



# TAIPAN

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## Schizoid dichotomy: How to live long and prosper when markets run amuck!

by J. Christoph Amberger



If you believe Alan Greenspan and the Feds, all is going according to plan. The U.S. economy is happily chugging along, fewer people are unemployed, and the eggheads, bean counters, and nit-pickers at the tiller are squabbling over whether there has been an actual recession or not. And the numbers by and large back up our innate predisposition to modest optimism:

Latest Commerce Department figures indicate that the U.S. gross domestic product for Q1 2002 grew at a revised 5.6% annualized clip. Consumer

spending rose at a 3.2% rate in the first quarter, and Uncle Sam and his state and local minions did their share to spread the wealth. But most importantly, at least in my book, after-tax corporate profits rose 0.9% in the first quarter... the biggest gain since Q2 2000.

And it's not only the U.S. economy. The Europeans, too, are reporting that their aggregate economy has turned the corner. And even the Sick Man of Asia appears to be pinching his nurses again: according to data released on June 7, Japan's GDP grew a respectable 1.4% in real terms in the first three months of 2002. That works out to an annualized rise of 5.7%.

There's virtually no inflation, and interest rates continue to hover at 40-year lows. Put all the pieces together and you should end up with a sizeable boom in the markets.

But these just fail to oblige. In fact, the day the Japanese GDP figures were announced, the Nikkei Dow dropped 1.18%. A classic case of "buy the rumor, sell the news"? Make that "sell the rumor, dump the news" and you get the picture...

### **Descent of the market**

If the economy is recovering, you wouldn't know it looking at the markets. In fact, if it were not for select *Taipan* plays, the picture might be bleak indeed.

Over the last couple of weeks (I'm writing on Friday, June 7, the day we're going to print), the Dow Jones Industrial index has shaved a thousand points off its March highs to trade close to 9,500.

Taipans, however, are not facing this drop unprepared: the Q1 rally in the Dow may have run against Bryan Bottarelli's **Dow 100 December 03 LEAPS (ZDK XV)** pick. (You remember, he originally made this recommendation in our December 2002 Forecast Issue, and then reminded you of it again in the May issue of *Taipan*.) In fact, over the last six months, you've had a couple of opportunities to enter this position at the recommended price of between US\$7.50-8.50.

As I write, it's up again... trading between US\$10 and US\$11, a quick

(over, please...)

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**TAIPAN**

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20% gain on what amounts to a “life insurance policy” on the markets...

But what’s ahead? In this issue, I’ve asked Adam Lass, our resident market Pythia, to consult his *WaveStrength*™ oracle... and give you a clearer idea of what lies ahead. Bryan Bottarelli, one of the few analysts with the uncanny ability to translate Adam’s sometimes arcane and always challenging forecasts into hands-on profits, will then “channel” his insights into some handpicked investment vehicles you can use for your personal gain. (It starts on Page 5.)

***The secret Bubble economy***

But profiting from the bucking of the indices is just one strategy to survive the slow-motion nosedive of the 2002 stock markets. One of our most successful strategies this year so far was riding the bubble that continues to inflate in the U.S. and U.K. real-estate markets

Most of our positions in *Taipan’s* Conservative Portfolio were entered in January and July of 2001 and have proven to be nifty little cash generators yielding between 3% and 13% annually in dividends.

*And that’s on top of the equity appreciation.* Here’s the most recent snapshot (as of June 6, 2002):

- **HCN:NYSE:** last dividend payment was US\$0.585 per share. Annual yield 8.35%. Gains (including dividends): 16.95% YTD, 74.77% since entry.
- **HCP:NYSE:** last dividend payment was US\$0.81(!) per share. Annual yield 7.6%. Gains (including dividends): 21.73% YTD, 48.99% since entry.
- **VGSIX:** annual yield 3.31%. Gains: 9.39% YTD, 15.47% since entry.
- And do I need to mention Impac Mortgage Holdings again? Today, **IMH:NYSE** posted yet another record, trading as high as US\$11.65. Including dividends, we’re up 49.63% for the year, and 77.42% since we recommended the stock a year ago.

***Fleeing the faithful***

Since most of our “conservative” plays involve REITs, we tend to be particularly

involved with their underlying engine. Which is the American public’s predisposition to go into debt. And terror or no terror, debt is the only true boom industry in the United States. In 2001, U.S. national income grew by US\$178.6 billion. Debt, on the other hand, increased more than US\$2 trillion—rising more than 10 times faster than income.

Is it entirely coincidental that the increase in debt went hand in hand with the biggest boom in real estate the U.S. has ever seen? You be the judge of that: total home sales hit a record 6.2 million units in 2001, and are now running at an annualized clip of 7 million units... something that has not happened in recent memory. (Up until 1996, sales never exceeded 5 million units.)

You do the math: between January 2000 and December 2002, 20 million units of new and existing housing will have been sold. If each unit involves only three household members, that means more than 60 million American residents were striking their tents and moving... a wave that makes the Great Migration of late antiquity look like a collegiate chess club excursion to rent an X-Files DVD from the campus Blockbuster!

The trend continues unabated: the Mortgage Bankers Association reported yesterday that its Purchase Index jumped 18.9% to a record 414 in the week ended May 31. Housing and housing-related goods and services are now thought to have contributed roughly half of one percentage point to last year’s increase in real GDP... roughly 50% of 2001’s total increase!

The pencil pushers at the Commerce Department reported on June 3 that construction spending rose 0.2% in April to an annualized US\$871.9. Private residential construction even rose 0.7%. All the while, the average amount of equity in a residential property is shrinking at roughly the same clip as the rate of refinancing, which jumped 6% last week as consumers hocked home equity for cash to buy bass fishing boats and jet skis.

***From real assets to bubble***

Curiously enough, unlike the last comparable move back in the late 1970s, the boom is taking place at a time when there is virtually no inflation... which means that real

estate is appreciating independently of its classic real asset role as an inflation hedge!

As long as mortgage rates stay low and the ingenuity of lenders can compensate for rampant appreciation by making debt servicing affordable, this boom may continue for quite a while.

