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## Crisis and opportunity: Dynamic Market Theory forecasts profits from market volatility in the Far East



J. Christoph Amberger

*“Cameco Corporation is showing a gain of 84%! I suggest you sell your shares at market,”* wrote Taipan editorial board junior member Ann Sosnowski on February 10 in a special email alert: *“If you remember, I recommended Cameco Corporation (CCJ:NYSE) for under US\$68.00 in September’s Taipan issue. (I have a recorded price of US\$65.00 the day after I issued the buy.) Since then, I’ve updated its progress in the 247profits e-Dispatch on an almost monthly basis. In December, Cameco’s stock split three-for-one, making each share worth about US\$21.70. At the end of January 2005, Cameco’s fourth-quarter net earnings rose 9% compared to the same period in 2003.*

*Currently, Cameco is trading for around US\$39.90. Your position from September is showing a gain of 84%! [...] Sell your CCJ shares at current market price!”*

Meanwhile, our British import Martin Denholm alerted us to profits in his play on **Abercrombie & Fitch**: *“If you took my advice to buy shares back in November 2003, you’re sitting pretty. We cashed out with a sweet 46% gain on the first half of the position on November 4, 2004.*

*“Recently ANF has enjoyed a blazing run, galloping up to US\$54.66 and setting a new 52-week high of US\$57.04 on February 7. If you’re still with me on the second half, that gives you a dandy 89.6% gain. As you know, new 52-week highs are bullish, so I’m sticking with it.”*

Our Chinese ADR’s also point to 2005 being a good year for Taipan’s Dynamic Market Theory. Of course, long-time Taipan members are not surprised that our Chinese stock picks are doing well. Indeed, ever since we recommended you buy stock in Hong Kong & Shanghai Bank back in 1989, Taipan has been on the forefront in capitalizing on China’s exponential profit potential. We recommended Chinese stocks and their ADR’s even before the tidal wave of foreign investment began flooding Mainland China after 1994. We were invested in Hong Kong almost a decade before it reverted to the People’s Republic. And we generated triple-digit gains for our subscribers even as the Asian currency crisis in 1997 was redefining the economic roles of the Pacific Rim countries.

But if you’ve been watching the mainland Chinese stock indices over the last year or so, you will have noticed an interesting trend: the Shanghai

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Composite, for one, looks like the track of a downhill skiing competition.

This might come as a surprise to folks who've modeled their views of China mainly on Chinese GDP growth rates and that country's bulging trade surplus with the US. But stock markets are the reflections of how a people really sees its immediate economic future. And a yearlong decline in the Mainland Chinese indices might be a better indicator of trouble in the making than any consumer confidence indicators in the world.

### ***Batten down the hatches***

Below the surface, not all is well in China: industrialization and urbanization may be proceeding at a helter-skelter pace. We might be well served to remember that there still is a vast communist bureaucracy underneath the dazzling capitalist trimmings that is as inefficient as it is corrupt and wasteful.

Some of the most aggressive and influential businesses are owned either directly by the state or by the armed forces. This "distinct" ownership has provided a perfect screen behind which Chinese business has armed regimes from Baghdad to Tehran to North Korea: after all, who's the Chinese government to tell army-owned NORINCO with whom it should do business?

Since 1994, the People's Republic has turned into the world's top investment destination, attracting the majority of the world's direct foreign investment. China's main attraction is its low labor cost. Unfortunately, Chinese politics are so opaque that it is almost impossible to obtain reliable data on what exactly those labor costs are... and how much of this attractiveness is owed to shady subsidies.

In the medium term, we see trouble brewing. China already borrows more as a percentage of GDP than the US. China's banks—much like Japanese banks in 1991—are buckling under a heavy load of bad loans and are being "*undermined by an institutionalized misallocation of capital with little regard for international norms of risk management and the extension of credit,*" as a Bloomberg correspondent put it recently.

### ***Age-bomb ticking***

Worse yet, China is in the same situation as most industrialized nations when it comes to demographics. Due to its rigorous one-child policy, ten Chinese workers will have to support three Chinese retirees by 2025. That may be comparable numerically to the United States and is far less burdensome than the ratios of Japan and Germany. But Japan, Germany, and the US have had a half-century of prosperity to create a fiscal backlog, however deficient it may be. The Chinese national pension system, however, already covers only 20% of workers. Business Week wrote on January 31: "*The national pension system has a shortfall of \$6.2 billion, which could reach \$53.3 billion by 2033, according to the Asian Development Bank. Most provincial pension plans are also in deficit.*"

The Chinese yuan will depend on its peg against the bargain-basement dollar to keep the export economy humming and China able to borrow to feed its growing class of unemployed. Beijing will do what it takes to come out ahead in the looming struggle to take business away from competitors such as Cambodia, Vietnam or Thailand. For Western consumers, that means prices for Chinese imports will get even lower.

For investors, however, it also means keeping a clear and critical eye on how the Mainland Chinese indices perform: as in Japan a decade and a half ago, they may provide the early warning system that signals when things come to a head.

