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Abundance of riches!

How our Dynamic Market Theory pinpoints profit opportunities no matter where the market is headed

J. Christoph Amberger

On May 20 at 11:18 A.M.—a day before our editorial deadline for this issue—*Taipan* members who had taken Brad Colburn's longstanding advice to buy shares of Given Imaging (GIVN) found the following alert in their email boxes and on 247profits.com:

> *"Sell your position in* ***Given Imaging (GIVN:NASDAQ)****," Brad advised. "GIVN was in the red yesterday while the rest of Wall Street—for at least part of the day—enjoyed a nice rally. Turns out that a 50-year old man died two weeks after taking one of GIVN's M2A pill-cams. There's no proof yet that the pill actually killed the man, but speculation was enough to send the stock down.*
>
> *"In pre-market, GIVN was trading at US$33.56. As I write, GIVN trades at US$33.04.* ***If you bought GIVN at the original entry price of US$9.55 back in December of 2002, then you're about to bag a 251% profit."***

Indeed, Brad appeared to be on a roll. Just a day before, he had alerted our members to take profits on two other *Taipan* positions:

> *"I want you to sell* **Hexcel Corp. (HXL:NYSE)***," he wrote on May 19. "In the April 2004 issue of* Taipan*, I told you that HXL would be a long-term play based on a series of volume spikes and the company's carbon fiber structure technology. […] As I write, HXL is trading at US$8.58. […] Take advantage of a good thing while we have it. We bought HXL at US$7.40.* ***At the current level of US$8.58 you should be sitting on a 15% gain. Take it. Also, bag your 78% profit in Midway Games (MWY:NYSE).*** *I originally recommended MWY in the March 2004* Taipan *at US$5.16. Yes, Sumner Redstone is still buying. In fact, he recently increased his MWY holdings to more than 50%. He practically owns the company now. […] MWY is feeling some pressure and is trading a little south of US$9.20."*

Yours for the taking

By all measures, taking profits of 251%, 78%, even 15% within two days of each other is nothing to sneeze at. It is especially sweet, however, to make this kind of money in a market that seems flaky at best, erratic at worst.

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Of course, it requires a little bit of commitment on your side: need I point out how important it is for you to take advantage of all that your *Taipan* subscription entitles you to? Like our news portal at www.247profits.com… *Taipan's* Internet presence at www.taipanonline.com… and our daily email alerts?

If you've had the opportunity to follow our daily coverage of the world stock and equity markets, I hope you're beginning to see how *Taipan*'s Dynamic Market Theory translates into profitable systems of investing. And the point of all this is that you, too, can enjoy investing successes like the ones we outline above.

In our view, the secret to profitable investing is quite simple:

Recognize that the stock market is dynamic, not static. Recognize that value is determined at any one point in time by what someone will pay for a stock, more than by any formula of earnings, sales, or "book value."

And develop a system that takes into account any of a number of indicators of actual value and price movement. Then stick to that system.

Surfeit of riches

In a nutshell, this is the essence of the analytical tools and systems our editorial team has developed over the years. Of course, it's not that simple. Because the last step requires knowledge and countless hours of research.

Taipan is a monthly reflection of the whole pragmatic approach we like to call Dynamic Market Theory. Each month I call our "Investors Think Tank" together and we review what's going on in the markets and how we can benefit our readers with profitable advice.

In fact, I challenge each member of our research team to come up with the most profitable idea they see in the whole market and show how it fits in with their particular system. (This has the added benefit of placing our researchers in a competitive position. Each one, of course, wants to be the "star" performer.)

I then take the best that our team has to offer for the month and feature it in our letter, along with the reasoning behind it. But since a monthly bulletin hardly keeps you up-to-date these days, you'll also get our ***247profits e-Dispatch.*** It's written by me, with contributions from all the members of our "Investor's Think Tank."

I consider this daily email alert to be something of an applied laboratory for our Dynamic Market Theory. After all, a theory is just an explanation for a set of facts that has been repeatedly tested and can be used to make predictions about natural—and market!—phenomena.

Each of our editors looks at a different set of facts to arrive at his or her conclusions and recommendations. We refer to these facts as "unique constellations of catalysts." Some are quite complex… such as the *WaveStrength* charting system Adam Lass has developed over the past decade and a half. Others contain hard-won "secrets"—conclusions our editors have arrived at in constant testing.

Take the "Blood in the Streets" Catalyst

Over the 16-plus years we have published *Taipan*, we've experienced our share of global market catastrophes. And following the motto of the late Baron Rothschild to "buy when blood is running red in the streets," we have turned crisis into profits time and time again.

Now, everyone has heard of the "Blood in the Streets" principle. But *Taipan* veteran and *Red Zone Profits* creator Christian DeHaemer has added his own twist to this maxim. He calls it "#4 in the *Red Zone's* '55 Rules of Trading.'"