Thus far, lenders have focused on making their services attractive to an extended group of prospects—people their predecessors in the business would have turned up their noses at. You can now buy houses pretty much anywhere in the USA without a penny down. Or borrow your down payment to avoid mortgage insurance.

But that, too, has its limits. Leave it to the Brits—who've had their own property bubble to deal with, with prices rising as much as 20% in a single year!—to come up with the Next Big Thing. Forget 30-year standard mortgages. Make room for the 50-year mortgage!

Actually, that's really nothing new. In Japan, where near-zero interest rates haven't made a dent in the cost of housing, some mortgages cover terms as long as 100 years. You actually never pay off the principal!

For the time being, we recommend you hold on to your shares of **IMH:NYSE**. This real-estate investment trust (REIT), however, plans future stock and bond sales to raise money to meet the rapid growth of its mortgage loan portfolio.

The company expects total assets to exceed US\$5.0 billion by the end of Q4 2002—well ahead of previous estimates. Impac now plans to buy about US\$1 billion worth of mortgage loans to be held in its long-term investment portfolio, after purchasing US\$491.8 million worth of mortgages in the first quarter.

To raise capital, Impac will issue a US\$750 million collateralized mortgage obligation offering in June. (That's securities repackaged from existing mortgage bonds for sale to investors.) Also, the company entered into an agreement with UBS Warburg LLC to periodically sell up to 3,594,082 shares of its common stock.

The inevitable dilution will probably not affect the stock too much, considering this money is paying for an asset.

The question is more fundamental. IMH primarily deals in acquiring, originating, selling and securitizing nonconforming Alt-A mortgage loans... loans that are weighted toward the flaky segment of the market. Any decrease in the real-estate market, any increase in interest rates is likely to negatively affect the core business.

On the other hand, we have just entered the prime real-estate and lending season. We're unwilling to let go prematurely of what so far has been an exceptional ride. But we'd like to define a safety net for our profits. We expect some fluctuation in the stock price over the next couple of days, but will establish a preliminary stop-loss at US\$10.75, which should provide enough leeway for us.

**But mind you: we're not done with this stock yet. If push comes to shove, we'll take our money off the table and buy back later... especially before dividend payments!**

### **Profit updates:**

- Space cowboy **Stratasys (SSYS)**, which we classified as a buy under US\$6.25 in our May 21 e-Dispatch, provided ample opportunity to follow our recommendation on May 29, when it traded as low as US\$6.10. On Monday, June 3, I recommended you put your exit level at US\$7. We took modest 13-15% profits on June 6 as the stock fell back past US\$7.
- On May 24, 2002, Brit Ryle wrote in the e-Dispatch: "Did anyone notice when my February *Taipan* position in **Crown Cork & Seal (CCK:NYSE)** was stopped out for a 100% gain? I thought not. That's weird, in my opinion. Doubling your money in 6 months usually doesn't go unnoticed. But that's what happened when CCK hit US\$10 on May 9. I'm sure if you bought Crown Cork & Seal at US\$5 like I recommended, you'll find something exciting to do with those 'boring' 100% profits."
- A week later, on May 30, the bell tolled for one of Christian DeHaemer's *Taipan* World Investor recommendations: "SAB Joins the High Life: Sell It for a 21% Gain. That's right, book profits of 21% on **SAB**. As always, we will look to get back in when the price is right." (More on that on Page 4!)
- A day later, on May 31, 2002, Ian Cooper decided that enough was as good as a feast. Before 2 P.M., he had posted his action alerts at [www.taipanonline.com](http://www.taipanonline.com) and [www.247profits.com](http://www.247profits.com). His message: Sell **WINK** for 52% profits! "It's time to take 52% profits on *Taipan*'s May issue recommendation of **Wink Communications (WINK:NASDAQ)**. Its recent run-up has been fuelled by continued growth within the interactivity market. While certain catalysts for future growth remain untapped as yet, the chart is looking a bit topky, which may forecast a rapid selloff in the near term. With this in mind, take profits now. We'll look to get back into this play at a later date. Even while the market has been getting its head handed to it, we still nailed 52% in less than two months."

Volatile markets require expert timing to optimize returns. Please make sure you take advantage of all our new media to keep abreast of the latest *Taipan* recommendations. You can either make it a habit to check our websites at [www.taipanonline.com](http://www.taipanonline.com) and at [www.247profits.com](http://www.247profits.com). Or you can let us do the work, simply by subscribing to our free e-letter, the *Taipan* Group's 247profits e-Dispatch.

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- **NEXT ISSUE:** The August issue of *Taipan* (Vol. 15, Number 10) will be available to subscribers only at [www.taipanonline.com](http://www.taipanonline.com) on Monday, July 22, 2002.

# Sony believes this company's patents have value—why doesn't the market? It will soon!



by *Christian DeHaemer*

Here's a company with zero debt, a market cap of US\$119 million, US\$114 million in cash... and they just leased 24 patent rights to Sony for US\$28 million dollars. It's up 39% since May 24—and the run-up is only beginning.

*This company is undervalued by US\$23 million!* And that's just one

stock we expect to pop this summer.

One would think that the highest productivity growth rate in 19 years would put some movement into this market. But as I write this, the Dow is up a miserly 30 points. The Labor Department says that non-farm productivity grew at an annual rate of 8.4% in the first three months of the year. That was the largest rise since the second quarter of 1983.

Despite the market's bearish mood, there is always a stock or segment that will go up. I have uncovered a little-known company that owns the intellectual property that just may save the major media conglomerates from themselves.

## **High-tech magic marker**

Sony recently spent years—and considerable cash—to build a high-tech security code that would protect their compact discs and DVDs from piracy. The new technology tried to stop consumers from copying music onto burnable CDs or their computer hard drives. This, in turn, was meant to stop them from sharing these files with the world on the latest incarnation of Napster, such as Morpheus or MusicCity.

A few days after this technology showed up in the stores, pirates defeated Sony's elaborate disc copy-protection technology. They discovered that by scrawling around the edge of a disk with a magic marker, you could hide the ring of code and your computer or disc burner would simply ignore it. This news spread across the Internet like the proverbial wildfire.