After all, they always do.

### ***Crisis and Opportunity***

Luckily, our Dynamic Market Theory thrives on just this kind of volatility. When the Nikkei started to buckle in 1990 and 1991, *Taipan* rode its epic decline to triple-digit profits with Kingdom of Denmark Nikkei Put Warrants. Since then, however, our analytical tools have improved dramatically. In fact, our *WaveStrength* team has spent the better part of a year developing and back-testing an analytical tool that harnesses the *WaveStrength* predictive system to chart the immediate future of the Chinese market. In this issue, *Trending East* editor Michael Wiles kicks

off the live-fire test of the system with a play on the iShares FTSE/Xinhua China 25 Index, a New York-traded ETF that we believe will become as effective a proxy for the Chinese markets as the

QQQQ's are for the NASDAQ.

No matter where the markets are headed at home and abroad, count on your *Taipan* team to show you how to turn crisis into opportunity! ■

## China on your terms: Profiting from China in your own back yard

*By Michael Wiles*

As all traders know, a great opportunity is made even better when discovered at its beginnings.

China is one such opportunity. While I know it seems strange to suggest China is "new" in any respect, recent developments have placed the country in position to become a larger player in the global market. What is more, some of these developments are designed to allow the US investor safer (and therefore more profitable) access to the country's continuing growth.

Before we get into all that, though, it's important we first examine the big picture.

### ***The dark side of the street***

Admittedly, and despite all its economic success, China is still a mess. Financial scandals and questionable businesses decisions (unacceptable environmental practices, for example) appear often within the Chinese market, creating fear in foreign investors.

And, honestly, who can blame them for being a bit skittish? Even without the scandalous business news, trade regulations in China have long made investing there a mystery (to say the least).

As a result, foreign traders have lost quite a bit of money in the past. For example, telecom companies were hit particularly hard a few years back when they structured investments based on the advice of Hong Kong consultants that either ignored or simply didn't understand Mainland China's trading policies.

Then there is China's current political climate (as well as that in surrounding countries), which is doing more than its share to frighten off foreign investment.

It's no wonder many domestic traders avoid the Chinese market altogether. But if you're serious about seeking out strong, long-term investment

opportunities, I suggest you not be among the timid.

### ***Rewards for the brave***

The reason is simple: The more people scared away by the occasional negative news from China, the cheaper a given piece of the action is, and therefore the more of it you can acquire for a relatively low investment.

And a piece of China is indeed worth having. For starters, the very future of telecommunications may rest in the country.

China already serves over 300 million mobile phone subscribers, making it the largest mobile market in the world, and that figure is expected to climb to 556 million by the year 2010. China also anticipates a large increase in Internet, cable television and fixed-line phone customers, which only stands to sweeten the gains.

Overall, China's economy is expected to grow 8% annually over the next five years. This figure is largely thanks to China's gaining strength in both the technology and raw material markets, as well as its abundant workforce and increasing social stability.

Now, you may still be hesitant to get involved because of China's arcane trade laws, but I am happy to say you can now put those worries to rest. London's FTSE Index (the British equivalent of the S&P 100), along with China's Xinhua Finance, have you covered.

### ***Liquid on both sides of the Strait***

The iShares FTSE/Xinhua China 25 Index (FXI) is an exchange-traded fund, comprised of China's top 25 most liquid companies, that debuted on the NYSE in October of last year.

The China 25 holds 50.98% H Shares (securities of companies nominated by the Chinese government for listing and trading on the Hong Kong Stock Exchange) and 49.02 % Red Chip Shares

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(securities of Hong Kong incorporated companies that trade on the Hong Kong Stock Exchange).

The five highest-weighted components of the 25 are China Mobile (Red Chip), PetroChina (H Share), BOC Hong Kong (Red Chip), CNOOC (Red Chip), and China Telecom (H), while the five best-performing components are Ping An Insurance (H share), China Resources Enterprise (Red Chip), Lenovo Group (Red Chip), Cosco Pacific (Red Chip), and China Life Insurance (H Share). On the other end of the spectrum, the five worst-performing components are Maanshan Iron & Steel (H Share), Aluminum Corp. of China (H Share), China Unicorn (Red Chip), Sinopec Shanghai Petrochemical (H Share), and Huaneng Power International (H Share).

### A prettier picture?

This information is all well and good, but what the newly interested trader really needs to know can be found in this quote from Fredy Bush, CEO of Xinhua Finance:

*“Listing the Hong Kong shares as an ETF first gave us the ability for American investors to invest now [...] this is the first China ETF in the U.S., and with all the investor interest, and with it being an ETF, it allows individuals finally to invest in the opportunity that is China.”*

One can begin to see the value of this ETF. Not only does it provide access to China under the SEC’s domestic regulations and allow US traders to gauge China’s market, it also serves to enhance China’s global value.

The more money this fund attracts, the better supported its components will be, and therefore China’s market will increase in value.

Truly, this ETF is a key, as well as a vehicle, for profiting from Chinese growth.