> *"4. When a disaster occurs in an emerging market country, go to www.ADR.com, find the company that has sold off the most, and buy it."*

On Monday, May 17, we once again had the opportunity to put our theory to the test: Indian stocks fell by as much as 17.5% that day after India's communist parties decided not to join newly elected Sonia Gandhi's Congress-led coalition. India's market valuation lost as much as US$40 billion in a single day. Both the Indian rupee and government bonds fell sharply, forcing

the Reserve Bank of India to assure investors it would intervene to safeguard the banking system and foreign exchange markets. The Bombay Stock Exchange and National Stock Exchange suspended trade twice in the morning.

An international crisis like this doesn't go by unnoticed and unexploited at the *Taipan* headquarters. Ian Cooper, for one, advised his *Red Zone VIP* traders:

> *"With blood in the streets after the plunge, we're recommending that you buy the two stocks that sold off the most in the melee, namely* ***HDFC Bank (HDB:NYSE) and Satyam Computers Services (SAY:NYSE).*** *Both should bounce back following the selloff. HDFC is a speculative buy under US$24. SAY is a speculative buy under US$18.25."*

Only a day later, it was time to take turnaround profits off the table:

HDB: bought at US$20.80, sold at US$26.90 for 29% gains.

SAY: bought at US$16.73, sold at US$18.40 for 10% gains.

Red Zone VIP member Doug S. wrote in to say: "Did great with this trade. In for 1,000 shares at US$21,116.45, out at US$26,244, gain of US$5,127.55 in 24 hours. Keep them coming!"

With the Iraq hand-over looming, the presidential elections warming up, and gold and the dollar caught in a highly speculative trading vortex, you can count on dozens of these dynamic opportunities to materialize the next few weeks. In this issue alone, we have half a dozen medium-term plays prepared for you. This will allow you to explore what other aces our editors have up their sleeves. But to capture the whole potential of what our Dynamic Market Theory has to offer, I urge you to take advantage of at least our free daily email alert. (You can sign up for it at www.247profits.com, day or night.) ■

Big-screen profits

Make 145% on this LCD TV flat screen maker

Chris DeHaemer

My 2000 Chrysler Town and Country, all wheel drive, LXI, leather, surround sound, giddy-up, was a bit too tame for my tastizzol. So, I added some flavor by dropping in some flat screen LCD's in the headrests.

Now my brood can watch the Wiggles in comfort and style as we cruise the highbrow boulevard of IKEA Place in search of that next accoutrement of taste and decorum that the three-year-old set just can't live without.

But as I was tooling around in search of truth, apple pie and the American way, I was struck by the fact that four LDC screens flashing and pinging Playstation and the latest Disney musical just wasn't enough. I needed more bling to go with my 20-inch spinners and low-profile aqua-treads.

It was a search then, a quest for more bling, that led me to the place where all gizmos are created…

Beware the Middle Kingdom

Strange things are afoot in the Middle Kingdom. China has hit the blacklist. Myth has it that its reported 9.8% growth is too much. It needs to slow things down a bit. Make money tighter, avoid imbalances, bad debt and inflation.

This idea, what I like to call the Great China Blowout, has recently let the air out of the Shanghai Composite Index. Indeed, it has fallen from 1,783 to 1,549—a 15% drop in six weeks.

This GCBO idea coupled with a now resolved presidential election has dropped the Taiwan index from 7,135 to 5,815 in the last year—a 22% decline. I'm not sure if that rates a "low" in the buy low theory, but it isn't a "high."

You see, Taiwan is an independent country in all respects with the exception that it can't declare itself an independent country. Its number one trading partner is China, the only country that cares about whether Taiwan is part of it or not. Every couple of

over, please…

years a new election in Taiwan brings up the subject of independence. China gets mad and tells Taiwan that it is a part of China. The US tells China not to invade. The new leader of Taiwan gets elected based partly on bashing China and then tells China that it likes the status quo.

Today, President Chen Shui-bian packed his inauguration speech with conciliatory language aimed at soothing Beijing and assuring the United States that he isn't a reckless leader seeking to spark a war with his communist neighbor. Clearly this marks a good time to buy Taiwanese stocks.

LCD

Now I know you're wondering what flat-screen LCD monitors, ill winds from China and the ever-unresolved independence issue in Taiwan have in common. Well, a PEG ratio of 0.48 for starters.

For newbies out there, a price-to-earnings growth ratio below 1.0 means that earnings are growing faster than the share price. This is good. The closer you get to zero, the better. I scanned 22 companies with a PEG ratio of less than 0.50 and with revenue over US$100 million.

I found two companies that look like great buys, both related to China. I'll tell you about the first one today.

Buying growth on the cheap: AU Optronics Corp. (AUO:NYSE)

On April 27, Taiwan's AU Optronics Corp. (formerly ACER), the number-three maker of flat-panel display screens worldwide, beat forecasts with a 65% surge in quarterly profits and a 6,980% rise year over year.

