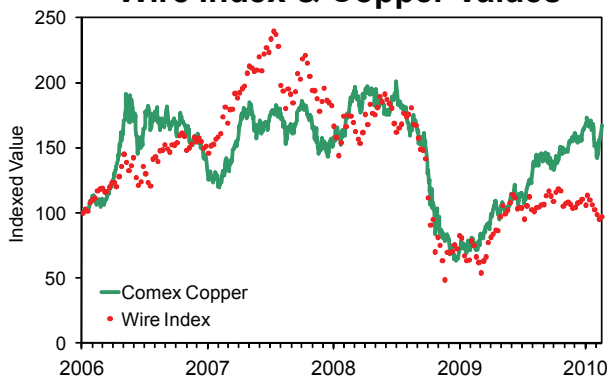


Dear Friends of IEWC, here is my account:

Industry News

The Wire Index recorded a slight decline this month, closing at 65.4 on the 19th. The Index's stagnant performance over the past nine months reveals a divergence worth noting. Historically, the weekly-measured Wire Index exhibited a strong correlation with commodity copper prices. This relationship is not at all surprising, considering that the majority of copper consumed around the world is drawn for wire and cable applications. As current and future demands for copper ebb and flow – as measured in futures prices for the metal – investors extrapolate a similar fate for the wire and cable companies that deal in the metal. As shown in the graph below, this relationship has held true with few exceptions since the beginning of 2006. Surprising then, is the way in which the Wire Index holds flat against a continued rally in copper prices. The recent departure is not explained by overall market trends either. While the Index remains essentially unchanged since May of last year, the S&P 500 enjoyed a 23% increase during the same period. Nor is a single stock in the index to blame. A

Wire Index & Copper Values



couple of the index's lighter weights have grown more in step with the market, but the general trend is underperforming. View the list of Wire Index stocks and historical data [here](#).

The broken link between copper and the Wire Index suggests that either copper is overpriced or the Index undervalued (or some combination of the two). While the sharp recovery in copper prices questions its credibility, it is not an unrealistic rebound given the depth of the decline at the end of 2008. More than anything, copper futures appear to be pricing in the expectation of future demands that have not yet come about. If these expectations prove too optimistic, copper could be pulled back down, but the robust beginnings of the recovery imply that copper traders are rightfully rosy. Considering the sluggish stocks of the Wire Index against the copper boom, there appears to be room for growth. Especially since the Index now lags behind the rest of the stock market, it seems most likely that it is the industry stocks that are more out of touch with reality. As business activity picks up and quarterly earnings statements improve later this year, look for the Wire Index to make up some ground.

US Economy

The economic recovery in the United States continues to strengthen. The 5.7% annualized growth rate recorded in the fourth quarter of last year serves as a precursor of the growth potential for this year. Manufacturing activity, in particular, has picked up this winter. Shipments of manufactured durable goods are up at a 17% annualized rate in the four months ending in December, and the January reading of the Institute for Supply Management's (ISM) Purchasing Managers Index was the strongest since 2004. The ISM also reported slowing supplier deliveries, a byproduct of the new demands in the market. Reflecting the scramble to meet growing customer demands, temporary hirings are also climbing. Bottoming in September of 2009 and adding 52,000 to the January payroll numbers, more temporary help jobs foreshadow a return to permanent employment gains soon. Politicians are getting frantic that the unemployment rate remains so high, but the lag is still typical for this stage of the recovery. Economic output is still much smaller than it was in 2007 before the recession, but the initial trajectory of the recovery points to a quicker rebound than many expected.

The Euro Area

The Euro is a grand experiment in a shared currency. Born conceptually in the early 20th century, hard plans for the currency were not established until 1992 and coins and banknotes for the currency were not circulated until 2002. Though still in its infancy, the currency of the Eurozone (a.k.a. the Euro Area – the 16 nations of the EU that have formally adopted the Euro) has been extremely successful. Recently, however, there are new concerns about the stability of the monetary union against the looming debt crises in the Euro Area's weakest members.

The basis for a shared currency like the Euro is found in the economic theory of an optimum currency area (OCA). An OCA simply defines the geographical region in which a single shared currency would maximize economic efficiency. The US, for example, is generally considered as its own optimum currency area, realized in the common US dollar circulated from Maine to Hawaii. If the federation of states did not represent an OCA, the US might instead establish separate currencies to exchange within the economically diverse East Coast, West Coast and Midwest regions. For anyone who has done much business internationally, the potential benefits of a shared currency are obvious. A single currency eliminates the exchange rate risk of cross-border trading and simplifies the transaction process. When forming international deals, businesses regularly accept a certain level of risk. Significant changes in the foreign exchange market can shift the relative value of revenue streams and cost structures, swinging profits wildly in either direction. Financial markets provide ample methods to hedge this risk with currency swaps and the like, but many of today's small, international businesses aren't sophisticated or large enough to engage with such financial instruments.