As you can see from the chart on the right, the China 25 already has an interesting history despite its youth. After an all-time high of US\$56.50 on 12/02/04 (denoted as “1” on the chart), the fund bounced along a downward trend, finally bottoming out at US\$52.00 on January 7 of this year (denoted as “2”).

At that point, the ETF began its ascent and has been slowly

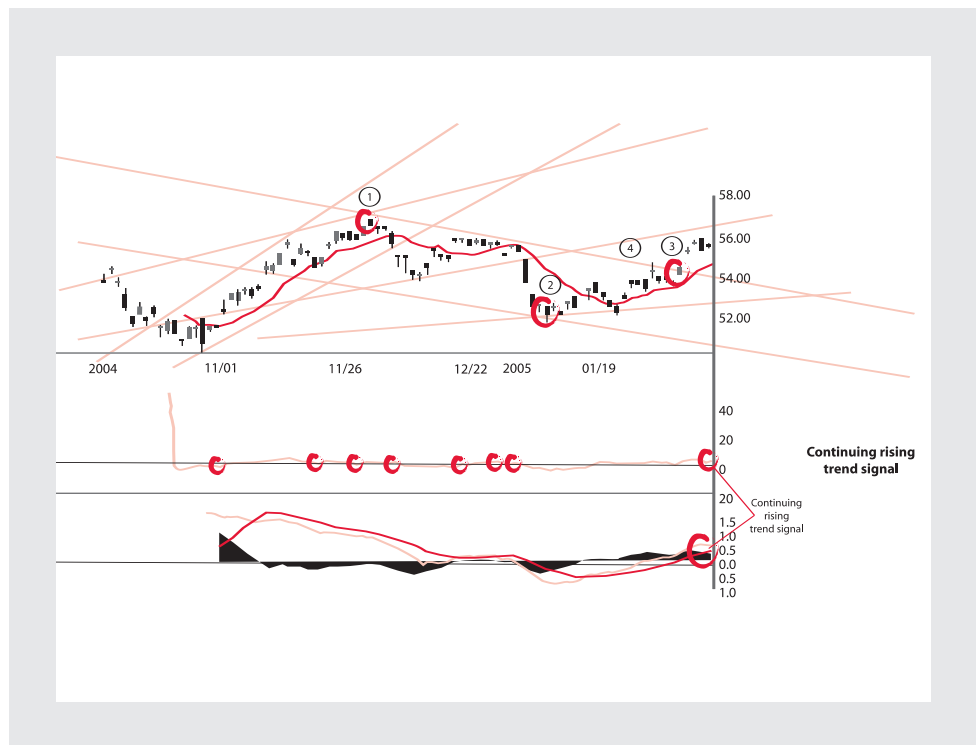
but surely moving along an upward trend since. This climb was put the test on February 4, when prices broke through the upper trendline of the former decline, reaching a daily close of US\$54.35 (denoted as “3”). At this time, prices continue to move within the reverse pennant of the upward trend (denoted as “4”), and the lower chart indicators (momentum and MACD) are still forecasting upward movement.

With a breakout already accomplished and both key corollaries showing buy signals, it is reasonable to expect FXI’s rally to continue for some time to come. Indeed, if one looks at this fledgling’s progress by month, the pattern of one strong month followed by two modest declining months finishing out at the 38.2% retracement looks both repeatable and quite bankable. A good initial entry point into this new asset should simply be to buy shares in the ETF itself.

**Buy China 25 (FXI:NYSE) below US\$57.50, with a growth target of US\$62.92 (21%) over the next 12 months.**

### Pain and pleasure

Now, please understand that while I think this asset’s price will move up, I do not expect that move to be a smooth one. As I mentioned earlier, China’s got troubles galore, and pure long investors may be dining on digestive aids for the duration of the play.



There are several ways to deal with this expected volatility. For those who only have level-one trading accounts, the solution is *Taipan's* usual -20% trailing stop. I strongly suggest that those of you who use this technique keep a close eye on the FXI's successive highs and move your stop up accordingly. Otherwise, you could find yourself stopped out prematurely.

The second method is a bit more sophisticated. It would be to purchase a series of consecutive long-dated out-of-the-money puts on the primary stock position. Should the market move against your primary position, this hedge will increase rapidly enough in value to cover losses up to 20% without taking you out of the play.

**Buy one FXI August 50 Put contract (FXI TJ) at or under US\$1.00 (US\$100 per contract) for every 100 shares of FXI you purchase. The options contracts should represent approximately 2% of the cash invested in FXI stock. If the FXI loses US\$5.00 over the next seven months, these puts will**

**increase to US\$2.40 (US\$240 per contract), limiting the losses on your FXI long position.**

I will offer a pricing update online at [www.taipanonline.com](http://www.taipanonline.com) on the day this issue posts to the website, and will follow both positions there and in the monthly print newsletter.

There is one final thing you should be aware of concerning this ETF. As I have said repeatedly, it will be quite volatile. But that volatility is not merely a threat to be defended against. It is also a free-standing opportunity in itself.