## **InterTrust**

This could be the reason Sony has turned to **InterTrust Technologies Corp. (ITRU:NASDAQ)**, the only pure play in digital rights management (DRM) and trusted computing technologies.

InterTrust has 24 patents for protection against multimedia piracy. Ninety more are pending. What I said at the outset bears repeating: *This company has no debt, a market cap of US\$158 million, US\$114 million in cash and short-term investments, and just leased patents rights to Sony for US\$28 million dol-*

*lars.* So for US\$16 million you get intellectual property worth at least US\$28 million. And it will likely be worth more than that to latecomers such as Disney or AOL Time Warner.

All the big media companies are complaining that CD sales are way down. There is a great deal of fear that piracy will erode their movie and DVD income as well.

Before the Sony news came out, ITRU had built a baseline on the chart at US\$1.25. That's the downside—and our default stop-loss. **ITRU is currently trading at US\$2.25. Get in now before the traders get back from the beach and "discover" this stock.**

## **Nuclear cool-down = 79% profits**

As nuclear tensions between Pakistan and India begin to cool down, we're seeing a decent rally in **ICICI Bank (IBN:NYSE)**. If you bought into my recommendation on January 11 at US\$4.27, you're now up more than 79% as it moves past US\$7.65.

ICICI Bank is the largest non-government owed bank in India. The nuclear war won't happen. In the face of "mutually assured destruction," cooler heads usually prevail. India is on the upswing. IBN will be a net beneficiary. **Continue to hold.**

## **SAB joins the High Life—sell it for a 21% gain**

Loyal Taipans know that I've played **South African Breweries (SAB:London)** five separate times over the past three years. On every occasion, those who have taken my advice have come out winners. This time is no exception. SAB is my prison bitch of investments.

The most recent run-up was fueled by rumors, now confirmed, that SAB would buy Miller Brewing, the makers of such fine pilsner as Miller High Life and MGD.

The US\$5.6 billion deal will make SAB the second largest suds producer in the known world behind Anheuser-Bush (BUD:NYSE). The deal is structured so that SAB takes on US\$2 billion in debt and pays US\$3.6 billion in shares to Philip Morris, the current owner of Miller. The new group will be called SABMiller Plc.

The downside is that SABMiller is seeking approval to issue 170 million new shares. This will cause a 14% dilution of the stock. Moreover, big mergers never work. See AOL Time Warner. Finally, remember the classic Wall Street axiom: "Buy the rumor, sell the news."

In light of these factors and our current 21% gain, I suggest you sell. **That's right, book profits of 21% on SAB. As always, we will look to get back in when the price is right.**

# The Dow is half empty... and draining fast!

*Could the next wave take us back to October '98?*



by Adam Lass

The question "Is America's economic cup half empty or half full?" is no longer relevant (if it ever truly was) to the U.S. stock market. That cup is more than half empty, and draining fast. Not only is a continuation of the recovery increasingly unlikely, even a flat market is rapidly becoming a pipe dream.

Indeed, the next step for the Dow Jones Industrial Average (DJI) is very probably a move back to at least 8,500 by the end of summer, a reasonably probable dip to 7,399 by mid to late September, and possibly a six- to eight-month plunge down to 6,800.

I know I usually discourse on the near-term future of the NASDAQ, but I would like to alert you to a larger potential threat to your equity positions. In addition to my in-depth analyses of the NASDAQ 100 and QQQ that form the core of the *Q-Wave* and *X-Wave* options trading systems, I have been studying the long-term charts of several key global indices... and I have detected an alarming waveform building in several of the high-beta correlated markets in the U.S. and Europe.

### Did 9/11 matter?

Over the next six to eight months, this wave could yield

results similar to the collapse I predicted last September. In fact, last September's collapse is particularly relevant, because, contrary to popular mythology, that drop had very little to do with the WTC and Pentagon atrocities.

