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J. Christoph Amberger

The single most important question to ask if you want to make money in the markets

Plus: Taipan *members reap huge gains on China Yuchai, Lexar and Netegrity*

In this issue I ask lots of questions. But none is more important than the question on page 4. For an investor on the hunt for profits, it's the single most important question you can ask yourself. But before we get there, let me remind you of the profits our team of analysts have been handing readers through our daily online and email services. Gains like these:

Stock	Buy	Price	Sell/ Update	Price	Gain/ Loss	Status
Cepheid CPHD	11/7/2003	$4.50	8/18/03	$4.34	-3%	Open
Encysive Pharmaceuticals ENCY 1st Half	10/15/2002	$2.07	6/26/03	$4.38	111%	Sold
Encysive Pharmaceuticals ENCY 2nd Half	10/15/2002	$2.07	8/19/03	$4.00	93%	Sold
Given Imaging GIVN	12/2/2002	$9.55	8/18/03	$11.32	18%	Open
Guilford Pharmaceuticals GLFD	2/3/2003	$3.26	4/4/03	$4.35	33%	Sold
KCS Energy Inc. KCS	4/3/2003	$2.57	8/18/03	$6.76	163%	Open

On August 25, our China and IPO specialist Siu-Yee Ng issued the following alert:

"China Yuchai has been on a tear after settling its dispute with its China unit. I was planning to hold this for the long haul, but with the stock trading at US$17.50 today… up fully 288% in less than 8 months… it is just too tempting. (You may remember that I first recommended it at US$4.50 a share in the January issue of *Taipan,* which came out December 30, 2003.)

"You now have two choices: Sell your entire position in **China Yuchai (CYD:NYSE)** and bank the 13 dollars of profits per share. Or, if your long-term perspective allows, sell half of it and free-ride the remaining half for potentially higher gains."

But wait, there's more: Her Chile play, **Quinenco S.A. (LQ:NYSE)**, hit a 52-week high. We're up over 53% in seven months! Her Black Budget play on **SGL Carbon (SGG:NYSE)** also hit a 52-week high. We're up over 62% in six months. And our other Chinese play, **Zindart (ZNDT:NASDAQ)**, is up 40% in two months.

Christian DeHaemer's January recommendation was to buy **Netegrity (NETE:NASDAQ)** under US$3.50. Now priced at US$8.71, it is up 148%. (He recommends you hold!) His February recommendation of **Abiomed (AMBD:NASDAQ)** was sold for 74% gains. He recommended you sell half of your position in his June pick, **Lexar Media (LEXR:NASDAQ)**, for 100% gains… and he continues to hold the other half at 136% profit. (Overall, his 2003 *Taipan* picks are up an average of 90.4% as of August 26, 2003.)

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If this rally continues, you can expect *Taipan* gains to go higher. But will the summer rally last?

Something has changed in the stock market. That "something," of course, is the dollar amount of Federal Reserve repurchase agreements, which has dropped considerably. There is a strong correlation between repurchase activity and the current rally in stocks: In the second week of August, the Fed's repurchase activity totaled US$48 billion. A week later, the total is was "only" US$35.25 billion. (Which means that for a mere US$83 billion, you, too, can create a 100-point rally in the NASDAQ.)

The question is: How long will this go on? How long will the Fed continue to feed the stock market's addiction to liquidity? I think the answer is simple—2,000 and 10,000… as in NASDAQ 2000 and Dow 10,000. Those are big, round numbers that will scream "the economy is OK" to the American people. But is it OK? Or is this rally based on a false idea of value?

Value vs. value

The traditional measures of value for investors all have to do with the actual or potential earnings of a company. What is it producing? What are its costs of production? What is its position in the marketplace? What is its competition? What is its future potential for earnings?

Oddly enough, few investors these days seem to care about value any more. They didn't back in 1999 (when all they wanted was an Internet-related business plan scribbled on a cocktail napkin). And unless they're seeing sales and earnings increases in US companies where we can't find them, they don't care now. But maybe you don't have to care about value to make money. In fact, based on *Taipan's* researches into Dynamic Market Theory, the traditional views on value are all wrong. I'll get to Dynamic Market Theory in just a minute, but first let me explain our view of value.

We believe most market theories deal with the "intrinsic" value of stocks or other commodities. In other words, the notion that the value comes from within the thing. That it has value by itself, regardless of any associations with other things.

But we believe that, for investors, the only value of any importance is the value that someone else places on a stock or investment at any given point in time.

Following this idea, there is really no such thing as a "bubble." If the price of a commodity like real estate, tulip bulbs or Internet stocks rises to hyper-value based on demand… then that is its true value at that moment in time.

Valuations are nothing but arbitrary numbers

You see, a "bubble" is an argument about value—mostly made in retrospect, after a particular investment fad has gone bust. (Investment fads that don't go bust, conversely, are called "strokes of genius," even if the underlying speculative analysis and risks are the same for both.)

