

# THE CUTTING EDGE

WOOD MACHINERY MANUFACTURERS OF AMERICA

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## Tax Cuts and the Economy



**By John Satagaj, London & Satagaj**

The President has laid out an ambitious tax cut plan, whether in total it is a stimulus plan is another matter. There is certainly one item that would meet our standard for a stimulus – an increase in direct expensing. It may be some time, however, before we see any action on the plan.

Current tax law (known as Internal Revenue Code Section 179) permits businesses to write off as expenses up to \$25,000 worth of equipment purchases.

The President's plan would increase that limit to \$75,000 and index it to inflation to encourage businesses to buy technology, machinery, and other equipment they need to expand. The amount of investment qualifying for this immediate deduction begins to phase out businesses with investment in excess of \$325,000. This is an increase in the current phase out base of \$200,000. The cost over 10 years is only \$16 billion. I think, if any pro-business aspect of his proposal survives the legislative process, the increase will survive. Many Democrats have embraced it in their own stimulus proposals.

The President has proposed allowing taxpayers to exclude dividends from their taxable income. Putting aside the pros and cons of the dividend exclusion proposal as a stimulus measure, one question I often get is whether the proposal creates an opportunity for WMMA members to lessen their tax liability. Many WMMA members are organized as S Corporations. By definition, the income of S Corporations is "passed through" to the S Corporation shareholders and not taxed at the corporate level. Therefore, for S Corporation shareholders (and sole proprietors and partners), the question isn't one of eliminating double taxation but whether moving to a regular corporate tax structure, often know as C Corporation status, and using dividends to channel income to the owners would result in a smaller tax bill. It turns out the answer is a mixed one at best. The corporate tax rate structure and the individual rate structure do not match up. When the question is simply one of turning over fewer tax dollars to the government, what you have to watch for is not the marginal rate of taxation (the rate for a particular income bracket), but the effective tax rate when all the brackets are blended. The effective rate of taxation is taxes paid divided by taxable income.

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# Public Policy

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The key question is whether an S Corporation shareholder would even be allowed to shift all profits coming out of the business to dividends. There are rules on the books already about compensation that would probably prohibit it and more limitations are likely to be imposed, if the President's proposal is enacted. At the end of the day, you must conduct a very specific numbers crunching exercise for your business to figure out whether it might reduce your taxes.

It may be some time before we see real action on the plan. If it moves slowly, it will be because a decision was made to use a legislative procedure that takes a little longer to complete, but lowers several voting hurdles. You may hear the words, "budget reconciliation" many times during the next several months. In theory, Congress uses a procedure by which it passes a basic budget, known as the "budget resolution" and then instructs the various committees to come up with the specifics to meet the budget goals. The budget resolution does not require Presidential approval but does require both chambers to agree. Once the committees develop their reconciliation plans, the chambers consider one or more bills, known as budget reconciliation bills, that carry those instructions. Procedurally, there are some advantages to moving controversial legislation through the budget reconciliation process. In the Senate, a Senate cannot filibuster a budget reconciliation bill, so only a simple majority is needed for passage instead of 60 votes. The disadvantages include a "germaneness" rule that requires the 60 votes and a rule that generally frowns on proposals that lose tax revenues immediately or in the short run.

The last session of the last Congress failed to adopt a budget resolution, so the process did not move forward on that basis. In 2001, the President's first major tax cuts were enacted using the budget reconciliation process. During the Clinton Administration, the President's opposition occasionally blocked reconciliation bills.

With the chambers of Congress controlled by the same party and the President of the same party, the prospects for aligning the stars to use the budget reconciliation process are much brighter. The leadership will have to consider whether the advantages of a lower majority vote requirement in the Senate outweigh the disadvantages, which usually restrict the scope of permanent policy change. As I write, the decision has not been made.