Over the next few months, I will focus on a series of call and put options plays in my regular *Trending East* column in *WaveStrength Market Report* (available for free to all *Taipan* subscribers at [www.wavestrength.com](http://www.wavestrength.com)) that will capitalize on these rapid movements. I expect these volatility-based plays to last no more than 12 trading days on average and to net between 25% and 75% gains per play. ■

## Log on... tune in... download!

### *A battered stock poised for revival, thanks to the "iPod generation"*



Martin Denholm

This may be the ultimate contrarian play. But I believe it's one that could also bring you a serious investment reward.

I don't believe in sugarcoating recommendations. If you take a look at the five-year chart of **RealNetworks Inc (RNWK:NASDAQ)**, you'll see it's pretty darn ugly. From the dizzy heights of US\$263.75 on April 13, 1999, the stock has plummeted all the way

down to US\$6.62 today.

But that's one of the reasons why I think things are set for a turnaround. After analyzing the chart, you're left with the question: "How much downside is left?" Answer: very little, if any.

That's obviously not the sole reason for recommending RealNetworks—far from it. The company is an industry leader in what has become one of the most explosive, fastest-growing fields: the online music subscription business.

### *Apple is sweet... but save some sugar for RealNetworks*

Just take a look at Apple Computer's incredible performance over the past year thanks to the stunning success of its iPod portable music players and the associated iTunes music network.

While these devices continue to be enormously popular, many folks don't know there are actually viable alternatives to the iPod. In fact, the reason for the sharp decline of RealNetworks and others like it is arguably not so much what RealNetworks *didn't* do, but rather what Apple *did* do in terms of an aggressive marketing campaign, which featured Irish band U2.

Apple certainly nailed its strategy and launched itself to the top, but its success has merely proved there is a huge market for online digital music. And this is where RealNetworks is making big strides at very little cost.

### *Bohemian Rhapsody*

With a 40% share of the Internet's music subscription market, RealNetworks' Rhapsody service

*over, please...*

is gaining by leaps and bounds. It was recently voted the "Best Downloadable/Subscription Music Service" at the Billboard Digital Entertainment Awards.

Very quietly—and seemingly effortlessly, because it took hardly any marketing or huge cash injections—RealNetworks doubled its Rhapsody subscriber base to 700,000 by the end of 2004. Each of those customers pays US\$9.95 per month for unlimited access to an online jukebox that has swelled to over 900,000 songs. That's huge growth from December 2001, when Rhapsody launched with just 80,000 songs.

Compare that to Apple's iTunes, which charges 99 cents to buy a song, and you're talking a total cost of US\$990 to fill an iPod mini (with space for 1,000 songs) or a US\$9,900 outlay to fill a regular iPod (with room for 10,000 tunes).

Given the enormous demand for portable music players these days, you can see why RealNetworks' CEO Rob Glaser recently told Barron's that there is "tremendous opportunity" in the company's business.

RealNetworks finished 2004 with a boatload of cash—US\$363.6 million (US\$2.14 per share)—on annual revenues that soared 32% over 2003 to US\$266.7 million. That's not bad for a company whose stock has taken such a beating. Moreover, the 34% sales growth during the last quarter was over five times higher than the average of its industry rivals, thanks largely to the rapid growth of Rhapsody subscribers.

### ***Anything but a micro-settlement expected from Microsoft***

There could be much more money on the way, too, if RealNetworks prevails in a major lawsuit against Microsoft. Even if you're not familiar with RealNetworks' Rhapsody service, you've probably heard of the company's Real Player, which you can download for free on the Internet.

Once the leading media player in the business with over 200 million free versions downloaded, Real Player today faces stiff competition, primarily from Microsoft's Windows Media Player. But it's competition that RealNetworks alleges is unfair because Microsoft packages its Media Player with the rest of its Windows software.

The main reason RealNetworks lost US\$23 million (14 cents per share) in 2004 despite strong revenue growth was because of the US\$11 million in spent on legal costs in the Microsoft case.

On the bright side, a settlement is expected to bring US\$500 million to US\$1 billion. That would be huge. RealNetworks' current market cap is US\$1.1 billion. And the odds would appear to be in RealNetworks' favor, given that Microsoft has already lost a US\$600 million European Union antitrust lawsuit pertaining to its Media Player.

In addition, top-end company projections call for sales to grow 20% to US\$320 million in 2005.

### ***Big profits in a burgeoning industry... but is RealNetworks ready to be gobbled?***

Despite its healthy cash position, word on the Street is that RealNetworks could be a ripe buyout candidate for a rich media or technology heavyweight.

And although CEO Rob Glaser, who owns almost a third of the company's stock, says he would rebuff any overtures, it might be difficult for him to resist if a fat offer rolled across his desk.

For now, however, both he and many economists see great potential in the online music subscription business. And far from conceding the fight to Steve Jobs and the Apple crew, many more believe the fight is just getting started and that the industry is primed to take off like satellite radio did a couple of years ago.

