

## Industry Outlook - Round Table

Mr. C. Baker Cunningham

Mr. Paul E. Neuhart

Mr. Yu-Lon Chiao

Mr. Norio Okayama

Dr. Valerio Battista

## Closing Remarks

Mr. Gérard Hauser

Mr. C. Baker Cunningham



### **Mr. Gérard Hauser**

ICF President

Good morning ladies and gentlemen.

The final item on the agenda is the Round Table with members of the ICF Council.

Each member will have the opportunity to share with you some thoughts and ideas about the cable market and challenges faced by the industry.

After the individual presentations, there will be a Q&A session during which I encourage you to raise questions and share with the audience your own views about our business.

It's a pleasure for me to leave now the floor to Mr. Baker Cunningham.

**Mr. C. Baker Cunningham**

President & CEO, Belden CDT Inc. (USA)

It's a pleasure to have the opportunity to comment on the state of our North American markets in a time when things are actually improving.

**State of the U.S. Economy**

Economic activity in the United States grew briskly in the second half of 2003 and the first part of 2004. Growth slowed somewhat in the summer this year, apparently due to consumer concerns about rising gasoline prices. Recently, however, macroeconomic data suggest that the recovery has resumed in the U.S. Nonresidential fixed investment and housing have been growing twice as fast as the overall economy during most of the last 4 quarters, providing some much-needed demand for building wire and industrial products.

The area of greatest concern is high oil prices, which have set records at over \$50/barrel. Petroleum prices, in addition to their direct affect on material costs for us, contributed to a moderately higher U.S. inflation level in the first half of 2004.

**State of the Wire and Cable Industry**

In the North American wire and cable industry, it's been a year of change. There have been several bankruptcies and consolidations. In early 2004, CommScope acquired the Connectivity Solutions business from Avaya. Superior Essex acquired Belden's North American telecom business. And, of course, Belden merged with Cable Design Technologies in mid-July.

A major influence in our industry this year has been the dramatic increase in the cost of raw materials — primarily copper but also plastics of all kinds—not to mention cost increases in freight, health care, and other services.

For the most part the industry has been successful in passing along material cost increases in our pricing in North America, with a lag, varying by market. The lag creates downward pressure on operating margins as copper rises, but may be beneficial later on.

Now, let's look at the various market segments.

**Magnet Wire**

Volume in the magnet wire segment appears to have stabilized and improved slightly in 2004. North American production of magnet wire has declined every year from 2000 through 2003, due to both a weak industrial sector and the tendency for industrial customers to move away from North America to lower labor-cost markets. For this segment to at least hold its ground is reflective of the overall improved level of manufacturing output in the U.S.

**Building Wire**

Demand for building wire has been fairly strong this year, and margins have improved over recent years, due to a number of factors:

the continuing strength of the housing market; some recovery in the commercial market; and consolidation and reduction in industry capacity.

This market experienced a stronger first quarter, probably due to the inclination of the channel to buy ahead of expected further material cost increases.

### **Power Cable**

The power cable market is experiencing a recovery of demand in the range of 8 to 10 percent year over year, adjusted for metals pricing, reflecting increased demand from utilities for primary and secondary distribution cables.

Since the 2003 blackout in the Northeast, the industry still awaits energy legislation in the U.S. that would stimulate improvement in the power grid overall.

### **Communications, Data, and Electronics**

The telecom cable market is experiencing a modest year-over-year improvement in volume in North America, and profitability should benefit from higher utilization after Belden's exit and closing of our large Phoenix, Arizona plant. North American Telecom spending on copper cable remains down nearly 50 percent from the peak of a few years ago. The planned implementation of fiber-to-the-home appears to be moving faster than we originally expected, continuing the pressure on the copper telecom cable business.

The North American data cable market is also enjoying a modest improvement in volume (5% range) while industry-wide material-related price increases are for the most part sticking. There is still a lack of major projects.