Revenues jumped to US$1.252 billion in March 2004 from US$999 million in December 2003. That's five quarters in a row of substantial sequential growth. A year ago they reported US$526 million in revenue.

EPS came in at US$0.82 for March 2004, compared to US$0.55 in December 2003 and US$0.1 in March 2003. That's a good year. Net earnings for the year ending March 2004 were US$808 million, compared to US$461 million in 2003. The growth was due to strong demand for laptops and monitors.

The stock had an equally impressive run, going from US$5 to US$30 before selling off back to US$20, where it is today.

On a T/A basis the chart has pulled back to its long-term trendline and looks like it will bounce at these levels.

A flat panel in every pot

AU has forecast that it will more than double its 2004 net profit, partly betting on a nascent market for big, flat-screen televisions. Revenue from TV screens yields a rich profit margin of around 30%, which would make up around 10% to 15% of AU's total for 2004, compared to 5.7% in the first quarter of this year.

AU opened a new plant using advanced production technology at the end of 2003, providing fresh capacity to meet booming demand for LCD TV's. As more capacity comes out, there will be some pricing pressure. But this shouldn't occur for at least a couple of quarters, as the LCD TV market won't really take off until the fall. As an aside, they make flat screens up to 46 inches.

LCD panels to grow 56%

The fun is just getting started according to the Electronic Components, Assemblies & Materials Association, which declared that monthly orders of all components were still on the rise for the ninth consecutive month during April.

March sales rose 4.4% from February. Other, more staid bureaucrats at the Federal Reserve Board said US electronics and computer production increased 1.1% between February and March. Market researchers at IDC predicted sales of LCD panels would grow 56% this year to reach US$37 billion in sales.

Capex boom

Things are looking so good at AU Optronics that they plan to sell 300 million shares as American Depository Reciepts (ADR's, 10-to-1

ratio) for an estimated US$664.9 million. I believe this 10% dilution is priced in.

The funds will partially cover new sixth- and seventh-generation plants at the Industrial Park in Taichung (central Taiwan) over the next five years. The first of these will start production in Q1 2005.

The most remarkable thing is the value. AU Optronics has a P/E of 11 and a forward P/E of 6.6. They also have a dividend yield of 0.57%. This isn't a small company. Its current market cap is 8.7 billion with 425 million shares outstanding and 300 million in the float.

You can compare them to Taiwan Semiconductor (TSM:NYSE), which has a P/E of 27, a forward P/E of 12 and a PEG ratio of 0.55—a good stock in its own right that reflects the current discount on Taiwanese stocks.

All of these high-growth tech stocks are undervalued, even the more expensive ones like Hitachi Ltd (HIT:NYSE), a Japanese company in a similar business that has a P/E of 147, grew revenue at a miserly 12% last year and didn't grow earnings at all. AU grew earnings a whopping 6,980% and revenue 138% and, again, has a P/E of 11. To reach the same valuation as TSM it would have to go up 145%. To match HIT… ah, I'm not even going to do the math.

Buy AU Optronics under US$24 as soon as you get this, then go to the big-screen store. As I write this, AU is trading at US$20.47. Contact: AU Optronics Corp., I Li-Hsin Road 2, Hsin-Chu 300, Taiwan, email info@auo.com, website www.auo.com. ■

Down is good

There is still a path to profits as gold and the S&P's lock-step march leads both substantially lower

Adam Lass

Last month I led off my column by warning that up was not necessarily a good thing so far as stock markets are concerned. My point was twofold: first, that by definition a higher market meant that more money was at risk. Second was that steep rallies like the one we've just witnessed frequently encourage an excess of blind trust in their continuation.

This month I'd like to explore the converse of that concept: down is not necessarily bad. A falling market tends to make investors wary of stupid ideas. Indeed, where a rising market can cloak a lousy business plan, a falling market can make decent books and inventive concepts shine like diamonds in mud.

But it is the technical options trader who has the most to gain from a falling market. On the options side of things, increasing volatility boosts the bang for your buck (a concept that I will let Bryan Bottarelli explain in more detail in his follow-on article). From my point of view, a market that is moving back through recently covered ground offers a plethora of clearly visible support and resistance nodes, a treasure trove of information compared to the paucity of guidance offered by a market that is extending new highs.

More danger and less risk

Looking at the S&P 500 last month, I noted that the index was resting at the bottom of the rising trend… and warned that this was the moment of maximum risk because many investors were calling it a buying opportunity for American stocks, regardless of their quality or the economic reality.

Now we are past that moment, and events on the ground are indeed as "bad" as I feared they might be. Rather than providing a pivot into the next rising cycle, the pennant point created by the bottom line of the rising trend and the Fibonacci 38.2% retracement became an unbeatable resistance node, yielding the third red monthly candlestick in a row.

More importantly, that third glyph (representing May's action to date) sits both below the old trendline and well within the arc formed by the last eight months' action. The probability that the S&P will regain the rising trend is steadily decreasing, while the chances that it will continue within this arc are now quite good.