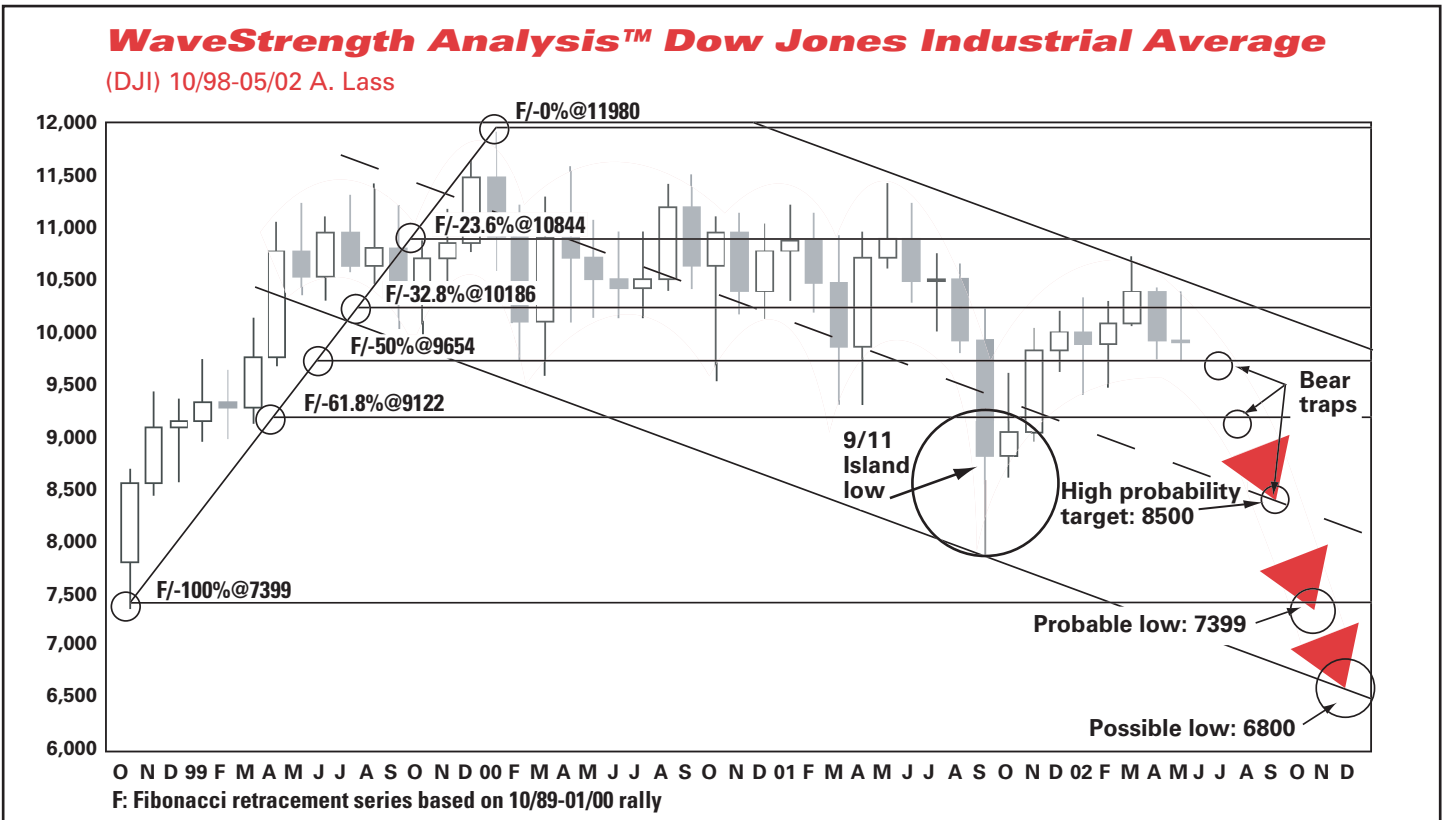
Indeed, that drop was just the fourth wave-bottom in a clearly marked series, while the supposed recovery of the past nine months was merely its reciprocal wave-top. *WaveStrength™* is now yielding strong indications that the slip from last March's high is just the beginning of a slide that could easily return the Dow to levels we haven't seen since October of '98.

There will be several key moments in this trend. Particular attention should be paid to the support nodes at 9,400 and 8,600... when it will appear to be turning around, but from what I can tell at this point, these will be nothing but bear traps.

### G-Men catch the Wave

The last time I made a call like this, I couched it in terms that earned me a personal visit from an FBI agent who was more than a little curious about my "sources." So this time I will be quite specific as to the source of this prediction.

By now, regular readers of this column are familiar with my proprietary *WaveStrength™* analytic system, which uses a combination of trend and wave studies and Fibonacci retracement patterns laid over Japanese can-



dlestick charts to determine probable future developments. The chart accompanying this column uses all these elements. To begin, I charted out the Dow Jones Industrial Average from October 1998 to May 2002, using Japanese candlesticks to denote each month's open, high, low and close.<sup>1</sup>

Over this base I have laid a Fibonacci retracement grid, using the October '98 low at 7,399 as the -100% mark and the January '00 high at 11,908 as the -0% mark.<sup>2</sup> The Fibonacci method stipulates that four intermediate levels, -23.6%, -38.2%, -50% and -61.8%, will form key support/resistance lines in the chart. In my Dow study, these stress lines fall out at 10,844, 10,186, 9,654 and 9,122, respectively. (There are two more Fibonacci levels I have not noted on this chart: -161.8% at 4,613 and -261.8% at 104. If the Dow retreats to these levels, advice on running down deer and building shelter from cardboard boxes will become more relevant than anything you read in this newsletter.)

In addition to the Fibonacci-generated horizontal support/resistance lines, I have placed three parallel sloping lines denoting the top, center and bottom of the Dow's primary trend subsequent to the '98-'99 rally, as described by the series's falling bottoms. And finally, within the grid formed by these intersecting lines, I have noted the distinct wave pattern created as investors move in and out of the market.<sup>3</sup>

### Vox populi

Simply put, this wave pattern is the graphical representation of the vast herd of investors slowly losing faith in the market. At the bottom of each downstroke, the market is losing a significantly higher portion of investors than it regains on the upstrokes. A simple enough concept... but this method of analyzing the phenomenon offers great insight into the market's likely future pricing behavior.

It was this wave pattern that alerted me to the high probability of a marked downward move prior to 9/11, rather than any "insider scoop." And once again this pattern is strongly suggesting a move to at least the F/-61.8%

point (9,122). There is a marked possibility of a rebound at that moment, as it marks the top of the 9/11 island formation, and sentimentalists are likely to seize on this as an excuse to call for a bottom—much to their peril.

*WaveStrength*<sup>TM</sup> is indicating a reasonable probability that this rally will fail at F/-50% (9,654), as will the other bear traps noted on the chart—including the one at the falling trend's midpoint. If allowed to continue unabated, this trend should continue into late fall with a likely bottom at F/-100% at 7,399... or possibly even the falling trend bottom at 6,800. That would mean a drop of nearly 3,000 points from current levels.

### Loss of faith

Is this plunge a fait accompli? Hardly. I have often stated that I do not read the "future" in any true sense of the word. All *WaveStrength*<sup>TM</sup> offers is insight into the market's potential behavior. Before you cavil that the improving economy ought to buoy the market, remember that *WaveStrength*<sup>TM</sup> measures not the market itself but the herd's faith in same.

And, barring some momentous new factor introduced into the mix—like George W. Bush naming New York Attorney General Eliot Spitzer to the helm of the SEC or Amazon paying its investors a real dividend—what's to steer us off this path? Face it: it's going to be a long time before investors forget how badly stung they were by the lying, cheating, and—dare I say—stealing that has been standard operating procedure on Wall Street for the past decade, and once again lavish largesse on the market.

<sup>1</sup> For more information on Japanese Candlesticks, I recommend Steve Nison's *Japanese Candlestick Charting Techniques: A Contemporary Guide to the Ancient Investment Techniques of the Far East*, and *Beyond Candlesticks: More Japanese Charting Techniques Revealed*.