Some of our specialty markets—like video, sound and security and some of our industrial niche markets—are showing greater improvement, with double-digit volume improvement year-over-year and pricing which effectively recovers the material cost increases. Manufacturing capital expenditures are now beginning to pick up along with industrial production volume. We also see above-average growth in the market for security applications, such as video surveillance and airport security.

### **Outlook for the Wire and Cable Industry**

In our business outlook, we and other public companies have indicated we believe the third and fourth quarters will continue the trends we saw in the second quarter. That's a plateau, but still a significant level of improvement over the demand of a year ago.

CRU's forecast for growth of both demand and production for North American cable overall is between 9 and 10 percent. That's on a true volume basis, without the effect of pricing. To put that in perspective, however, if we achieve 10 percent recovery in volume we are still far from our peak demand in the years of 1999 and 2000.

### **Outlook for the Economy**

Continued expansion is likely through 2005 and beyond, due to continued stimulus of lower taxes, low interest rates, and government spending on both domestic programs and the war on terrorism. Oil prices are expected to remain high because of high world demand, and this could be a risk to the continued expansion. Thank you.

**Mr. Paul E. Neuhart**

President & COO, OFS (USA)

I'd like to say that the North American optical fiber cable market has returned to health, but that is not exactly the case yet. Although in 2004 we have seen some encouraging signs in North America, the actual unit growth in the telecommunications segment is about 15 to 20%. But in the CATV marketplace, we are only seeing a flat or even declining growth, even though overall the unit volume has grown. The problem still exists that demand is far below capacity, so there is still pricing pressure on the optical fiber and optical fiber cable.

The major catalyst in North America for fiber to the home and fiber to the premises has been Verizon's initiative and SBC has also started to do fiber to the neighborhood or fiber to the node. Additionally, municipalities and the RUS broadband build-out is playing a favorable role. But still one of the key influencers in North America is the FCC and the regulatory environment is playing a role in fiber deployment. The rebundling of the UNEP elements for broadband has helped a lot, but there are still issues such as voice over IP. The TELRIC pricing (total element long run incremental cost) has been changed too, so that it now favors the RBOCs and does not favor companies like ATT, MCI and some of the CLECs (competitive local exchange carrier). I emphasize the regulatory environment, because with the right regulatory environment we believe that what will happen is that Verizon, SBC and Bell South will accelerate their build-outs especially Verizon and SBC. This will put pressure for more bandwidth and some of the CATV companies. So we feel that it will have a very positive effect.

This should translate into double digit growth for several years to come. Fiber in the loop should go from about 10% now to probably 40% single mode fiber in the loop by the year 2009. So the issues for the industry are some of the same as those Baker mentioned, but certainly raw material pricing has become a significant issue and because of the capacity demand imbalance passing on those increases is very difficult. The regulatory environment is key. Of course overall economic growth is important too, because that more than ever has an impact on the demand for bandwidth. For some people in the US bandwidth is a necessity, for others it's a luxury, so the state of the economy plays an important role. Thank you.

**Mr. Yu-Lon Chiao**

Chairman, Walsin Lihwa Corporation (Taiwan)

I would like to comment about the Asian market. This is considered to be one of the best years since 1997 Asian economic crisis. Not only is the Chinese market booming, the Southeast Asian market has recovered and the Japanese market is doing relatively well this year.

My comments will focus on the Chinese market. Last year China's GDP was still growing at the rate of over 9% for the year. This growth was driven by fixed asset investment. Chinese fixed asset investment including new factories, buildings and roads was growing at over 40% per year during the last few years, which has led to a big demand in materials and to power shortage in China. This is why we have seen steel prices and copper prices continue to rise. Since the end of last year China has seen some signs that this overheated economy needs to be cooled down. What China has tried to do as a first step is to emphasize the structure of the economy, by emphasizing that more of the growth should come from the industrial sector or the consumer rather than from fixed asset investment. In order to cool down fixed asset investment, bank loans and land usage land permits for planned construction of new housing are being controlled. Now, after one year there are signs of a slowdown in fixed asset investment, but it still remains at a relatively high level and China's economy is still growing at about 9%.