With 230 online music stores in operation, digital music sales in the US and Europe hit US\$330 million in 2004 as fans downloaded ten times more songs (200 million) than in 2003. The International Federation of the Phonographic Industry expects sales to double again this year. And current projections call for that figure to hit US\$2 billion by the end of the decade. RealNetworks hopes to capitalize on the explosion by introducing a digital MP3 player of its own later this year.

That's a big turnaround for an industry that suffered so much from illegal downloading. But with one million songs now available for downloading legally, quickly, easily and at reasonable prices, plus stiffer penalties for offenders, the market is changing. Digital music sales now account for 1% to 2% of record company revenues. If current trends con-

**There could be much more money on the way, too, if RealNetworks prevails in a major lawsuit against Microsoft.**

tinue, that figure could shoot to 25% by the end of the decade.

### Not just a one-trick pony

Subscription services account for over three quarters of RealNetworks' revenues, but that money doesn't just come from music services. The company also offers online video game subscriptions, a movie deal with Starz cable channel, and a media software division.

In early February, RealNetworks expanded its coverage further by cutting a lucrative deal with Nokia, the world's leading mobile phone maker. This will bring RealAudio and RealVideo technology to Nokia's phones and expose RealNetworks' digital media services to millions of Nokia users worldwide.

In June 2005, RealNetworks and Comcast, America's largest broadband provider, will launch a service to bring subscription-based Rhapsody RadioPlus to Comcast's 6.5 million high-speed broadband customers. This will give listeners access to 90 radio stations—and the capability to build their own customized stations.

RealNetworks has lately also announced a partnership with Sonos Inc.'s wireless Digital Music System, which allows users to remotely control the music in their home. This is RealNetworks' ninth such Rhapsody-on-demand deal with outside consumer electronics companies.

In Europe, RealNetworks recently expanded its video games business by reaching deals with Britain's Telewest ISP, RTL.de in Germany and Free in France for its top-ranked RealArcade downloadable games service.

So why pay a fortune for shares of one of the digital music industry's "big boys" whose upside is limited anyway? RealNetworks is a cheaper and potentially more lucrative investment. If you're still skeptical, take comfort in the fact that insiders own 63% of RealNetworks shares. That shows they're confident in the company's future prospects. So am I. And you should be, too. A few bucks buys you a piece of an industry leader whose business could be set to hit the big time.

**Buy RealNetworks (RNWK:NASDAQ) under US\$7.20. ■**

## Gold: A swift breakdown, or a slow and painful death?



Sara Nunnally

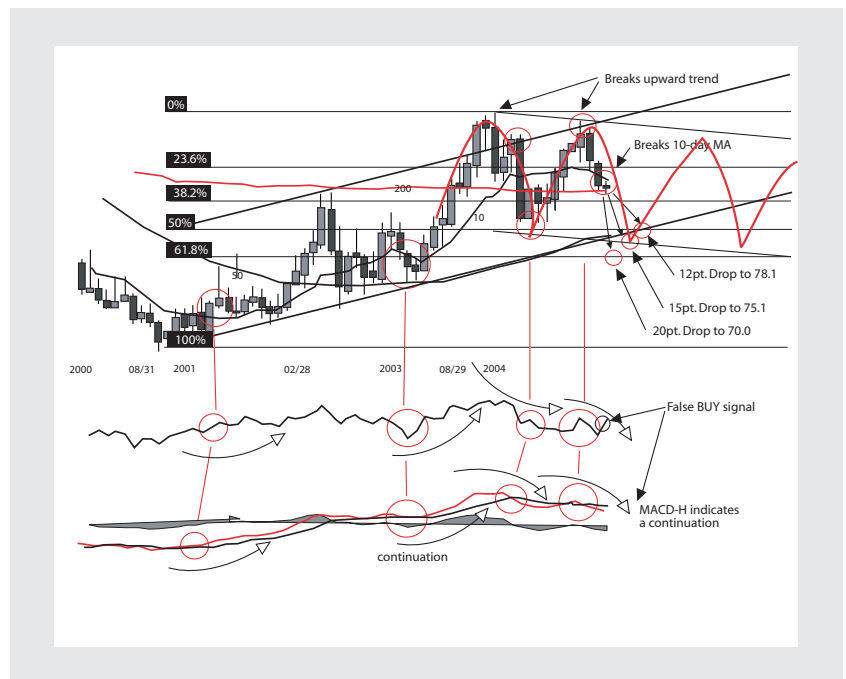
The Gold Bugs out there are probably a little on edge. For them, gold trumps all, and to see those slimy little green-backs pulling themselves back from the brink is like a slap in the face.

But you know, actual Gold Bugs make up only the minority of gold

investors. Most recent investors got in for the ride when gold was on the rise, fair-weather friends out to stuff their pockets with profits and ready to get back out when the wind turns.

Well, folks, the wind is turning.

The G-7 is now considering tapping into the IMF's gold reserves to help fund a plan to alleviate debt in Third World countries. The dollar is gaining strength. When gold wavers, investors start to turn away.