<sup>2</sup> Background on the Italian mathematician Leonardo Fibonacci is plentiful and fun to read. Information on how his formulas apply to financial calculations is rare and obtuse, but if you are game, try Robert Fischer's *Fibonacci Applications and Strategies for Traders*.

<sup>3</sup> Note: These wave patterns are fractal in nature. As one examines any given leg of a wave, the pricing oscillations within it will correspond to the larger pattern's wavelength and amplitude.

## If the Dow's half empty and draining fast... here's how to profit off its pending implosion:

*Use this LEAPS to make 312% when the Dow hits 6,800 next October!*



by **Bryan Bottarelli**

If you're familiar with how Adam and I run our *Q-Wave* and *X-Wave* trading systems, then you know the drill...

Adam gives an in-depth analysis from his *WaveStrength*<sup>TM</sup> forecasting system, littered with unpronounceable words (like Fibonacci), unidentifiable support and resistance points (like

23.6%, -38.2%, -50% and -61.8%) and an incomprehensible conclusion about where the market's headed.

Then he hands it off to me with a simple assignment: Find a way to profit off it.

With all those sloping lines, retracement points, and candlestick patterns, I must concede... the guy gets it right time after time after time. So I'd look like a fool if I blew his dead-on market forecast with a bonehead profit strategy. Luckily, it hasn't happened thus far. In 2001,

Adam and I averaged 25% with our X-Wave trading system... and this year, we're averaging 28% with X-Wave and 27.2% with our new Q-Wave trading system.

When it comes to the Dow, the profits are just as nice.

In the May issue of *Taipan*, I recommended an US\$8.00 LEAPS put on the Dow, specifically the **December 2003 Dow 100 Put (ZDK XV)**. This option gives you the right to sell the Dow for 10,000 anytime before December of 2003. Since our entry at US\$8.00, the Dow has suffered two days of -150 losses, which has pushed this LEAPS up 20% in 2 weeks. As I write this, the Dow LEAPS trades between US\$10.10 and US\$11.10 per contract.

**If you're not holding this 2003 Dow LEAPS, step it up a year... buy the Dow December 2002 Put for US\$9.00 and sell it for US\$28 when the Dow hits 7,000!**

If you missed my first Dow put recommendation, then don't miss this one. For you latecomers out there, the new way to profit off a Dow free-fall comes in the form of the **December 2002 Dow 102 Put (DJV XX)**.

This option gives you the right to sell the Dow for 10,200 anytime before this December (no matter what price the Dow is trading for at the time). To own this right, you

pay US\$900. But should Adam's forecast come true, this Dow put will be valued around US\$2,800 as the Dow approaches 7,000. *While Dow shareholders eat their lunches through a straw, you could be making massive profits.*

If you're currently holding any Dow stocks, I strongly recommend adding this option to your portfolio. And if you're still intent on holding onto deteriorating blue chips like Wal-Mart, G.E., and Home Depot (the latter happens to be my favorite short right now), at least do yourself a favor and watch this option... to see how it gains value as your "great American companies" continue their slow downward spiral.

If you want to discuss this Dow put option strategy... or hear more about my two trading services, *Q-Wave* and *X-Wave*, meet me at the Agora Wealth Conference, August 14-18 in San Francisco. I'll be glad to give you a full rundown. That is, as long as you're buying the drinks afterwards!

P.S. For more information about the Agora Wealth Conference, call the newly married Siu-Yee at 410-454-0427. While you've got her on the phone, ask for her broiled abalone recipe. It'll knock your socks off... literally!

I P O T R A D E R

## Guard your assets with these security plays!



by Siu-Yee Ng

As we all know, there's no privacy online. Someone or something is tracing your every mouse-click. Someone could be sending you an email virus or stealing your identity at this very moment.

Hacking into a database is actually easier than you think. The hacker only has to find one of a huge number of existing security flaws to attack computer systems via the Internet.

Most of the systems compromised in the "Solar Sunrise" Pentagon hacking incident were attacked through a single vulnerability. A related flaw was exploited to break into many of the computers later used in massive distributed denial-of-service attacks.

Recent compromises of Windows NT-based web servers can be traced to hackers who gained entry via a well-known vulnerability. Another vulnerability is widely thought to be the means used to compromise more than 30,000 Linux systems.

A few software vulnerabilities account for the majority of successful hacks because attackers are

opportunistic, taking the easiest and most convenient route. They exploit the best-known flaws with the most effective and widely available attack tools.

They count on organizations not fixing the problems, and they often attack indiscriminately by scanning the Internet for vulnerable systems. But there are solutions to these problems, and I'll tell you in a minute how you can profit from hack attacks.

### Stop the break-ins!

Despite all the well-publicized virus outbreaks and

Stats as of May 29, 2002			
Company	Ticker Symbol	Market Cap	P/S Multiple
Check Point Software	CHKP	US\$4.30B	9.43
Verisign	VRSN	US\$2.37B	1.94
Internet Security Systems	ISSX	US\$816.2M	3.62
RSA Security	RSAS	US\$340.8M	1.31
SonicWALL	SNWL	US\$428.4M	3.63
Stats as of May 23, 2001			
Company	Ticker Symbol	Market Cap	P/S Multiple
Check Point Software	CHKP	US\$12.7B	30.0
Verisign	VRSN	US\$10.28B	14.3
Internet Security Systems	ISSX	US\$2.2	10.0
RSA Security	RSAS	US\$2.0B	7.0
SonicWALL	SNWL	US\$1.0B	12.0

security invasions, many companies still feel Internet security is not important. Many corporate IT departments think the best way to secure data is to limit access.

But here's the cold, hard truth. We all communicate, research, buy and sell on the Internet. The Internet is not going away. So you can see the importance of the Internet security industry.

And now, with all the political tensions around the world, cyberterrorism has become a big threat. Despite the economic slowdown, government agencies continue to spend on IT. A total of three IT companies with the government as their biggest client have debuted this year, raising a total of US\$370.4 million.