All of this will play out against the backdrop of the deficit concerns I outlined last month. The Congressional Budget Office (CBO) has released the most recent numbers regarding the federal deficit. CBO projects a deficit of \$199 billion for the current fiscal year and a deficit of \$145 billion for next year. The President has pledged to work towards a budget for the next fiscal year that holds discretionary domestic spending to a four percent increase. He is putting the rest of his deficit reduction eggs in the tax-cut-leads-to-economic-growth-leads-to-new-tax-revenues basket. We will see how it plays out.

***If you have questions or comments about this article, or other Public Policy issues, contact John Satagaj at e-mail@lonsatlaw.com or 202/639-8888. You can also e-mail WMMA headquarters at [wmma@fernley.com](mailto:wmma@fernley.com).***

|                       |  |
|-----------------------|--|
| Charles A. Granger    | President  |
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| G. A. Taylor Fernley  | Management Liaison   |
| John Satagaj and      | Legislative Counsel  |
| Andreas S. Kalisperis | 1010 Massachusetts Ave. NW, Suite 400<br>Washington, DC 20001 (202) 639-8888 |
| Joseph Mc Hale        | Legal Counsel  |



|                                |                 |
|--------------------------------|-----------------|
| Harold Zassenhaus              | Export Director |
| 7758 Wisconsin Ave., Suite 306 |                 |
| Bethesda, MD 20814             | (301) 652-0693  |

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*The opinions expressed in any articles by outside consultants are their own views and not necessarily those of the WMMA®.*

## Announcing: A New WMMA Staff Member

The WMMA Board of Directors is pleased to announce a talented addition to the WMMA team: Bill Norton. Bill joins WMMA as Marketing and Information Director, a position that falls directly in line with the strategic initiatives set forth in December of 2002.

### **Bill's responsibilities will include:**

- Liaison for the Industry Marketing Committee
- Liaison for the Informational Committee (new Strategic Initiative)
- Liaison for the Business Model Initiative (new Strategic Initiative)
- Coordinator of development of marketing programs for all Association activities, programs, and services

Bill is a seasoned business management professional with 15 years of diverse event management and marketing communications experience. He is a proven leader, with skills in creative analysis, negotiating, problem solving, team building and budget management. He has particular strengths in event marketing promotion, multi-tasking, event/project planning and implementation, strategic development, and client/vendor management, while achieving corporate objectives.

In conjunction with your current WMMA staff, Ken Hutton, Harold Zassenhaus, Jean McCann, Raylene Torres and Karen Boyle, Bill will be supporting you and your marketing needs well into the future. Bill will be present at the February Carolinas TSI Expo, and at the Woodworking Industry Conference in April. Please welcome Bill to the WMMA family!

### **Contact Information:**

Bill Norton  
WMMA Marketing & Information Director  
[wnorton@fernley.com](mailto:wnorton@fernley.com)  
215-564-3484 x235

## Management Information Committee to Dissolve

### *New Industry Initiatives Replace Committee Role, Reports*

As part of WMMA's new strategic visioning plan, the Management Information Committee will disband. This decision was made because one of the primary tenets of the Association's new strategic initiative is for "WMMA to gather primary industry data and to position itself as the source of information for the entire woodworking industry." This work will now be carried out by a task force, thus eliminating the need for the committee and its programs.

The committee dissolution also means the discontinuation of the standard management information committee reports. This includes the monthly Executive Trends Report and the Quarterly Delinquent Dealer Report.

In announcing the decision, WMMA President Chuck Granger praised the work of the committee and Chair Matt Carroll (Black Bros Co), noting, "The Management Information Committee has demonstrated great dedication and insight in seeking out reports to assist member companies. We appreciate their diligence in carrying out their committee mission. However, the association will be taking a new approach to industry information and data collection. The Management Information Committee has provided a great framework; we are optimistic that our new task force can take this initiative to a new level."



# Association News

## New on [www.wmma.org](http://www.wmma.org)!

Did you see an article in a 2002 Cutting Edge edition that really struck you? Don't know exactly where to find it? Or do you want to revisit a certain Public Policy article or a WMMA annual update but can't seem to place it?