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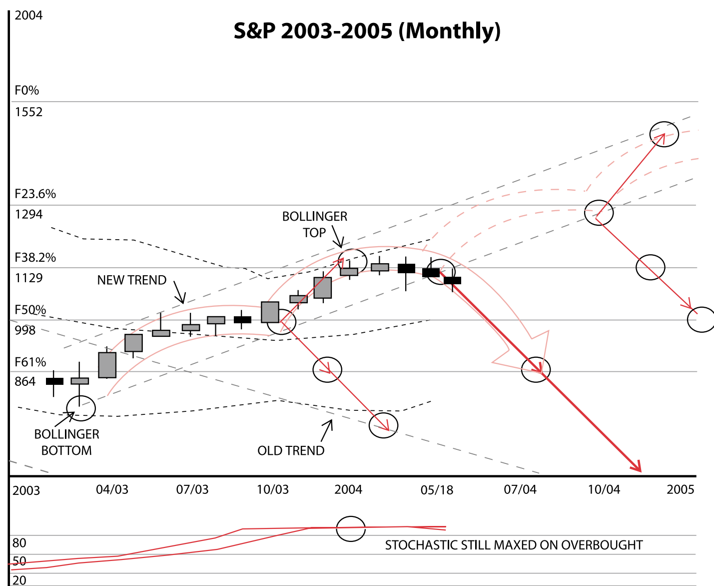


the 61.8% marker at the same moment that it intersects the bottom Bollinger band, rendering 864 by late September or early November an attractive node that must be respected by anyone managing an active portfolio.

This conclusion is bolstered by both the Bollinger cycle as well as the slow stochastic study, which, despite three months of retrenchment, is still registering well into the overbought range between 80 and 100.

Now some might say that there are more reasonable alternatives to options in a market preparing to shift dramatically to the downside. Two that are frequently mentioned are either a move to simple cash or simpler gold. Unfortunately, there are lurking dangers for both that render them unusually unsuitable for protective purposes at this juncture.

Chills and thrills

Now it gets scary for stock investors and really quite thrilling for put options holders. The next few months' action looks to be quite steep and will appear as a sudden collapse to the unwary (who will undoubtedly seek to put a news event at its root—bad news indeed for officeholders who, in reality, have little if any real control over the factors driving this drop).

The next likely resting point for the S&P will be the support node at the confluence of the Fibonacci 50% retracement and the 20-month moving average (which provides the central driver for 3-band Bollinger calculations), 30 to 90 days out at 998.

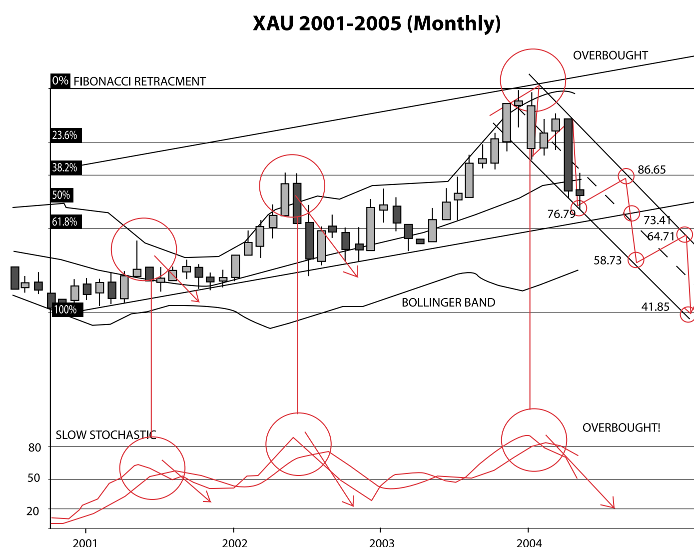
This node is a peculiar one: some theories peg it as a possible 180°-turnaround point. But while I have seen this happen more than once, it is not the norm, and most analysts place more faith in the Fibonacci 61.8% retracement line.

An attractive proposition

In this particular study, I note that our falling arc may very well meet

A double-edged shield

The source of the dangers to these alternate assets is inflation, or rather, the things investors have done and will do to protect themselves from it. For the past several months, both the US central bank and the US Treasury department have done



their best to encourage a diminishment in the dollar via printing, increased circulation, historically low rates and substantial jawboning. These policies have led to the recovery so necessary for the current administration's reelection.

But the fear of inflation inherent in these actions drove a number of investors into gold earlier rather than later. The result: gold and the senior metal producers of the XAU climbed in lockstep with the S&P.

Now, with actual inflation looming as the most important factor of the next 18 to 36 months, neither gold nor dollars nor Treasury bonds look to be an adequate shelter for a declining market. In fact, my charts indicate that we may very well see all four asset classes decline simultaneously. Should this manifold collapse come to pass, a selection of long- and short-term puts against entire groups will be the only practical method of managing wealth.