BY THE
NUMBERS
(US)

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

+0.9%

**January
Unemployment**

9.7%

Retail Sales
(Dec to Jan change)

+0.5%

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

+1.0%

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

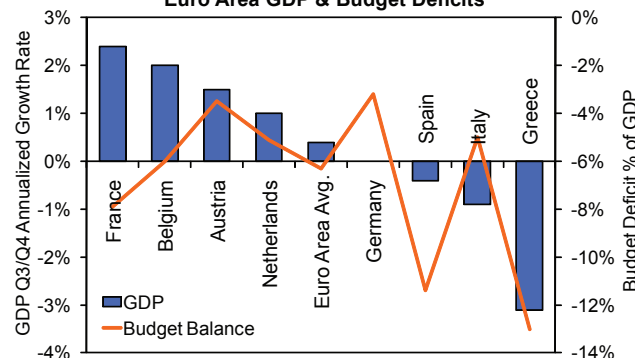
+2.6%

A shared currency also introduces a level of macroeconomic price stability that might not be possible otherwise. With monetary controls consolidated in an institution like the European Central Bank (ECB) in Frankfurt, Germany, there tends to be less meddling with currency values. Separated from the political pressures of any one government and generally unmoved by the economic performance of any single Euro Area country, the ECB focuses its eye almost exclusively on inflation, providing a sound foundation for economic growth for all countries that share the Euro. Substantiating this theory are the benefits to the Euro Area since the introduction of the Euro. A handful of studies on the subject show that trade between Euro Area countries has increased 5-10%, with greater investment and financial integration as well.

In defining an OCA, it is the tendency towards price stability that also limits the geographical region which might effectively share the same currency. In times of economic decline and crisis like we just experienced, central bankers typically swoop in with a flood of extra money and lower interest rates designed to boost lending and keep the gears of the economy turning. With a shared currency, however, central bankers will generally only react when the entire currency zone is under stress, leaving struggling economies on the fringe to their own means of stimulus. A shared currency like the Euro brings about more stability, but ties the hands of policy makers a bit when trouble arises. For this reason, an optimum currency area is usually limited to a group of fairly homogenous countries. In the case of Greece, it is this country's many differences from the Euro Area's stronger members that stresses the currency. As shown in the graph to the right, a snapshot of current GDP growth rates and budget balances for the Euro Area's largest members reveals an uneven balance. Countries like Germany, Austria and the Netherlands have a fairly responsible budget considering the times (though still in deficit), and are pulling out of the recession. Greece and Spain, on the other hand, are still contracting and face budget balances of more than 10% of GDP. The Maastricht Treaty establishing the monetary union included strict criteria for the member countries to attain and maintain fiscal responsibility – designed to prevent just such a scenario – but the measures have largely gone unenforced.

An Uneven Union

Euro Area GDP & Budget Deficits



With Greece and some of the other Euro Area countries in a bind, financial markets are threatened by the risk of sovereign debt defaults. As a last resort in countries with a unique currency (like the US), the government can always print more money to deflate the value of its currency and outstanding debts. For Greece, however, this exit door is barred, making default more likely. There is some chance of a bailout from Germany and the other core member countries, but such response is unpopular and stands counter to the Euro Area's original agreement. The implications of a Greek default on the rest of the world are a bit abstract. There are few direct links between Greek government bonds and finances in the rest of the Western World, but there are significant relationships. If Greece does actually default on its bonds, investors would sense a similar risk for other countries in a budget crisis, including the US. With greater risk in the market, investors would demand higher returns on government bonds, magnifying the financing costs for fiscal stimulus efforts around the world.

While the Euro Area is certainly in a pickle, the net effects on the world economy will likely remain small. In all fairness, the uneven nature of the Euro Area is not all that different from the balance of the fifty United States. With that perspective, the problems of Greece should be no more troubling than those in California. As a silver lining, the fears around Greece could prove to be a healthy scare for the rest of the world. Even if it takes a Greek default to drive the rest of the world towards greater fiscal responsibility, it may prove to be a valuable lesson.

Oil/Gas/Polymers

If nothing else, the oil spike of 2008 desensitized us all to higher crude prices. After falling below \$35/bbl twelve months ago, NYMEX oil futures have crept back up towards \$80 with little fanfare. These higher prices are already translating into higher polymer costs, reflected in Dow Wire & Cable's recent notice of a price increase to go in effect throughout North America on April 1st. Oil closed at \$79.81 on the 19th of this month. NYMEX Natural gas futures fell back this month after a series of spikes since last August, closing at \$5.04/mmBtu on the 19th.

Sincerely,

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