Now an entire listing of 2002 Cutting Edge articles is right at your fingertips, at [www.wmma.org](http://www.wmma.org). Simply visit the "WMMA Newsletter" link at <http://www.wmma.org/newsletter.htm> and view the archived listing of 2000-2002 issues. The first item is an Excel Spreadsheet, organized by month, by topic.

### This new resource should prove convenient:

☞ when wanting to supplement a company-wide discussion with information that is already "out there"

- ☞ when reviewing Member News... "When did those two companies merge...?"
- ☞ when seeking Standards information, because your group is now looking into exporting...

What may not have seemed pertinent then, is suddenly pertinent now. And WMMA has made it easier than ever to use our popular Cutting Edge as a timeless resource.



## The 12th Annual Woodworking Industry Conference is right around the corner!

### Woodworking Industry Conference

April 9 – 12, 2003

Renaissance Vinoy Resort and Golf Club  
St. Petersburg, Florida

Save your company hundreds of dollars by registering EARLY for the 2003 WIC in St. Petersburg, Florida. If you are certain you are attending the Conference, register TODAY!

- \$ Register a delegate before March 1st and save \$100!
- \$ Register for the Contact Table program before March 1st and save \$75!
- \$ Register for the Saturday Optional Contact Table Program before March 1st and save \$50!

### PLUS...

- ▶ WMMA Executive Committee, Directors, Committee Chairs, and Committee Members all receive

registration discounts. Don't forget to include your coupon with your registration!

- ▶ If you have never attended the WIC before, you are eligible for one FREE registration as a "First Time Attendee!"
- ▶ If your company has had NO representation at a WIC in the last 5 years (from 1998-2002), WMMA offers TWO FREE registrations to two delegates from your company, PLUS a \$500 cash stipend.
- ▶ New this year: Register your spouse and children (over 12 years) FOR FREE!



The 2003 WIC promises to be exciting and rewarding for all delegates and families. Check your mail for the WIC brochure and registration information, which was sent to you in late January. And you can always view the Registration and Event information at [www.wmma.org](http://www.wmma.org), under "What's New."

Do not delay. Make your arrangements today. The early bird catches the savings.

For more information on all WMMA programs and services, visit the website at [www.wmma.org](http://www.wmma.org). You can also contact headquarters at P: 215/564-3484; f: 215/963-9785 or E: [wmma@fernley.com](mailto:wmma@fernley.com).

## Thoughts on ExpoAMPIMM

By Harold Zassenhaus, WMMA Export Director

From January 15-18, the WMMA organized a pavilion at the inaugural ExpoAMPIMM, a Mexico City woodworking equipment and accessories trade fair sponsored by the Association of Mexican Providers to the Woodworking and Furniture Industry (AMPIMM). The WMMA decided to take a flyer on the show since it held great promise of focusing on the woodworking equipment industry and attracting quality visitors. I think we made the right decision.



### Positive Points

- ◆ Exhibit facilities are new and excellent with high ceilings, no columns, easy freight access, good lighting, and the capability of providing electricity and compressed air services from under the floor.
- ◆ The facilities are relatively close to the business and hotel districts of the city (20-30 minute taxi ride).
- ◆ The hall layout was very good.
- ◆ All major distributors exhibited and most machinery available in Mexico was represented. Virutex, the largest dealer in

the country (Weinig, Biesse), decided to exhibit in the end. It previously had declined membership in AMPIMM and actively supported the rival fair, Promueble.

- ◆ All visitors wore bar-coded badges read upon entry and, through the organizer, exhibitors were able to access visitor information.
- ◆ The quality of visitors was very good, according to dealers and exhibitors. The last day, Saturday, proved to be a very good day for many, as potential buyers came back and many new visitors attended from Mexico City and other regions.