Timing is everything

However, you should not purchase puts across the board, as there are some rather interesting twists ahead, timing-wise. For the next 20 to 60 days, you can expect to see considerable oscillation in the XAU. The upper parameters of this action will be the Fibonacci 38.2% line at 86.65. The lower boundary will be the 50% marker at 76.79. Once the index pinballs its way to the top line of the falling trend, you can expect another dramatic one-month price drop to follow. Date-wise, I am looking for September, price-wise I expect a bottom around 58.73.

Again, both ends of this prediction are captured nicely in the Bollinger and slow stochastic studies, which show that despite gold's relative price decline, it has not hit any bottom boundaries. Indeed, it is still showing some signs of being overbought.

The S&P's rotting phase is over

The current SPX chart offers sizable downside trading opportunities that gold does not

Bryan Bottarelli

Before I begin, let's take a moment to review our *Taipan* commentary from the last four months. In February's column, Adam concluded that the S&P 500 was on track to match 2003's gains, possibly as soon as June 2004. We targeted a conservative move to SPX 1,315 and played SPX June 1,175 Calls (SPT FO) for US$23.50.

In March, Adam gave you evidence (scientific and otherwise) that the S&P 500 would rise another 200 points, targeting 1,455 by early summer. Again, we reiterated our June 1,175 Calls. But in April, we began to see signs of the rally ending (primarily due to horrific acts of terrorism overseas). As a protective measure, we added SPX June 900 Puts (SXB RT) to our basket in case of an SPX drop to 1,000, 950, or even 900.

In May, Adam noted that SPX chart-watchers found the index at the point of maximum risk, saying that the S&P's recent gains held the key to its own failure. The resulting price movement was a complete stall, as we witnessed the major indices grind to a sudden and dramatic halt.

Quicksand investing

Weeks passed where the SPX moved neither higher or lower. Of course, neither our maximum upside nor downside target of 1,455 and 900 was attained, which has subjected our options plays to deterioration in value. As I write, both trade for nominal value, rendering this play worthless (unless we witness a dramatic upside or downside event in the next 2 to 3 weeks).

This frustrating stall has forced us to look to other indices for substantial price movement, which is why we've included a potential opportunity on the XAU gold and silver index. It would appear that the XAU is primed for a drop—which would make buying XAU puts a nice play at current levels. And since the move is down, your potential gains could make up for our loss on the SPX.

You see, the primary pricing vehicle governing options premiums is volatility (commonly referred to as the "fear gauge"). As a general rule, volatility—which is measured on the CBOE under the symbol VIX—is ***inversely correlated*** to the market.

That is, if the market is going up, the VIX moves down as broad-based fear grows less and less. On the flipside, the VIX goes up when the markets move down—as fear becomes more and more prevalent in the marketplace.

As volatility (driven by fear) rises, so do options premiums. This is why Adam and I prefer playing put options in a downside market over call options in an upside market. With puts, your profit potential increases at a more dramatic rate.

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XAU booby-trap

This downside pricing power could soon be exhibited on the XAU. Looking at Adam's XAU chart, it appears as if we could soon see a move from the $86 level down to the mid $70's. But a closer look reveals a red flashing warning sign. Like the S&P, the XAU first enters a premium-eating stalling pattern.

Although the parameters for a fall are in place, buying XAU puts doesn't work right now. In 60 days we could be in business. But right now, steer clear of the XAU and focus on the S&P. After all, the S&P has finally broken out if its recent trading range—and will soon witness a dramatic fall unlike anything we've seen thus far in 2004.

Make a note: The S&P's stale trading range has finally ended

Now that it's clear that the S&P will fall, it's time to revisit the thesis of buying SPX puts for your portfolio. Specifically, I'm looking at the SPX August 1,100 Puts (SPT TT), which currently trade between US$38.00 and $40.00 per contract, and the SPX September 1050 Puts (SPQ UJ), which trade between US$25.00 and $27.00 per contract.

Given the market volatility, I want to ensure you get exact pricing on these newly recommended SPX puts. Therefore, I will be giving our exact "buy" recommendation on the *Taipan* website closer to our publication date. Please stay tuned for updates via the *247profits e-Dispatch* and our daily *WaveStrength Market Report* on this important recommendation.

Since timing of index options trading is so important, we recommend you join our free daily email service called the *WaveStrength Market Report.* To sign up, simply go to www.wavestrength.net and enter your email address for free membership. ■

Are we jumping headfirst into space exploration? Nah, but we're not afraid to play the hype.

This contract-rich US$1.08 company isn't too shabby

William Colburn

George W. is looking to re-ignite the booster rockets under his space program this summer. He may have hit a temporary snafu with the Iraqi abuse scandal, but a space speech is in the drafting stages.

Here at *Taipan* headquarters, we're excited. Not about the prospect of actual space exploration—the chances of anything meaningful happening in the near future are fairly slim.