This means that efforts to cool it down have not yet really had an effect. New measures will probably be taken which could include an increase in interest rates. Also, the minister of finance could loosen control on the currency exchange rate, because any sign changes which might affect the economy in general could be a more effective way to cool down the economy. I think this is quite important, because China is facing inflation, over-investment in some sectors and a serious pollution problem, which might lead to a banking crisis like in Japan, if the economy is not adjusted sooner.

In the short term, this fixed asset investment has had a very positive effect on our cable business. In our experience with cable in the power sector, we have had one of our best years and for the first time we have seen some balance in cable manufacturing between supply and demand. This is the first year total tonnage of Chinese cable output exceeded that of the United States which is about 2.3 million tons. In power cables, XLPE medium high voltage make in the order of 760,000 tons, magnet wires come to approximately 600,000 tons and building wire to about 500,000 tons. Usually in the developed countries, the building wire makes up the most important usage of power cables. If you look at the building expansion in China the tonnage of building wire is relatively low. That means that per square meter, the use of power wire is relatively low. This means that a lot of this investment in buildings is taking place in the countryside. This relationship may change in the next years.

As far as power shortage goes, this year in China was about 45 million kilowatts. They need to invest in 120 million kilowatts in the next three years in order to balance this power demand. 75% of this power comes from coal plants and only 5% from nuclear plant. That means that the mix in power generation needs to be changed in the next decade and new sources of power must be introduced. Looking at investment in the power sector in the next years will also include upgrade of the network. This means that the biggest demand for power cable will come in the next few years.

Looking at the market in China during the last few years, I have always been very positive. The problem in that market has always been on the supply side. The

other main problem in China is the number of players. If the market is now balanced, hundreds of decision makers will begin investing. I don't know where that will lead, whether this will be similar to the optical fiber situation in China. In the Chinese market for optical fibers, the best year was 2001, since then the market declined and has since recovered, so that this year it is at the level of 2001. From the point of view of demand for fiber, it has remained quite steady in terms of quantity. The difference lies in a 500% increase in supply over the last four years. Twenty different drawers of optical fibers have entered this market in the last few years. So even if the market has remained quite steady in comparison to the rest of the world, the price problem is very severe – probably worse than in the United States. This therefore is the current situation and it will take a very long time for the optical fiber supply/demand situation to balance. Those are my comments on the Chinese situation. Thank you.

**Mr. Norio Okayama**

Chairman of the Board of Directors & CEO, Sumitomo Electric Industries, Ltd. (Japan)

Ladies and gentlemen, I would like to report on the demand of copper wire and cable and fiber optic cable in Japan.

**Demand Trend of Copper Wire in Japan**

**2003 in retrospect:** Starting from copper wire and cable: According to the report by the Japan Cable Makers Association (JCMA), the actual turnover in fiscal 2003 in Japan is 815.900 copper-tons, which is higher than fiscal 2002 by 1,400 copper-tons in volume and by 0.2% in ratio. In September 2003, JCMA forecasted a serious decline of the turnover in fiscal 2003 which could be lower than 800.000 copper-tons. If that had resulted, we would have had the lowest turnover in the last 29 years since 1974.

However, the outcome is over 800.000 copper-tons thanks to the good performance in the 2nd half of fiscal 2003 of the automobile, electric machinery and construction sectors.

**2004 projection**

1. The continued decline of investment in the infrastructure by electric power utilities and telecommunication carriers as well as the fact that the disappointing turnover in the sector of construction compared to the original forecast of fiscal 2004 made by JCMA this March, would have a negative impact on the improvement of the copper cable demand. However, according to the JCMA's reviewed forecast made this September, the turnover of fiscal 2004 will reach 821.000 copper-tons thanks to the stable and good performance of the automobile and electric machinery sectors. The annual turnover of 821.000 copper-tons in fiscal 2004 is higher by 4.000 copper-tons than the original forecast and higher than that of fiscal 2003 by 0.6%.