### The Fair

**Size:** Approximately 3,500 Sq. m

**Visitors:** Approximately 3,000

**Exhibitors:** Approximately 90

**U.S. Exhibitors:** 15

**WMMA Members Exhibiting On Their Own:** 2

**WMMA Members Exhibiting In Their Dealer's Booth:** 9

**WMMA Members In The WMMA Pavilion:** 4.

### Negative Points

- ◆ Turn out was less than anticipated (3,000 vs. 5,000).
- ◆ The sponsor, AMPIMM, admitted that both advertising and mailing campaigns were less than they should have been. In addition, there was no VIP program and little advertising done in foreign country trade publications, with the exception of *Vetas*.
- ◆ Exhibitor catalogs were not distributed (they were placed at the rear of the exhibition hall with no notice).
- ◆ Exhibitor manuals were distributed very late and were inadequate, missing order forms for some of the services.
- ◆ Ordered services were costly. For example, security service was \$70/night and cleaning \$1.50/sq. m. per day.

### Summary

This was an inaugural event facing competition from a relatively well-known fair, Promueble, that opened three days later in the same city. Considering this, the fair got off to an excellent start. While the numbers were low, the quality of visitors was high. The exhibitors in the WMMA pavilion were expecting to make contacts, better define the market and/or identify potential dealers. There were a couple whose expectations were exceeded --- exhibits were sold, additional leads generated and dealers identified.

The event's administrative shortcomings can be easily overcome and event marketing should improve. However, since AMPIMM has little cash, marketing will likely continue to be weak.

The organizer has decided to hold the event annually for the next two years and every other year thereafter. In doing so, they expect it will grow on its strengths and continue to pull relevant exhibitors from Promueble.

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## WMMA Pavilion

- ◆ **Size:** 78 sq. m.
- ◆ **Exhibitors:** 4
- ◆ 4 members shared the WMMA booth, with 2 sending their export managers.
- ◆ The location was very good as all visitors could easily see it upon entering the hall.
- ◆ The pavilion reflected a professional image and well represented the association.
- ◆ The contractor was accommodating to minor changes.

AMPIMM will continue its dialogue with the other major Mexican fair, TecnoMueble, held in Guadalajara every July, in the hopes of convincing them that both fairs will be stronger if held in alternate years. If all goes according to plan there will be two major trade fairs in Mexico: held one year in Guadalajara and the following year in Mexico City. Unfortunately, in the interim, there will be at least three Mexican fairs held annually.

## The Market

Members should devote more attention to the Mexican market. Although it may not be a large one for a long time it is easy to travel to, largely within member's time zone, has 80

million inhabitants with a growing middle class and has a base of solid dealers.

Mexico is facing significant competition from China. Woodworking companies are moving to China to take advantage of lower labor costs. If Mexico is to grow economically it will have to invest in capital equipment and adopt measures to continually increase productivity. This could play to members' strengths.

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# Ligna: We're Sold Out

## Ligna Hanover

### May 26 – 30, 2003

WMMA contracted for 158 square meters of space and we are sold out. This will be the first time that the owner (VDMA) and the organizer (Deutsche Messe) have allowed associations to have exhibits on the show floor.

Members can still share the WMMA booth for \$200. This entitles you to have product literature on display, show product tapes and work out of the booth if you plan to attend. Within ten days of the fair's closing a report on the fair, along with leads generated, will be forwarded to you. If interested, visit the website at <http://www.wmma.org/members/mpdf/tradefairpartform.zip> for a participation form. Please send in your form as soon as possible.

The WMMA pavilion is located in Hall 14, stand G20. It will have a small lounge and bar serving coffee and tea. If you plan to attend Ligna, drop by or have your meetings at the Pavilion. The WMMA will also have a booth and access to conference facilities in the "International Industry Associations" area. Details will follow.

We will be updating the "WMMA Member Guide to Ligna." It will contain practical information on getting to Ligna, getting around Hanover, a few do's and don'ts, and information on the WMMA association booth. Look for it shortly on the WMMA website.