We're excited about the press surrounding the new space program. The buzz. When Bush's program kicks into full gear, there'll be a firestorm of activity and quick investment opportunities. And you know *Taipan*... we're never hesitant about jumping on potential profits.

I want you positioned so you can feed off the space buzz earlier than the rest of the pack. I'm recommending shares of **SpaceDev Inc. (SPDV:OTC-BB).**

SPDV is engaged in the conception, design, development, manufacture, integration and operation of space technology systems, products and services. The company is focused on the commercial development of low-cost micro-satellites, nano-satellites and related subsystems, and hybrid rocket propulsion, as well as the associated technical services to government, aerospace companies and other commercial enterprises.

Its products and solutions are sold directly to these customers and include sophisticated micro- and nano-satellites, hybrid rocket-based orbital maneuvering and orbital transfer vehicles (MTV's) and safe sub-orbital and orbital hybrid rocket-based propulsion systems. SPDV is also developing commercial hybrid rocket motors and small high-performance space vehicles and subsystems.

If you're a longtime *Taipan* subscriber, you may

remember hearing about SPDV in 2001. A lot of things have changed in three years. SPDV has amassed a juicy list of clients, including the Missile Defense Agency and the Air Force Research Laboratory.

Last year, SpaceDev was awarded an exclusive follow-on contract to provide the hybrid rocket motor systems and components for SpaceShipOne, a space shuttle that could be capable of taking regular Joes into space. The U.S. House of Representatives has already passed legislation that could result in streamlined licensing of private manned space flights.

The total contract value is estimated at US$429,000. Approximately US$106,000 of revenue was realized in the three months ending March 31, 2004, with approximately US$63,000 from engineering change orders and the remaining US$43,000 from the contract.

In a test last month, SPDV successfully propelled SpaceShipOne on its second manned flight, achieving a higher speed and altitude.

Think it gets better than that? You bet…

The CEO of SPDV was invited to speak at a public hearing for Bush's "Commission on Moon, Mars, and Beyond" in California last month. I don't know about you, but I'm seeing big things with the president's attention and the new progress on SpaceShipOne.

In addition to the SpaceShipOne contract, SPDV is starting its own financial buzz. Shortly before this issue went to print, SPDV released Q1 earnings.

Profit from operations was US$12,000 for the first quarter of 2004, compared to a loss from operations of US$364,000 for the same three-month period in 2003 and a loss from operations of US$12,000 for the fourth quarter of 2003.

For the three months ending March 31, 2004, revenue increased 90.4% to US$1,015,000, compared to US$533,000 in the same period of 2003. Revenue grew 12.5% compared to the fourth quarter of 2003.

EBITDA increased US$334,000 to US$28,000 for the quarter, compared to EBITDA of minus US$306,000 for the same period in 2003 and US$2,000 in the fourth quarter of 2003.

These earnings continued a streak of success. Q1 marked the second consecutive quarter for positive cash flow, the fourth consecutive quarter for cash flow improvement, and the fifth consecutive quarter for revenue growth. Management is expecting this trend to continue for the rest of the year. I like it when management is bullish on the company. But I love it when that bullish stance is well deserved.

In anticipation of SPDV's solid future and the chance to take a big profit when the space program gets rolling, I'd like you to buy SPDV at current levels. As of this writing, the stock trades for US$1.08. **Buy anywhere up to US$2.00.** ■

Pent up demand = profit opportunity

Ian Cooper

While Q1 2004 ended with a whimper over expectations of a poor jobs report, no one expected to see payrolls surge by 308,000 jobs in March, tripling forecasts and bettering even the most optimistic guesses. But although the strong jobs data could be a boon for consumer confidence and spending, skeptical investors are likely to remain on the sidelines waiting for confirmation and hoping that the FBI terror warnings are just more hot air.

Increased consumer spending would be great especially for furniture retailers, who will benefit from pent-up demand for home furnishings after all the refinancing. It doesn't hurt that today's featured company recently saw its CFO buying shares in his own company.

The Rowe Companies (ROW:AMEX)

If you're not already familiar with ROW, the company makes upholstered and leather sofas, love seats and chairs, supplying them to more than 1,200 retailers through its Storehouse and Rowe Furniture subsidiaries. Rowe Furniture serves the middle and upper middle market in the United States. Storehouse is a lifestyle home furnishings business with 61 retail stores.

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Thanks to a 24% increase in the Storehouse unit, net earnings for Q1 2004 came in at US$149,000 or a penny per diluted share, compared to a loss of US$813,000 or six cents per diluted share last year. Net shipments were up by 11% to US$70.7 million from US$63.7 million last year. Gross profit was up by 35.5% from 35.1%.

And the Storehouse retail business had 18.8% same-store sales growth for the third consecutive quarter. Total sales shot up some 23.9%.