But what about security companies geared towards the public sector? Companies are now even tighter with their purse strings when it comes to IT spending. Just take a look at the chart on page 7.

As you can see, these security stocks once belonged to the billion-dollar club. But in a little over a year, they have lost an average of close to US\$4 billion! How quickly things have changed.

Is this the time to buy these battered, undervalued stocks? Are companies ready to loosen their purse strings and spend the necessary funds to increase Internet security?

The market is slowly recovering. Manufacturing is picking up and consumers continue to spend. As the market recovers, so will these two security plays:

Although its stock price has fallen 69% in a year, **Check Point Software (CHKP:NASDAQ)** remains an industry leader.

Check Point develops, markets and supports Internet security solutions for enterprise networks and service providers, including virtual private networks (VPNs), firewalls, intranet and extranet security. Check Point also offers traffic control quality of service (QoS) and IP address management.

Information, and the ability to access and distribute it, is a key asset in today's competitive business environment. The need to communicate effectively has led to the installation of ever more network-based communications systems ("connectivity"). Increased connectivity in turn creates the need for better technology to safeguard and manage the access to information available over these growing global networks.

Don't forget, data can be intercepted during the transmission over the Internet. Although the explosion of connectivity provides tremendous benefits, it also exposes an organization's sensitive information and applications to unauthorized access, both through connections to the public Internet and from within the enterprise.

Such risks are driving a critical need for enterprises to protect their information and information systems from unauthorized access and use.

### **Transmission completed**

Using Check Point's Secure Virtual Network (SVN) architecture, an organization can connect and secure all

elements of the enterprise IT structure: networks, applications, systems and users. Check Point has increased its revenues yearly. It rang in US\$219.6 million in 1999, US\$425.3 million in 2000 and US\$527.6 million in 2001.

Because of the economic slowdown, Check Point's Q1 revenues decreased 28%. But they're on target for strong sales in the second quarter. Don't count Check Point out—the year is not over yet.

Granted, there is a slowdown in the IT sector, but Check Point has the potential to be one of the first to climb out of the rut. It has plenty of cash and remains profitable. And on May 22 there was a huge increase in institutional buying.

**Check Point (CHKP:NASDAQ) is a buy on dips under US\$16.50. For more information on Check Point, contact investor relations at 3 Lagoon Drive, Suite 400, Redwood City, CA 94065, tel. 650-628-2000, fax 650-628-2116, email ir@us.checkpoint.com.**

### **Protect your credit**

We've all heard about the dangers of hackers getting hold of your credit-card information. Well, **Entrust, Inc. (ENTU:NASDAQ)** is a global provider of public-key infrastructure (PKI) and authorization products and services that protect e-businesses and their customers from hackers.

Since 1994, it has provided its award-winning PKI solution primarily to global enterprises and government entities, as well as small- to midsized businesses and individuals.

During the first quarter of 2002, Entrust continued its strategy of focusing on core vertical and geographic markets. It was also successful in expanding sales of its

Sell targets: take profits of 57% and 30% off the table!

- **WCI Communities' (WCI:NYSE)** lock-up period is quickly approaching. On September 8, 2002, it will be the first time insiders will be allowed to sell their shares. We may see increased selling pressure in the next few months in anticipation of this. **Put a sell target on WCI above US\$30 and take your 57% profit off the table.**
- Another provider of IT services to the U.S. government debuted on June 5, 2002. This sector is hot and underwriters know it. But it won't be long before it gets saturated. **Put a sell on Anteon International Corp. (ANT:NYSE) above US\$23.50 for a 30% return.**
- Compared to **Medical Staffing Network's (MRN:NYSE)** competitors Cross Country (CCRN:NASDAQ) and AMN Healthcare (AHS:NYSE)—both of which have market caps in excess of a billion dollars—Medical Staffing has much more room to run. As we approach the summer months, temporary staff will be in greater demand as healthcare professionals take vacations. **We're already up 34%!**

secure web portal product solution.

Revenues from the secure web portal solution actually increased 36% from the fourth quarter of 2001 and over 100% from the first quarter a year ago.

Total revenues decreased 13% for Q1 of 2001 compared to Q1 of 2002. Revenues in North America only decreased 1%. It was the 32% decrease in revenues outside of North America that really put a dent in the company's Q1 earnings.

Entrust has a P/S ratio of 2.25 and a market cap of US\$261.0 million. Institutional buying remains strong, a positive sign for the company's growth potential.

**Entrust (ENTU:NASDAQ) is a buy on dips under US\$3.50. For more information on Entrust, Inc., contact investor relations at One Hanover Park, 16633 Dallas Parkway, Addison, TX 75001, tel. 972-713-5800, fax 972-943-7305, or email investor@entrust.com.**

## Get boring, get wealthy:

*It's time to leave the "story stocks" behind and invest in value*



by Briton L. Ryle

It's a tough market for stock-pickers. But my Taipan Traders just took 16% and 50% gains on a couple of stock positions. At the same time, we loaded up on put options on some ridiculously overpriced semiconductor stocks.

It seems obvious to me that the NASDAQ is hell-bent on retesting the post-9/11 lows. And chances are, it will go lower. The thing to remember is that we're seeing the inverse of the tech bubble days from 1999 and 2000. Picking stocks then was like shooting fish in a barrel. Despite the absurd valuations, shorting the market was suicide.

Now, it's the longs who are suicidal.

### Supply and demand

Another thing to remember is that the NASDAQ isn't trading according to fundamentals. While earnings estimates are still too high for the second half of the year, it's possible to create a compelling bullish argument based on recent economic data.

The economy is recovering. Durable goods orders are up. Unemployment is stabilizing. Inflation is more or less in check (though the recent surge in gold prices suggests that many expect it to pick up). Even a weak dollar can be interpreted as bullish for corporate profits.

But the real story behind the NASDAQ's plunge is supply and demand. There's too much stock out there left over from the delirious days of the IPO tech bubble. And there are no buyers. Plus, there are a bunch of institutions with no qualms about rubbing salt in the wound by dumping millions of shares on the market at any price.