For more information on exhibiting with WMMA at foreign trade fairs, or any other export development business, Contact Harold Zassenhaus, WMMA Export Director at **P:** 301/652-0693; **F:** 301/986-1389 or **E:** [zemg@erols.com](mailto:zemg@erols.com). You can also contact headquarters at **P:** 215/564-3484; **F:** 215/963-9785 or **E:** [wmma@fernley.com](mailto:wmma@fernley.com).

## 2002 Round-Up

by Art Raymond, A.G. Raymond & Company

Many of the final numbers for 2002 are now in. How did the economy do last year in areas critical to wood products manufacturing?

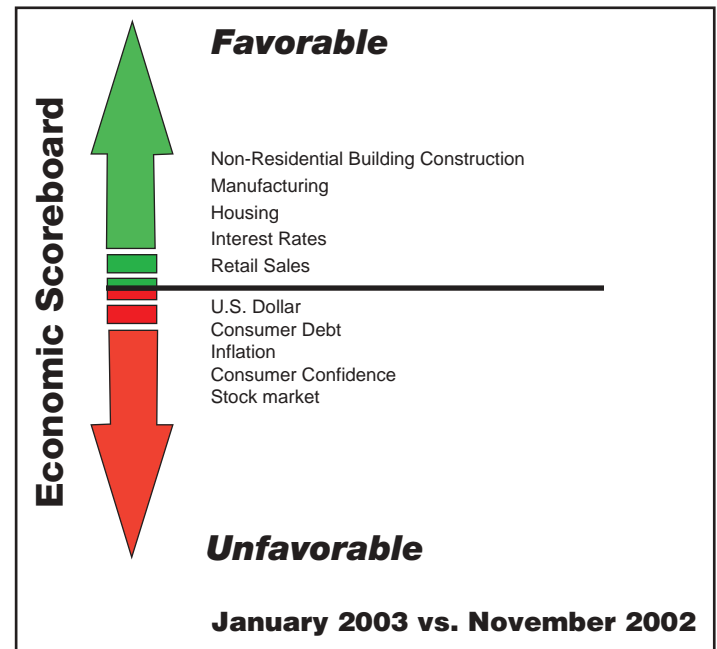
- ▲ Gross domestic product was up 2.4% vs. 0.3% for 2001.
- ▲ Business investment was up 1.5% in 4Q, the first increase in two years.
- ▲ Housing starts rose 6.4% to 1.84 million, a 16-year high.
- ▲ Home resales increased by 5% to 5.56 million, a national record.
- ▲ Personal incomes for those working rose about 3.5%.
- ▲ Inflation, at 2.4%, became a non-issue.
- ▲ Home prices increased by 7.1%.
- ▼ Manufacturing jobs continued their 29-month decline with losses totaling two million jobs since July 2000.
- ▼ The stock market was down for the third consecutive year for the first time in 60 years, losing \$2.8 trillion in value.

All in all, not a bad year for the average working American with a house and a small stock portfolio.

### The Falling Dollar

The U.S. dollar, which weakened by 13% last year against a broad basket of other currencies, may be one of the top economic stories of 2003. Will the dollar continue its decline, help U.S. exporters grow their international sales, and give some protection to U.S. producers facing low-priced, offshore competition?

In the face of a steep stock market decline, a recession, and a rising trade deficit over the past two years, the dollar has been surprisingly strong. Remember that two natural factors determine the value of any currency:



■ **Foreign trade** - Usually a country running a sizeable trade deficit sees its currency fall. The U.S. trade deficit is setting new records every month in the face of a slow economy. Our current account deficit is running at about 5% of GDP.

■ **Capital flows** - Money moves to the country with the best investment returns. During the boom of the 90's, investors around the world poured cash into our stock market. Now with stocks down and interest rates at a 41-year low, U.S. financial assets are less attractive to foreigners. Hence, less capital is coming in to pay for overheated importing.