Undervalued

On a fundamental basis, ROW is at least 31% undervalued, taking into consideration its US$69.23 million market cap and its US$100.64 million enterprise value. And you can see there's plenty of room for growth once you compare ROW's paltry market cap to that of Ethan Allen's US$1.57 billion and Furniture Brands' US$1.88 billion.

Add to this Furniture Brands International's decision to up guidance for Q1 2004. The company now expects 2004 sales and earnings to be better than previously forecast and Q1 EPS to come in around 55 to 57 cents per diluted share, bettering earlier calls for 50 to 53 cents per diluted share. Furniture Brands strengthened trends at each of its companies through Q4 2003 and January 2004.

ROW's gross margins of 36.2% are greater than the industry average of 34%, price-to-sales is less than 0.3, and the company's CFO just bought 5,000 shares between US$3.69 and US$3.70. There's every reason to be excited.

As for the March 24 furniture sector downgrade on concerns about a slowdown and low-priced upholstery imports, pay no attention. This downgrade allows us to get into ROW on the cheap.

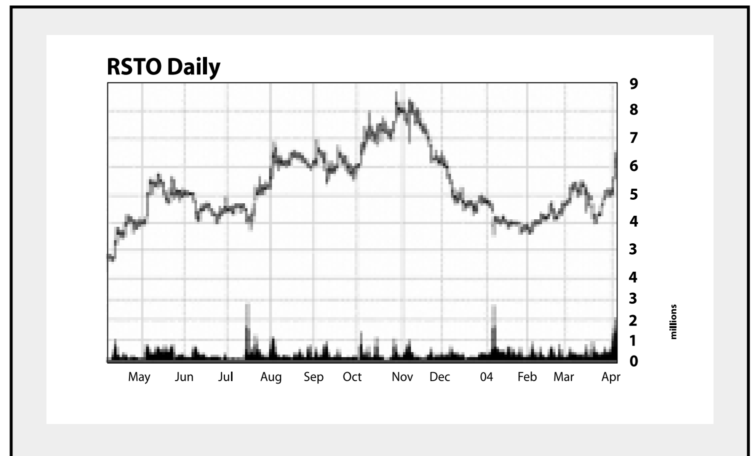
The future's so bright…

Strong home sales, refinancing opportunities, an improving economic climate and pent-up demand are fuelling predictions that US consumers will spend more than US$71 billion on furniture this year. That's a 5.4% increase over 2003 and would be the highest rise in spending since 2000, when furniture sales shot up more than 7%.

Buy shares of The Rowe Companies (ROW:AMEX) under US$6 and enjoy the ride. Our near-term price target is US$10. Contact: 1650 Tysons Boulevard, McLean, VA 22102, tel. 703-847-8670, fax 703-847-8686.

ROW appears to be a good company to own in this market segment, if you are buying just one. But if you'd like to decrease your risk through diversification, the competition is performing well also. And insider buying isn't going to hurt.

Restoration Hardware, Inc. (RSTO:NASDAQ)



Continuing demand for refinancing and furniture, and news that insiders have bought 193,000 shares over the past six months, make this furniture retailer attractive. Undervalued by 4% given its US$197 million market cap and its US$205 million enterprise value, it looks all the more so.

For those of you unfamiliar with the company, RSTO is a specialty retailer of home furnishings and functional and decorative hardware in 31 states. The company also operates a direct-to-customer sales channel that includes both catalog and Internet sales, and a furniture manufacturer by the name of The Michaels Furniture Company, Inc.

For Q4 2003, the company posted net revenue of US$165 million, a 6% improvement over the US$155.2 million posted a year ago. Net income

came in at US$7.9 million from US$9.7 million. Both were in line with prior EPS guidance of 20 to 24 cents per diluted share. Same-store sales were up by 0.7%. And revenue from direct-to-customer sales shot up a whopping 51% to US$26.6 million from US$17.6 million.

As for the company's future, direct-to-customer revenue is expected to increase 30% to 40% in FY 2004 from FY 2003. And RSTO expects to be cash-flow positive for a second consecutive year, with little to no debt on the bottom line.

Regardless of the numbers, we're following the insiders, who seem to know a bit more of the inner workings of RSTO than the average investor. Considering they bought 193,000 shares over the past six months, we'd say something is up and we wouldn't want to miss the boat.

We're issuing a speculative buy on shares of RSTO under US$7. Contact: 15 Koch Road, Suite J, Corte Madera, CA 94925, tel. 415-924-1005, fax 415-927-9133, website: www.restorationhardware.com. ■

Drilling for deep profits as oil production goes domestic

Erin Beale

It's home to brown pelicans, truckloads of party-seeking spring-breakers, and thousands of miles of coral reef. Some 4,800 feet deep in parts, a sprawling canyon rivaling Arizona's majestic wonderland, it also houses vast as-yet-undiscovered reserves of oil and natural gas.

Kudos if you guessed the Gulf of Mexico.