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When it drops, they run.

Look at a five-year chart of the Philadelphia Gold and Silver Sector (XAU) index and you'll see a double-top formation: two sharp peaks touching the index's 52-week high of US\$111.50.

Though these peaks are the culmination of a run-up from lows back in late 2000 and early 2001, they've clearly broken trend. Both peaks have topped the upper trendline, and the second peak's high is below that of the first.

Momentum tells us that the Gold Bugs are hoping this blip can sustain the upward trend.

It won't.

Our chart indicates the start of a downward trend. MACD-H crosses only briefly—a continuation signal. XAU will maintain its downward slope.

Our only question is, "How slippery is this slope?"

The downward trend shows the index arcing down in regular waves, dropping to at least

US\$78.06 and possibly US\$75.13 before bouncing off the bottom trendline. But the double-top formation could send the XAU plummeting back to the beginning of its upward climb at US\$45.

We'll start conservatively. **Buy XAU June 90 Puts (XAU RR) between US\$5.80 and US\$6.50.** If the XAU hits US\$78 in the next 100 days, these puts will increase from US\$5.80 to US\$12.00... good for a 106% gainer.

And if the XAU continues to drop, we'll jump in again at a later date.

Now, we're not saying this ride will be as smooth as the bunny hill. There's an interesting node on our chart where the 38.2% retracement line intersects with a line extended from the two previous bottoms. This might stall XAU's decline. We think it will continue its drop through the retracement line, but should this node affect our play we'll be sure to let you know. ■

## Bulletin board bargains



Alex Chinn

As a general practice I try to avoid the bulletin boards. Over-the-counter (OTC) stocks are susceptible to manipulation and are often the domain of penny-stock merchants looking to rip off the unwitting. However, there are also some real values and trusted companies on the bulletin boards. Some of these might get included on one of the major stock exchanges in the near future. Here are my two

favorite picks from the pink sheets.

### Goodbye dumb cars

Let me be clear: I *hate* the Smart Car. If you've visited Western Europe in the past decade, then you've inevitably stumbled across the comically tiny auto at some point. These rides actually make the Mini Cooper look like a Hummer. It's not just the size that puts me off, but the proportions of the car seem off and it looks like a mental patient cooked up the design.

But people love these things. Maybe it's that you could parallel park one inside a matchbook, maybe it's that you can get 60 mpg (70 with diesel fuel). Regardless of my contempt for its styling, the Smart Car has proved incredibly popular in Europe. Its

maker, DaimlerChrysler, says that it won't sell them in America until at least 2007.

### Why wait?

Santa Rosa, CA based Zap (ZAPZ) decided not to wait. Zap sells electric-powered vehicles such as ATV's and scooters. Zap has started importing Smart Cars and converting them into models suitable for use in America. It didn't expect an immediate outpouring of support, but it received one nonetheless.

Zap set up a tiny, austere booth at the National Automotive Dealers Association show to promote the Smart Car and, over the course of the show, received US\$37 million in orders! The total number of orders received is now in the US\$40 million range. Zap is working furiously to convert cars quickly enough to meet the unexpected demand.

Over 9,000 customers have signed up on the waiting list already. Zap envisions being able to deliver around 250 cars per week. Before being cited for lack of EPA certification (which it has now received), Zap tried to auction their first converted Smart Cars on eBay... and the top bids reached over US\$30 thousand.

Whether you love 'em or hate 'em, Smart Cars will be spreading all over America in the near future. For the next few years, Zap will be the only one profiting from them. **Buy Zap (ZAPZ:OTC-BB) under US\$4.00.**

## Shoot for the stars

Man may have reached the moon 36 years ago, but in 2005 the space race is *really* starting to heat up. Apparently a lot of billionaires still harbor childhood dreams of being astronauts: Six of the richest men around are funding private space flight companies out of their own pockets.

## Rich boys with expensive toys

Jeff Bezos, founder of Amazon.com, has set up Blue Origin, a space flight company that will transport astronauts and supplies to and from space stations. (At least that's the prevalent theory. Bezos has been tight-lipped about specific plans for Blue Origin once it leaves gravity behind.)

PayPal founder Elon Musk has started SpaceX, which is building low-cost rockets from scratch and aims to make money by lofting satellites into space for governments and large corporations.

John Carmack, founder of I.D. Software, has created Armadillo Aerospace in hopes of launching a manned suborbital vehicle in the next few years.

Most famous so far is SpaceShip One, built by Burt Rutan, which won the Ansari X prize by twice launching into low Earth orbit and returning. Paul Allen funded the whole project. Rutan heads Scaled Composites, which is currently designing space vehicles in both space-plane and rocket form. Scaled Composites is also going to supply the vehicles for Richard Branson's Virgin Galactic, which will transport paying customers to the edge of space for a hefty fee.