Add the risk of war in Iraq, and you have a declining dollar. Many economists believe that the dollar will fall to \$1.16 vs. the euro this year.

But don't forget that another factor – government intervention – also affects foreign exchange rates. Japan is famous for buying dollars to keep the yen weak and their exporters happy. Other Asian countries like South Korea and China have joined that club. China, the primary competitor of many U.S. manufacturers, ran a \$100 billion trade surplus with the U.S. in 2002. But their currency, the renminbi,

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# Business Briefing

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remains within a narrow band around 8.27-8.28 to the U.S. dollar. The Chinese have shown no sign of reducing their intervention.

With the renminbi artificially fixed in value, China is exporting deflation around the world. Their trade surpluses have risen for nine years. 2002 exports were up over 22%, and their economy grew by nearly 15%. Yes, this performance deserves applause. But the rest of world is paying a heavy price in lost jobs for Chinese success.

By economist Adam Smith's definition, the U.S. and China are not engaged in trade. The flow of goods is virtually one way eastbound as we simply use Chinese labor to produce for U.S. markets. Ultimately, this situation should redress China's undervalued currency.

A stronger renminbi would reduce the cost of U.S. hardwoods and veneers for Chinese furniture makers, U.S. machinery would become more competitive, and the prices of Chinese made furniture and other wood products would rise. The economics would change. Competition would revert to a somewhat level playing field.

Will the Chinese revalue, or will U.S. industry cry out for import protection? Our guess is a 15% revaluation. Keep your eye on this story.

## Higher Taxes Anyone?

A small, almost unnoticed story from Oregon should relay to Congress an important message – voters think governments should cut spending in tough times, just like the rest of us. On January 28, Oregon voters, not known for their conservatism, defeated Measure 28, which asked for a tax hike to support \$310 million of government spending. As one voter said, "When I don't have enough money, I have to change my habits. Government should be the same way."

## Sector Situation Report

*Latest news from the wood products industry by sector...*

☒ **Office Furniture** – Sales of office furniture remain in the doldrums. BIFMA reported December shipments 6% below 2001. Shipments have now declined year-over-year for 22 consecutive months. For the year, the industry has shipped 19% less product than in the first eleven months of 2001.

■ **Herman Miller** reported 2Q sales declining by 9.5%, while gross margin improved to 31.8% as a result of cost savings initiatives.

■ For its 3Q2003, **Steelcase** noted that sales fell by 11.6% and gross margin declined to 28.1%.

Industry analysts are not expecting a sustainable recovery in this sector until business investment improves.

☒ **Kitchen Cabinets** – Cabinet sales rose 9.3% in December vs. the same month 2001, according to the KCMA's Trend of Business Survey. Sales of semi-custom cabinets, where the consumer has tremendous choice of style, species, color, and configuration, were up 19.5% for the month. For the full year, 2002 cabinet sales were up 10.8%.

■ **American Woodmark**, the second largest U.S. cabinetmaker, reported sales growth of 15% for their 2Q2003. Gross margin declined to 24.3%, due to temporary operating inefficiencies attributable to bringing new capacity on line. Management has suggested that 3Q sales may grow by only 5% due to slower sales at Home Depot, which provides 40% of its total volume.

Through refinancing, U.S. homeowners pulled about \$135 billion out of their home equity in 2001. These cash-outs supported home improvements like new kitchens. Economists are suggesting that a slower rate of refinancing in 2003 will spell the end of this source of cash. With it may go the two-year boomlet in the cabinet industry. Stay tuned.