Between Mexico and the southern borders of the United States, some 100 billion barrels of oil and petroleum are estimated to lie in very deep waters and shallow waters alike. Oil production from the area has nearly doubled in the past ten years and is projected to produce levels upwards of 1.8 million barrels per day this year. The Gulf of Mexico has become the second most important reserve after the Persian Gulf.

We've uncovered one of the nation's fastest growing public oil and natural gas companies with strong emphasis on digging and exploration in the Gulf of Mexico—and if you act quickly, you can still buy shares under US$10.00.

Pumping dollars

We all know that gas prices have taken the express elevator to the ceiling lately. In fact, today marked the fourth straight day of record-breaking prices at the pump. The average for regular gas topped US$2. I can't imagine how much it must cost to fill up a gas-guzzling SUV when my little Hyundai sedan is taking upwards of US$20 to top off.

Analysts predict that prices will hit the US$2.50 a gallon range by summer. Demand is kicking into high gear, not only in the US as families pack up the minivan for a good old-fashioned road trip, but also in countries like China and India.

OPEC is threatening to cut oil production. And although President Bush expresses concern about the rising oil prices, he refuses to tap into the US Strategic Petroleum Reserve (SPR).

As Christian DeHaemer wrote earlier this week, "The SPR was originally set up in response to the 1973-74 oil embargo. It is the largest emergency stockpile of government-owned crude oil in the world. And it is almost full. But while politicos call for a halt to further shipments... arguing that the sudden drop in demand would ease gasoline prices... the Administration steadfastly refuses to comply."

Shifting locations

The number-one oil source lies in the Middle East, mainly the Persian Gulf. But as the Iraqi war and Middle Eastern terrorism worsen, there is a

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over, please...

renewed push to focus on domestic production.

Saudi Arabia is having great difficulty tapping reserves from its oilfields, the largest in the world. And just this morning, rebels blew up an oil well in Northern Iraq, sparking a fire that raged for 24 hours.

It's time to look elsewhere to meet our oil and energy demand—and federal incentives are helping to shift focus towards the Gulf of Mexico. The Minerals Management Service, a division of the Interior Department, announced in January that it would suspend royalty collections on successful wells drilled in parts of the Gulf.

The resources are there. The Minerals Management Service recently upped its estimates of "deep shelf" Gulf of Mexico natural gas reserves by a whopping 175%.

Companies are flocking to the Gulf to try their luck. Just last week, the Central Gulf of Mexico Federal Lease Sale in New Orleans drew 83 companies looking to seal the deal on lease blocks.

Fully 30%of domestic oil production emerged from Gulf waters in 2003, and that figure is expected to increase to more than 40% over the next six years. Natural gas production is also on the rise.

Fifty-five bid winner

Magnum Hunter Resources (MHR:NYSE) is one of the premier oil and gas companies in the Gulf of Mexico and its continued rapid growth is making investors sit up and take notice.

A Texas-based energy company, Magnum Hunter owns three gas-collecting systems in Texas, Arkansas and Oklahoma. Because Magnum is an independent company, none of its systems are regulated by the Federal Energy Regulatory Commission (FERC). Additionally, MHR has ownership rights to four additional gas-processing plants scattered throughout the South.

Magnum made headlines at last months's New Orleans bid-off when it won the high bids on fifty-five separate lease blocks in the Gulf of Mexico. Magnum is now the proud owner of over one half of the new blocks awarded, with interests ranging from 40% to 100%. As attention to the area grows and space lessens, Magnum's new blocks put them in good position to dominate oil and gas production in the region.

Additionally, a March announcement from the Magnum camp proclaimed the discovery of six new exploration fields on the shelf of the Gulf.

The basics

Magnum's forward P/E of 11.66 and PEG of 0.87 instantly make the company worth looking into. The company's balance sheet looks good as well: its debt-to-capitalization ratio stood at 82% in December, 1999, and shot down to 60% in 2003. MHR's short-term goal is to reduce the number to 50% by 2004—and its looks like they'll easily succeed.

After participating in 124 new well drills in 2003, recent Q4 numbers show a net income increase of 137% compared to Q4 2002. Fiscal year 2003 showed a 22% revenue increase and a 16% rise in oil and gas production. The company's daily oil and gas production rate has grown 52% since 1996.

MHR shows an impressive 74% increase in revenue growth, further demonstrating that this company is growing—fast. Shares have seen a 52-week increase of more than 76%.

And you can't beat MHR's affordable share price. Shares of Anadarko trade upwards of US$50, while Chevron's go for US$85.50. With shares prices that high, the chance of making impressive gains is greatly diminished.

Magnum Hunter Resources (MHR:NYSE) is the best choice for cashing in on Gulf Mexico oil and gas production, and is a buy under US$10.00

Contact: Brad Davis, Senior Vice President of Capital Markets and Corporate Development, 600 East Las Colinas Boulevard, Suite 1100, Irving, TX 75039, tel. 972-401-0752, fax 972-401-3110, email investorrelations@magnumhunter.com. ■

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