Last, but certainly not least, is Robert Bigelow, the man who funded the Ansari X prize and currently funds the US\$50 million America's Space Prize. Bigelow intends to launch space habitats and "orbital resorts" starting in 2010. He certainly hasn't been shy about pulling out his checkbook to promote this vision, so we can't overlook his bold venture.

Carmack, Rutan and Musk are among several space flight companies that recently formed the Personal Spaceflight Federation, which is dedicated to working with Federal regulators to establish safety rules and standards in order to make personal space travel viable. The federation has attracted attention not only from the media but also from NASA, which is now considering the use of commercial space flight companies for resupplying the International Space Station.

## The right investment stuff

So there are six billionaires, each astute and successful in their fields, convinced that private space flight is the business of tomorrow. So far, all evidence seems to agree. After all, long before it even launches its first flight, Virgin Galactic has a huge waiting list of people willing to pay US\$190 thousand for a ride to the edge of the atmosphere. Musk's SpaceX has several contracts to deliver satellites into space for the US government, which believes it can do so for less money than NASA. Unfortunately, all of these companies are privately owned. After all, they are the brainchildren of billionaires who don't need any outside funding to make them work.

There is a publicly traded company that will profit from the privatized space race, however, and it's currently languishing in bulletin-board obscurity.

**SpaceDev (SPDV:OTC-BB)** is no stranger to the space flight business. After all, it provided critical systems to SpaceShip One.

In 2003, SpaceDev won the contract to build the hybrid motor ignition system, electronic controls, fuel casting, main control valve, injectors and fill/dump/vent systems for SpaceShip One.

Clearly SpaceDev did a fine job,

as SpaceShip One twice successfully launched and landed. As the contractor for these flights, SpaceDev is well positioned to handle the majority of similar work from Scaled Composites in the future. While SpaceX does all of its own fabrication work, Armadillo Aerospace and Blue Origin might be next to enlist SpaceDev's services once their respective rockets are closer to completion.

In addition to meeting the specific needs of these space flight companies, SpaceDev is looking to the future of space flight as a whole, creating a wide and varied portfolio of various space-related, low-cost technologies. If even one of these creations has a significant effect on the space flight industry, the monetary implications would be huge. Such products as micro-satellites and improved satellite communications systems are among the items being developed.

## Tested in space, sold in America

SpaceDev is in an ideal situation as the only parts manufacturer whose products have been involved in a successful private launch. Not only pri

**Apparently a lot of billionaires still harbor childhood dreams of being astronauts.**

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vate space companies but even government agencies such as NASA or EADS (Europe's space agency) could very well look to SpaceDev in the near future as space missions become more frequent. Remember, we've just begun our exploration of Mars and Saturn, and American space flight has been put on hold until recently due to the shuttle crash.

There's plenty of money just outside of Earth's atmosphere, and SpaceDev is in great shape to

claim it. Over the past 21 months, revenues have more than doubled to approximately US\$1.2 million, and earnings were finally in the positive in 2004. SpaceDev is a bargain that might well launch in the near future, just like the products it makes. Buy SPDV under US\$2.50.

*Remember, the above-listed symbols are for bulletin board picks. These do not appear on a major American exchange. Contact your broker for information on how to buy SpaceDev and Zap. ■*

## Chile winds, hot profits



Erin Beal

It's no secret that commercial airlines have struggled of late—to say the least. For a while it seemed you couldn't flip through the channels or browse any news website without finding headlines declaring strikes, layoffs, bankruptcies. The big guns like Delta and United were forced to cut pay and benefits in order to compete with the newer, deeply discounted outfits like JetBlue and AirTran. But not even the cheap air-

lines could contend with skyrocketing oil prices, which topped out at a whopping US\$60 a barrel.

But now oil prices are finally easing and many airlines are picking themselves back up. Though many are still risky investments, I've found one undervalued carrier of passengers and cargo that shows solid growth in earnings and revenue... and pays a dividend to boot.

If you've followed my recent *Taipan* recommendations, you know that I am bullish on the growing popularity of emerging markets, especially in Latin America. Readers who followed my suggestion to buy shares of Brazilian steel outfit **Companhia Siderurgica Nacional (SID:NYSE)** and Mexican media company **Grupo Televisa SA de CV (TV:NYSE)** have seen solid gains, with plenty more long-term upside potential.

Though the trend to invest overseas waned in popularity in the past years, falling off 1994's booming highs, money is again flowing out of our borders. In fact, the *Wall Street Journal* recently reported that 75% of the new money invested in mutual funds went to international funds. I've been following these trends, and can officially declare that the boom is on and it's time to jump in.

### Hidden profits below the equator

This month our Latin American investment safari takes us to Chile, home of the strengthening peso and one of the leading airlines on the continent. **Lan Airlines S.A. (LFL:NYSE)**, formerly known as Lan Chile S.A., provides both domestic and international passenger and cargo air services to more than 50 destinations in Chile, Peru, the South Pacific, the Caribbean, Europe and the United States. In fact, Lan Airlines is the main provider of these services in Chile, and one of the largest airlines in the burgeoning Latin American market.

