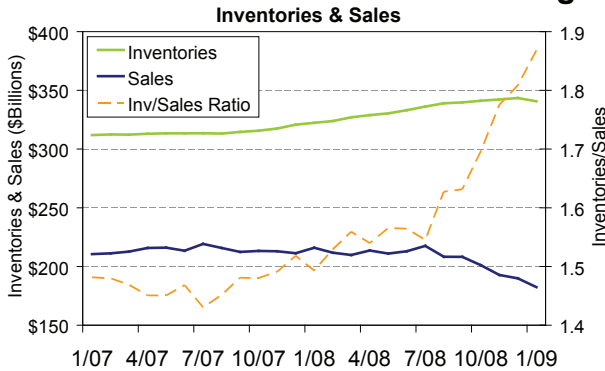
**Mfg.'s New Orders
for Durable Goods**
(Dec to Jan change)

-4.5%

**February
CPI Inflation**
(over prev. 12 months)

0.2%

US Durable Goods Manufacturing



improvements in information technology allowed for more sophisticated and reliable inventory management techniques, fluctuations in inventory even received blame as the catalyst for some recessions. If enough businesses incorrectly forecasted demands and created a glut of inventories, the collective drawdown of stocks became an aggregate contraction in sales, employment and economic activity.

Although the current downturn is very noticeably rooted in the excess inventories of the housing market, inventories of the manufacturing sector have now become a problem as well. Studying only the trends of durable goods manufacturers, as displayed in the chart to the left, inventories were visibly slow to react to the decline in sales that began last summer. As sales fell off and inventory levels continued on with greater inertia, the ratio of monthly inventories to sales climbed from roughly 1.5 to almost 1.9 in January, calculated here as a quotient and a measure directly translated into the number of months inventory on hand at current sales levels. When increased demands for these manufactured goods return and sales pick up, the higher inventory/sales ratio will extend the time before these shipments translate into a noticeable uptick for the suppliers and component manufacturers further upstream. As demands trickle in, manufacturers accustomed to holding 1.5 months of inventory and currently sitting on 2 months will be able to satisfy new orders for a period without cutting new purchase orders of their own.

Breaking these ratios down by sector may give some indication of how quickly demands for wire and cable components will recover in each market once the broader economy turns around. Using the average inventory/sales ratio during 2007 as a benchmark, we gain some measure of the current inventory surplus in each market from the most recent numbers reported for January of this year. As shown in the table to the right, this ratio has grown across the board, with similar increases among manufacturers of equipment, computers, electronics and appliances, significantly higher ratio increases in the aerospace and auto market, and only a mild increase in the inventory/sales ratio for the marine industry. From this, we might presume that the marine industry will respond quicker to the recovery than the appliance and equipment market, the appliance and equipment market faster than the auto and truck sector, and so forth. The only deceiving thing about these industry ratios is the increase shown for the aerospace industry. Where most of these sectors have a 2007 average ratio that is relatively constant from its more historical average, the aerospace industry experienced a declining inventory/sales ratio through much of the last decade. This makes the industry's recent 24% increase in inventory/sales less worrisome as it is arguably only a return to more historically sustainable ratios as high as 5.0.

Manufacturing Sector	2007 Average Inventory/Sales Ratio	January 2009 Inventory/Sales Ratio	% Change
Machinery	1.85	2.15	17%
Computers & Electronics	1.39	1.62	17%
Electronic Equip. & Appliance	1.36	1.61	18%
Aerospace	3.57	4.42	24%
Marine	1.35	1.41	4%
Auto & Truck	0.74	1.03	39%

US/Mexican Trucking

A dangerous wave of protectionism is flaring up along the US-Mexican border. In passing the \$410 billion spending bill this month to fund various cabinet departments and federal agencies, the US also put a stop to the pilot program that allowed approved Mexican trucks to operate on US roads, a program pushed through by the previous administration in the fall of 2007. NAFTA originally promised open trucking between the US, Mexico and Canada by 2000, but safety concerns and a powerful labor lobby caused the US to violate the original agreement, denying Mexican trucks access to US roads. Without open trucking between the US and Mexico, trailers traveling across the border require three different trucks to do the work, increasing transaction costs and raising the prices of goods traded between the two countries.

In retaliation to the US canceling the pilot program, which built a stellar safety record for the Mexican truck carriers involved, Mexico passed new tariffs on 89 US exports. The tariffs mostly affect agricultural products and household goods, with select types of coffee makers and dishwashers the only products on the list likely to contain any wire and cable products. The tariffs appear targeted and largely symbolic, including sunflower seeds, for example, a prize agriculture export of North Dakota, home state of Senator Byron Dorgan who amended the bill to suspend the trucking program. Although this protectionist exchange is mostly political at the moment, this sentiment reflects a dangerous trend. Erecting barriers to trade destroy wealth for both parties involved and risks turning the current recession into an even more depressing state.

Sincerely,

Brian Hirt

Brian Hirt
M.A. Economics
IEWC Business Analyst
BHirt@iewc.com
262-957-1118



Disclaimer: IEWC provided this newsletter and the information herein for your convenience only and does not guarantee the accuracy or completeness of the information. IEWC assumes no responsibility for the use of, or reliance on, the information provided herein and disclaims all liability for any and all damages arising out of the use of, or reliance on, this information.