### What's it going to take?

One of *Taipan's* core beliefs is that you should buy when there's blood in the street. But with the exception of the post-9/11 selloff, we haven't seen panic selling. Even the revelation that several big investment houses are under investigation for fraud hasn't done much to shake the average investor's complacent confidence in stocks.

And until I see fear in the eyes of investors, until my

Mom asks me about shorting stock, I will remain fundamentally bearish about the NASDAQ.

### Who bought Crown Cork & Seal?

At present, I see exactly three favorable investment ideas: emerging markets, commodities and value. I'm well represented in the emerging markets category with plays like Petrochina (up 25%) and Hanaro Telecom (up over 115%).

And since I'm not an expert on commodities, I'm sticking with value. *Taipan* readers could have done well with my value play on Crown Cork & Seal. I recommended it in January below US\$5. The stock went as high as US\$12.65 before my US\$10 stop-loss was triggered. Crown Cork & Seal was a clean 100% gain.

I practically begged 247profits e-Dispatch readers to let me know if they bought the stock. And I got exactly zero responses. The lesson? Despite representing the best chance for a really nice gain, nobody likes value stocks. I guess that's why they're value stocks. And why the investors who buy them are usually called "contrarian."

### The US\$1.98 sucker pageant

It's been over two years since NASDAQ 5,000. Yet investors still seem to want "story stocks"—you know, the next Microsoft or Intel that's selling for just US\$1.98.

I watch the NASDAQ in five-minute ticks every day. And I still see an incredible amount of hope in the market. There's a hardcore group out there—and I'm sure it includes some fund managers and other institutional investors—who haven't learned the most basic rule of a bear market: sell the rallies.

Every time the NASDAQ rallies a percent or two, the hope becomes palpable. "Maybe that was the bottom," the bulls hope. And the NASDAQ smacks them every time. It's like a bizarre sado-masochistic version of "Groundhog Day."

But that's the NASDAQ. Other areas of the market are doing OK. Small caps are doing great this year. Retail stocks have performed pretty well, as have defense and, of course, value stocks.

**Where to put your money**

To put things simply, there are two kinds of maladies that affect stock prices—chronic and treatable. The NASDAQ’s problems are chronic. They require radical surgery (via restructuring) and even death (via bankruptcy).

September 11, on the other hand, is a classic example of a treatable event. I don’t mean to make light of the tragic loss of life, but the terrorist attacks were an isolated event. Bad management and certain types of lawsuits are other examples of treatable maladies. Companies take their medicine and they get better.

These days, investors are having a hard time distinguishing between the two. In fact, I’d say investors are prone to misdiagnosis. But for those who can tell the difference between a chronic and a treatable condition, there are some fantastic opportunities.

**Getting healthy**

I hope my use of a medical metaphor wasn’t too annoying. But I have a reason. I want to tell you about an outpatient medical services company called

**Healthsouth (HRC:NYSE).**

Healthsouth runs approximately 1,900 facilities offering outpatient rehabilitation, surgical and diagnostic services. Healthsouth operates throughout the U.S. and in Puerto Rico, Canada, England and Australia. It’s a big company, with revenues well over US\$4 billion.

Healthsouth is also a very stable company. It has institutional support, predictable revenue growth and profit margins in the 10% range. Stability always comes at a price, so assessing Healthsouth’s value isn’t as easy as measuring discounts to book and sales.

Industry comparisons become more important, as do price-to-earnings (P/E) and price-to-earnings-growth (PEG) ratios. For instance, of the profitable healthcare companies with a market cap above US\$1 billion, the average price-to-book is 3.7 and the average P/E is around 35.

In comparison, Healthsouth trades at a discount to its peers, with a price-to-book value of 1.2, a PEG ratio of 0.8 and a P/E of 25. If you’re wondering “why the dis-

count” you’ve been paying attention.

**You don’t always get what you pay for...**

Healthsouth’s valuation is low for two reasons—a lawsuit and a change in reimbursement for its inpatient rehabilitation business. Both happen to be one-time, treatable events. And as the market gets wise to this, the stock price will likely rise.

First up, the lawsuit. On October 18, 1998, Healthsouth responded to a couple of class-action lawsuits alleging that it violated Medicare rules for outpatient rehabilitation treatment. The stock dropped from US\$30 to US\$10.

In January of this year, the Department of Justice got involved with the lawsuit. The stock dropped from US\$15 to US\$11. Healthsouth says the claims are without merit. And even if that’s wrong, the suit involves less than 5% of the company’s revenue.

The change in reimbursement from Medicare is a non-issue, because Healthsouth was able to reduce costs to compensate for it.

**There you have it**

Somehow, telling you that Healthsouth could double in price over the next year seems at odds with my value-investing thesis. But it’s true. US\$28-US\$30 is a very reasonable 12-month price target for this stock.

But a be forewarned—if you buy this stock you won’t be regaled with nifty technology, you won’t be able to show off the company’s products to your envious friends and coworkers, and you won’t be bombarded with lofty, unattainable earnings projections.

In fact, this stock will probably bore you to death. But year from now, when Healthsouth is trading north of US\$25 a share, you might find that something to get excited about.

**I rate Healthsouth (HRC:NYSE) a strong buy below US\$15. I’m placing a one-year price target of US\$28 on the stock. You can contact Healthsouth at One Healthsouth Parkway, Birmingham, AL 35243, tel. 205-967-7116, email nfo@healthsouth.net.**

TURFWAR PROFITEER

**The old gray mare just ain’t what she used to be...**

**Turning a terrible loss into huge gains**



by Jay Salomon

About a year ago, we brought you word (on the *Taipan* website) of the mysterious equine disease called Mare Reproductive Loss Syndrome (MRLS) devastating the Blue Grass country. Some 550 late-term abortions were reported in the spring of 2001. But the stunning news is that over

3,000 more fetal losses are now known to have occurred later on.

The opportunities to make serious money from this tragedy are numerous. Yet we have seen relatively little notice of them, even in the vast thoroughbred industry press. To date, no one even knows what causes the problem.