Despite the rough patch that the airline industry has been skidding on, Lan has managed to post solid results, something that cannot be said for many other airlines and couriers. The most recent earnings show a steady 28% increase in revenue and a 159% increase in net income. Passenger and cargo revenue are both edging up nicely.

The most recent monthly traffic report (for January) showed an 18% rise in system passenger traffic and a 22% increase in international passengers. This is the latest in a steady stream of growing traffic reports: December saw a 14.8% rise in overall system traffic, while November added 12.2%.

### Deals abound

How is Lan growing its number of passengers? Simple—it's expanding its services across the board. They started slowly, growing their empire in Chile and the neighboring Latin countries, but have now conquered three US destinations in addition to new additions in Argentina. Just a few weeks ago, the Lan booth caused a stir at New York's travel expo, garnering overwhelming interest in south-of-the-border travel.

A deal that could prove to be Lan's golden ticket to bolstering the bottom line was recently struck with Lufthansa Cargo. A handling agreement between the two companies in both North and South American airports is poised to improve service and efficiency. More importantly for Lan's books, the union will help reduce carrying costs and lead to an increase in net income. Earnings growth for the next quarter is forecast at 25%, with sales growth expected to ring in around 31%.

Lan is attractive fundamentally, with a forward P/E of 14 and a PEG of 0.9, indicating that it is

undervalued. The Lan chart shows a beautiful unwavering uptrend, and all things considered I'd set a US\$55 medium-term price target. Though we're not catching the beginning of the ride, I see plenty more upside potential over the coming quarters, especially if oil prices continue to subside.

**Lan Airlines S.A. (LFL:NYSE) is a buy under US\$40, currently trading at US\$35.40.** Contact: Lan Airlines SA, Avenida Americo Vespucio 901, Renca, Santiago de Chile, tel. 562-687-2525, website [www.lanchile.com](http://www.lanchile.com). ■

## This "dog stock" is ready to explode!



Siu-Yee Ng

This month's company is in a billion-dollar industry few of us think about. And get this: only two publicly traded competitors even come close to offering the same service. I first followed this stock in 2001, when it went public. I recommended it and less than four months later we walked away with a solid 26% gain.

It's time to revisit this dog stock. It's moving again...

Think about this for a minute. Over 62% of US households own at least one pet. The US population of companion animals is approximately 188 million, including about 143 million dogs and cats.

According to the American Pet Products Manufacturers Association (APPMA), there are approximately 65 million pet dogs in the United States alone, and 39% of US households own at least one dog. On average, dog owners spend

US\$263 on veterinary care in the past 12 months.

And there are even more cat lovers out there. There are approximately 77.6 million pet cats in the United States, and 34% of US households own at least one cat. Cat owners spent an average of US\$113 on veterinary care in the past 12 months.

So you see, pets are part of the family—and when they are sick, in most cases money is not an issue. With or without pet insurance, most people will pay the money to make sure their pets live a long, healthy life.

### **WOOF is not a newbie anymore**

Since VCA Antech (WOOF:NASDAQ) went public in 2001, it has proved that it can survive in this competitive market. Unlike many of the companies from the tech bubble that either closed shop or sold their business at a discount, VSA continues to grow. VCA operates the largest network of US pet care facilities. It has laboratories in all 50 states and its animal hospitals are in 34 states. And this

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*over, please...*

growth has been through acquisitions.

On June 1, 2004, VCA merged with National PetCare Centers, Inc. This added another 67 animal hospitals in 11 states.

And on October 1, 2004, VCA acquired Sound Technologies, Inc. This is the nation's largest supplier of ultrasound and digital radiology equipment to the veterinary market.

VCA currently has three operating segments:

Laboratory, Animal Hospital and Corporate. They operate as separate units because they have different products, services and functions. The laboratory segment provides testing services for

veterinarians. The animal hospital segment is what most pet lovers are familiar with. This segment provides veterinary services and sells related retail and pharmaceutical products. Corporate provides sales and administrative support for the other two segments.

**Profit centers**

Laboratory revenue increased US\$4.3 million for the three months ended September 30, 2004, and

US\$17.0 million for the nine months ended September 30, 2004, compared to the same periods in the prior year. Animal Hospital revenue increased US\$36.3 million and US\$70.6 million in the same periods. This isn't bad, especially when you consider that many pet products that once were sold only at veterinary hospitals are now also sold at pet stores like Petsmart and Petco.

Even vaccinations are now given less frequently. To offset this, VCA has placed greater emphasis on high-quality veterinary care and wellness programs, which are more expensive. These trends

have resulted in a decrease in the number of treatments and an increase in the average revenue per treatment.

As I write this, the company has announced that it will report fourth-quarter 2004 results on February 24, 2005. It looks as if the stock is experiencing resistance at US\$20. But there's been increased buying in the past two months, which leads me to expect positive fourth-quarter results. **VCA Antech (WOOF:NASDAQ) is a buy under US\$20.** ■

**Pets are part of the family—and when they are sick, in most cases money is not an issue.**

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