2. If we compare the demand of fiscal 2003 and fiscal 2004 sector by sector: In the sector of electric power utility, the demand of 19.000 copper-tons in fiscal

2003 is down to 17.000 copper-tons in fiscal 2004, and in the sector of telecommunication, 73.000 copper-tons in fiscal 2003 is down to 68.000 copper-tons. In the meantime, the demand in the sectors of electric machinery, automobile and construction is expected to increase steadily. There is concrete evidence that in the sector of electric machinery, the demand of 197.000 copper-tons in fiscal 2003 will increase to 203.000 copper-tons in fiscal 2004, in the sector of automobile, 76.000 copper-tons in fiscal 2003 will increase to 78.000 copper-tons in fiscal 2004, and in the sector of construction the demand will increase from 366.000 copper-tons to 367.000 copper-tons.

**5-year projection:** In accordance with the JCMA's 5-year projection, which is made this September, the demand is almost flat or shows a small increase during the coming 5 years and the turnover in 2008 will be 824.000 copper-tons. This is because there is uncertainty in the increase of the demand if we consider the influence of the revolution of the industrial structure, even though a gradual recovery of the Japanese economy is expected with an increase of GDP by 2.1% per annum.

#### **Demand Trend of Optical Fiber in Japan**

**2003 in retrospect:** Let me go on to fiber optic cable. JCMA announces that the demand for optical fiber cable in fiscal 2003 in Japan is 9,715.000 fiber-kilometers, which is lower than fiscal 2002 by 35.5%. This is due to the completion of NTT's investment in the underground trunk network and all the investments by the public and private sectors have been maintaining a very low level except for the investment in the field of railway.

**2004 projection:** It is expected that the demand by the CATV service providers will increase because they are planning to invest in the fiber optic trunk network to replace the existing metal-based trunk network. However, a serious decline of the demand is inevitable, because NTT will not necessarily make a remarkable investment for the increase of FTTH subscribers as they have already completed the trunk network construction to meet the market requirement for the time being. This means that even though the market is stimulated by the investment by the new FTTH service providers, their demand is too small to cover the big decrease of the demand by NTT, other existing telecom carriers and the electric power utilities. JCMA has announced a drastic revision of their forecast of fiscal 2004 this September in which total domestic fiber demand will drop to 7,822.000 fiber-kilometers which is lower by 16.8% than the original forecast made this March or by 19.5% than the result of fiscal 2003.

**5-year projection:** Nowadays, it is impossible to expect such huge demand as in fiscal 2001 and 2002, as the current cable demand is shifted to lower fiber count cables for subscriber loop from the higher fiber count cables for the trunk network which has been already completed. On the contrary, if we draw our attention to the future demand, there is a big potential of an increase in demand by the additional investment on the FTTH trunk network by existing service providers

attributed to the increase of data traffic as a result of the popularization of the FTTH service or a new investment by a newcomer in this market. Furthermore, a stable increase of the demand is expected in the market of the private sector such as the LAN in office buildings and FTTH or CATV networks in the condominiums.

Considering such market situation, JCMA expects that the domestic fiber demand in Japan in fiscal 2008 will be 10,047.000 fiber-kilometers assuming that the average annual increase ratio from 2004 through 2008 to be 6.5% per annum. Thank you very much for your attention.

**Dr. Valerio Battista**

CEO, Pirelli Cavi e Sistemi Energia SpA (Italy)

**Power Cables Sector**

After the last 2 years of negative trend, the situation in energy cables seems to have reached a plateau which is witnessed by the improvement in first half-year operating results posted by almost all industry players.