What’s more, the syndrome has reappeared this spring, although the numbers do not look as bleak. But

some evidence exists that MRLS may also have popped up in other breeding areas, including New York.

Here's why we are so excited about nailing some serious coin: 3,000+ lost Kentucky foals represent approximately 30% of the entire crop in that state... and Kentucky accounts for about 30% of all American thoroughbreds. This means that the number of weanlings and yearlings (thoroughbreds that will reach the track in 2003 and 2004) is seriously depleted.

### ***Their kingdom for a horse***

But purses continue to rise as simulcasting, account wagering and slots revenues grow and grow. According to *Thoroughbred Times*, a record US\$1,146,377,367 in purses was awarded in 2001. The average purse was US\$18,936, a 4.9% rise in one year, and a whopping 43.9% since 1996.

Obviously, the engine for profits here is the basic rule of economics: supply and demand. Most racetracks were already desperate for runners before the MRLS numbers kicked in. Now, they will need to cover the huge gap caused by the disease.

The potential to land big dollars from the equine shortage is unparalleled in its own right, but since it occurs at a time when the price of gold is apparently headed dramatically upwards, the opportunities are almost unimaginable.

Thoroughbreds, generally, fetch much higher prices when commodities are also on an upward spiral. But the thesis of this article is that MRLS will only provide a windfall if the buying public continues to ignore the profit potential. Therefore, we must distinguish the natural rise in the price of a commodity from any sudden spurt based on the unique opportunities caused by the disease—if both numbers rise precipitously, our opportunity is gone.

Those in the best spot to make money from the crisis, naturally, are breeders with live 2001 and 2002 foals already in their barns... animals that can be sold privately, or at auction, or raced.

For everyone else, the trick will be to outsmart the competition in the clever purchase of racehorses... or to join in established, reliable syndicates or partnerships that do the same. The current lack of supply will eventually provide buyers with advantages they

never had before, and our sense is that few realize how incredible this sudden advantage (courtesy of MRLS) really is.

A risky but sometimes almost indecently profitable opportunity known as "pinhooking" is another possibility for Taipans to consider. The practice will be familiar by analogy to those whose normal market action includes arbitrage and futures. Pinhookers buy young horses (frequently weanlings) that look undervalued by owners or bidders. The purchasers have only one goal: develop the animals for resale as quickly as possible, usually before they are ready to compete on the track. MRLS provides an ideal ground for pinhookers, because the public's wake-up call as to the value of these thoroughbreds in a supply-tight market should come at just the time the animals are ready for sale.

If you're not convinced of the immense profits to be made even from traditional horse-trading, consider this inspirational example. Last fall, a Maryland couple long active in the breeding industry (with moderate success) went to Kentucky and purchased a stallion for a reported US\$200,000, more or less. They bought Our Emblem (even though his record on the track was spotty and his first crops of runners showed little talent) because of the stud's impeccable bloodlines, especially on the dam's side. The stallion had scarcely arrived in his new home when three of his progeny (born long before the purchase) suddenly won graded sophomore stakes. But the real coup came from the Kentucky Derby and Preakness scores turned in by just one of them, War Emblem. Offers poured in for the stallion, but the Murrays wanted to wait until the Belmont before deciding what to do. But when the powerhouse Kentucky duo of WinStar Farms and Taylor Made offered US\$10,100,000 plus two free stud seasons a year, the Murrays could wait no longer, and re-sold the horse. In less than half a year they multiplied their investment well over 50 times! Ready to step up to the plate yourself?

### ***Get smart—then outsmart***

At this point, we post a warning to any reader unskilled in the breeding, buying and racing of thoroughbreds: as with all investments, only a fool rushes

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in to purchase that which he knows nothing about.

The first step is to learn something about the business. You can begin with home schooling from the substantial literature provided by the Thoroughbred Owners and Breeders Association (TOBA). You'll learn that even the biggest names in the business usually have a bloodstock agent on their team. We've discussed the premise of this article at length with one of them, Paul Randall, and respect his advice that beginners hoping to cash in on MRLS should probably shy away from the big-ticket auctions at Keeneland and Saratoga. Lesser venues (or other sales at these two) will probably produce greater value. Remember, the average yearling at the July Keeneland Select sale last summer (not a prime year, by the way) fetched US\$710,247, but many other sales don't come close to that amount. The average at the recent Fasig-Tipton Midlantic Sales for two-year-olds in training was about US\$33,000, and these thoroughbreds were bought ready to race. You might also consult with a large breeder such as Country Life Farm—the Pons family operation even puts together partnerships and syndications.

Meanwhile, we will continue to monitor the profit potential ourselves throughout 2002, posting advice on the 247profits website after key auctions. Look for the first of these around July 22, after the results of several sales in Keeneland the week before have been digested. If prices suddenly seem to reflect an awareness of MRLS and get too high, we will immediately let you know.

Unfortunately, this is not an industry where tons of reliable information to logical questions is always available (except for ours). We have seen few factual reports giving specifics about the dead or aborted fetuses. Did a

disproportionate number of them involve the state's fancier mares, or was the syndrome spread evenly from the finest Kentucky stud farms to the most humble?

And we'd like to know whether the live 2001 and 2002 foals are completely sound, or will their careers (both on the track and even at stud) be compromised by unknown sequelae from the disease? Should we assume the worst and make sure our purchases were not foaled in the Kentucky area? Could sales and auctions abroad actually give us the biggest bang for our buck if the supply shortage forces prices up in the States?

And most of all, will MRLS continue to take its toll in future seasons, making current purchases even more valuable?

So far, despite massive research and many theories, MRLS remains a mystery.

Happily, the way to profit from it is not!

**Contacts: Thoroughbred Owners and Breeders Association (TOBA), [www.toba.org](http://www.toba.org). Paul Randall, Bloodstock Consultant, 410-239-3271. Josh or Michael Pons, Country Life Farm, PO Box 107, Bel Air, MD 21014, tel. 410-879-1952, fax 410-879-6207, [www.countrylifefarm.org](http://www.countrylifefarm.org).**

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by *Siu-Yee Ng*

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