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# Business Briefing

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- ☑ **Home Furniture** – News from this sector continues mixed:
  - **Furniture/Today**, the leading industry newspaper, forecasted that 2003 sales would rise by only 2.4% vs. 4.2% in 2002. Imports are predicted to continue their growth.
  - **Furniture Brands**, the largest furniture producer in the U.S., reported a 24.9% sales increase, reflecting its acquisition of Drexel Heritage, Henredon, and Maitland Smith in 2002. Gross margin improved to 25.5%, reflecting higher margins from its growing import business. Soft business conditions continue at higher price points in its product line.
  - **La-Z-Boy**, the second largest U.S. furniture maker, warned of weaker sales in their 3Q2003. The maker of brands such as Pennsylvania House and England says that earnings will be lower.
  - Manufacturer **Stanley Furniture** reported a 12.3% increase in 4Q2002 sales. Better factory utilization and increased imports generated a gross margin of 24.8% and an operating profit of 10.8%.
  - **Ethan Allen**, the well-known producer/retailer, reported Q2003 sales up 3.1%.
  - Retailer **Pier One**, with 1,000 stores nationwide featuring imported goods, saw December sales grow 10.7%, suggesting solid holiday business. By comparison, **Havertys** reported its December sales down 2.8% in total with comparable store sales falling 9.9%.
- ☑ **Non-Residential Construction** – According to Dodge Analytics, total construction (residential and non-residential) advanced by 1% in 2002 vs. 5% growth in 2001 and 6% in 2000. Offsetting a strong housing market, the non-residential segment fell by 10%. Commercial categories were

weakest – warehouses, down 22%; hotels, down; and offices, down 28%. In the institutional category, construction of healthcare facilities improved by 2%. School construction, which set records in 2001 and was strong in the first half of 2002, fell 5% for the year. Retail store construction fell a modest 7% but saw strength from national chains. Construction of manufacturing plants dropped 35%, reflecting continuing shift of production offshore.

- ☑ **Wood Flooring** – Strip flooring shipments in November were up 19% over the same month in 2001. For the year shipments are 10% higher than 2001.

If you have questions or comments about this article, contact author Art Raymond at [info@raymondnet.com](mailto:info@raymondnet.com) or 919/831-0070. You can also e-mail WMMA headquarters at [wmma@fernley.com](mailto:wmma@fernley.com).

## WMMA Mission Statement

The WMMA shall represent and support domestic manufacturers of equipment and tools used in the processing of wood and wood products from the forest to finished products.

# Business Briefing

## 2003 Wood Technology



## Clinic and Show

The 31st annual Wood Technology Clinic and Show will be held March 19 – 21, 2003 at the Oregon Convention Center in Portland, Oregon.

The Wood Technology Clinic and Show presents the largest exposition in North America, featuring over 800 booths and occupying over 150,000 gross sq. ft of exhibit space. The show will feature over 400 manufacturers and distributors representing North America and abroad. The show is expected to attract over 7,000 attendees.

In addition to the exposition, a comprehensive and dynamic conference program comprises three full days of highly targeted sessions covering industry growth trends and opportunities, business management issues and production practices. The program has been expanded for 2003 to include additional seminars on the engineered wood segment.

For the latest information about WTCS 2003, including online registration and housing reservations, please visit the official show web site at [www.woodwideweb.com](http://www.woodwideweb.com), or call 1-770-291-5409 or 1-800-933-8735. For information on exhibiting at the 2003 event, contact Fred Cambria at 646-854-5087.

### Member News

Hasko, formerly known as Haskew & Company, R.K., and manufacturer of "Heavy-Built" flooring and rough mill machinery, is proud to announce the promotion of Stephen Pugh to Vice President of Sales/Sales Engineering. Steve will focus the company's attention to design and layout of complete systems and continue to coordinate custom rebuilds and field service.

## "What Does Your WMMA Dues Dollar Buy?"

**Industry Tradeshow Discounts**

**Worldwide Publicity**

**Monthly Newsletter**

**Educational Opportunities**

**Industry Advisor Program**

**Industry Safety Standards**

**Industry Statistics**

**Economic and Benchmarking**

**Data**

**Regulatory Alerts**

**Legislative Calls to Action**

**Internet Links**

**Leads for New Business**

**Access to Overseas Distributors**

**Export Trade Certificate**

**Networking with**

**Industry Peers**

**Manufacturer/Distributor**

**Conferences**