Demand for industrial cables seems to indicate slight recover, despite activity in Europe remaining stagnant. The effects of a significant, sustainable general up-turn are yet to be seen.

Price pressure on general market remains quite strong. Copper price seems to have stabilized which is finally allowing a delayed recover of profitability lost in the first half of 2004. Unfortunately copper premium, non metallic raw materials and energy are still increasing and will likely put some additional tension on this extremely competitive market.

As far as utilities are concerned, volumes remain generally stable, but price pressure is still very strong. Furthermore multi-annual contracts with fixed hollow price will impose, if not properly managed, a significant toll to cable manufacturers.

On the transmission side, the black-outs occurred in the last two years have put some pressure on system operators to invest in the reinforcement of the grid. There are signs of such investments being in the pipeline. However delays in authorization and financing processes, together with a general reluctance to embark in major infrastructural projects from the utilities themselves, are slowing down the execution of these plans.

Nevertheless it is expected that a new wave of infrastructural investments will restart on the power network, with positive effects possibly to be seen already in second half of 2005.

In general terms, the battleground for 2005 will be characterized by the two main following topics:

**Overcapacity:** notwithstanding 2 consecutive years of low volumes and prices, there is little sign of capacity rationalization. Unless further capacity is removed from the market, opportunity of profitability recovery for the cable sector will remain weak

**Raw materials prices:** copper is expected to remain constant on present price levels. However significant increases in copper premiums, oil prices, energy, and transportation costs are foreseen in 2005. No major negative impact on investments is foreseen at this stage but significant pressure on margins is to be expected. Not to be forgotten that higher raw material costs induce higher working capital levels which, in turn, make the achievement of return targets even more difficult.

These two trends may pose a potential threat to the industry profitability in the short-medium term. It is paramount that these matters are treated with appropriate sensibility by the industry, in order to be able to take advantage of a new period of economic growth.

### **Telecom Cables Sector**

The telecom cables and fibers market remains in a very depressed state following the well documented crash of 2001. Manufacturers continue to face the challenges of reduced levels of demand, overcapacity of production - cable and fiber, and the continuing need to improve efficiency and reduce costs in the business.

Prices, which have fallen steadily throughout this period, finally appear to have bottomed-out, albeit at levels which currently generate minimal operating margins. The overall value in the business is only at approximately 30% of its level of 2000 and we remain firmly in an environment of consolidation and low investment in the manufacturing base.

On a slightly more positive note, however, there are finally some signs that a degree of recovery could be underway in the marketplace. The main driver for this recovery is the adoption of Broadband services, predominantly in many of the world's more developed regions and the potential 'pull-through' effect this will have for manufacturers of associated equipment. Almost 15% of all fixed telephone lines globally now deliver a broadband service with the number of new connections growing steadily as both domestic and business users are tempted by the range of services now available including fast Internet, voice over Internet, music download and video on demand.

In terms of direct positive impact on the cable supply industry the effects are not so immediate. Initially it is the manufacturers of the customer premises equipment - producers of modems for example - who are seeing the benefits of the broadband revolution as most broadband connections are actually provided over the existing copper telephone link. However there is now a modest level of demand for new copper cable to be used in the recabling of exchanges in order to support the broadband roll-out. What the industry really needs however is for the advent of broadband to stimulate a new level of growth in the optical cable industry. Whilst this is clearly a future possibility it is not yet a reality in today's business although we are now seeing initial 'last mile' fiber projects being established in a number of markets, including those of Western Europe.

The critical manufacturing overcapacity dilemma still remains and volume growth from broadband alone will not be sufficient to cure the industry of its problems.

**Mr. Gérard Hauser**

ICF President, Chairman & CEO, Nexans (France)

Our Prague convention is coming to an end and I would like to make a few comments before we begin the General Assembly.

First, on behalf of you all and of my colleagues from the ICF council, I would like to thank our guest speakers for finding the time to join us here in Prague from all across Europe and beyond, and for their high quality presentations. All the topics they covered are real for the global cable industry. The enlargement of the European union, investments in power networks, specific requirements of the Oil & Gas industry as well as the competing broadband technologies in access networks, are matters which are and will continue to impact profoundly our industry.

Second, I'd like also to make a few brief comments about the challenges cablemakers face going forward. Between 2000 and 2003, we went through a pretty rough and long crisis with the abrupt collapse of telecom markets combined with relatively poor market conditions due to the economic crisis in many parts of the world. Volume growth was depressed, pressure on prices high and the financial performance of our industry as a whole was not at all satisfactory.

I, we, certainly hope that 2004 will be a transition year: Globally speaking, the economic situation is better in most regions and a number of depressed markets appear to have reached the bottom or even to be recovering. In brief, there are reasons to be more optimistic today than one year ago. However we should not rely on market improvements alone to solve the difficulties facing the cable industry, nor to restore its financial health and attractiveness to investors.

On the contrary, we should all together take advantage of this added room to maneuver in order to fix some of the problems our industry has been facing for decades. However, fixing long lasting structural issues will require some discipline to reduce further overcapacity.

We must assess carefully the justifications for capacity expansion projects and implement pricing policies which are economically sound in order to generate appropriate returns. In particular, the very significant price increases of copper, aluminum as well as oil and its derivatives, which are important elements of the cable cost structure, must be passed on to the market price as soon as possible.

Clearly, a lot has been done over the past 2 to 3 years by many of us to reduce excess capacity and restore the financial health of the cable industry. I hope, I feel, that more remains to be done for the industry to generate higher, more satisfactory returns on capital employed. When we meet again next year in Tokyo, we will see how much progress will have been made over the coming 12 months in making our industry more profitable and more attractive to all our shareholders.

I thank you all for your participation in this convention.

**Mr. C. Baker Cunningham**

ICF Future President, President & CEO, Belden CDT Inc. (USA)

Thank you Monsieur Hauser.

It is a great pleasure, privilege, and honor to become the new President of the International Cablemakers Federation.

We all owe a debt of gratitude to Monsieur Hauser for his outstanding leadership as President of the ICF for the last two years. Today, the ICF is a strong organization, with a sound financial condition, and well positioned to address the challenges that face our industry in the future. So, I would like to personally thank Monsieur Hauser for his service to the ICF, and say that I look forward to having the benefit of his advice and friendship during my term as President.

In preparing for this Congress, I reflected over the past decade in our industry. There is no doubt that the wire and cable industry is a vital component of economic development around the world. It is also an industry that has been experiencing dramatic changes. These changes involve technology, they involve geo-politics, and they involve economics.

Over the past few years, many of us have struggled to have the level of profits we would like, or even as much as we had in the past. World-wide industry demand declined by about 25%. Profit margins vanished, or were severely compressed.

There have been a number of mergers, realignments, divestitures and other structural changes that have occurred. I believe these will continue as we as an industry adapt to the globalization of the world economy and the effects of new technology.

As you heard from our panel earlier today, we are seeing improved market conditions. Demand is increasing again after three years of decline. That is good news. But, that will not hold back the tide of change that is affecting us all.

Some of us will prosper. Some of us will struggle. Some of us may disappear or be absorbed by others in the industry to form even stronger challengers to the current leaders.

I don't know what the outcome will be, but I do know that we all face challenges in a changing environment. The common bond that we share is a commitment to the wire and cable industry. I think in these uncertain times, it is more important than ever that this organization, The International Cablemakers Federation, provides the forum for industry leaders to get together to exchange ideas, learn about new development, and create relationships to insure that we remain a great world industry.

Thank you very much. I look forward to the opportunity to be your President for the next two years.

That concludes the 2004 ICF annual Congress. I thank you all for attending and I look forward to seeing you in Tokyo next year.