For example, at the market peak in early 2000, it was said that the stock market had a valuation of US$17 trillion dollars. That amount had dipped to US$8.5 trillion by October 2000. Right now, the valuation of the stock market is about US$10 trillion. But all these figures are assignments of value based only on what a small percentage of shares is trading for.

What you would find if you tried to sell all the listed shares of, say, Microsoft at one time is that the price would collapse… no matter what was going on at the company or in the stock market.

There are almost <u>11 billion</u> shares of Microsoft outstanding. On any one day, only 25 or 30 million might change hands. If you dumped all 11 billion shares on the market at one time, the price would plummet because of the monstrous excess in supply.

So the "valuation" commonly given to any or all stocks is arbitrary, not real, even if it is based on the latest sale of a few shares of the stock.

Those subscribing to a bearish view of the market like to say that around US$8.5 trillion dollars of equity valuation was "destroyed" in the bear market from early 2000 to October of that year. But since valuations are assigned arbitrarily anyway, they can't be destroyed. They change up, they change down. But they never go away. And that US$8.5 trillion wasn't "created," but was <u>generated by the reallocation of savings and spending money put into stocks, which pushed share prices up overall, causing the higher "valuation."</u>

And here's another interesting little fact:

In 1982, at the beginning of the last "bull market," there were only about 1,500 companies listed

on the New York Stock Exchange, with roughly 40 billion shares. The "market valuation" was around US$1.3 trillion.

But by 2000 and the end of the "bull market," there were over 3,000 companies listed on the New York Stock Exchange… with over 349 billion shares available.

Granted, some of these were start-ups, but it's obvious that a lot of the "wealth" that was "created" actually came from existing private companies going public, taking advantage of a rising market and putting shares of their company up for sale to the general public.

These companies were already in existence, with dynamic value. It's just that their value was now counted as part of the stock market. So in these cases, wealth wasn't created—it merely changed hands, from a few private owners to millions of stock investors.

Realistically, since stock market valuations came down, the amount of money invested in stocks also came down. Much of that money was simply reallocated to other assets… like real estate, bonds, gold, and other commodities.

Finding true value using *Taipan's* Dynamic Market Theory

Stocks are valuable to investors because their prices change, both up and down. If they didn't change, why would investors want them? It would be easier to hold cash—it's more liquid, and there are no transaction fees.

Now, anyone with a computer can see—in an instant—that a stock's price has moved from US$20 to US$25. And anyone with any imagination can see that you could have made a quarter for every dollar you put down. That's how it begins. And that's usually about the time average investors make their first mistake.

Because, as soon as you start looking for a particular stock whose price could rise, you introduce the idea of valuation—that a stock's price is somehow linked to the prospects of the company. But this is true only in the most general understanding of valuation.

If you watch stocks trade on options expiration days, you'll realize that "valuation" takes a back seat to the infinitely more powerful forces of money flow. The only question is, who's going to be left holding the bag?

Watch a stodgy old NYSE stock as options expiration day (the third Friday of every month) approaches. Pay particular attention to the open interest on puts and calls in the vicinity of the current stock price. Like clockwork, the greatest number of people who can be squeezed out of their money at expiration, will be. Whether that means selling down a "good" stock or pumping up a "bad" one!

Want to know where the S&P 500 and NASDAQ are headed? You could listen to bulls or bears or stock analysts. You could track unemployment, follow earnings trends, and pay close attention to market gurus and the financial media.

But if you really want to know, you should check the "Commitment of Traders" report released every Friday by the Commodity Futures Trading Commission. This report is more valuable than all the economic or technical analysis known to man.

Because this report will tell you what the big money, the money that literally moves the market, is doing. And this is where you'll get your first clue about what's really behind value… and why we prefer to use the realities of Dynamic Market Theory.

You see, 99 times out of 100, you'll find that the big money is doing the exact opposite of what "the herd" is doing.

The investors looking for steady-growth, low P/E stocks in which to park their US$100,000 IRA have no idea what they're up against. The big money, the guys with billions upon billions in buying and selling power, WILL have their way. And if that means dropping a low P/E stock even lower, then so be it.

For example: eBay currently trades at 22 times sales, has a P/E above 100 and a 50% premium to its growth rate. It is richly valued, to say the least. Eight million shares are sold short. And the open interest on options is about 2-to-1 in favor of the puts (investors betting the stock will go down). A lot of people are betting the stock is overvalued… and expecting it to fall.

It's not that they're wrong. It's that they're asking the wrong question.

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The single most important question you need to ask is not whether it's overvalued, but who's going to make money?

When you know the answer to that question, you can make a fortune. That's how the richest people in the world make their money. Here's what I mean:

The top three institutional owners of eBay have about US$3.5 billion in the stock. Add in the next three institutional owners, and you're talking about US$6 billion. So, will the investors who have approximately US$800 million in shorted stock ever turn a profit?

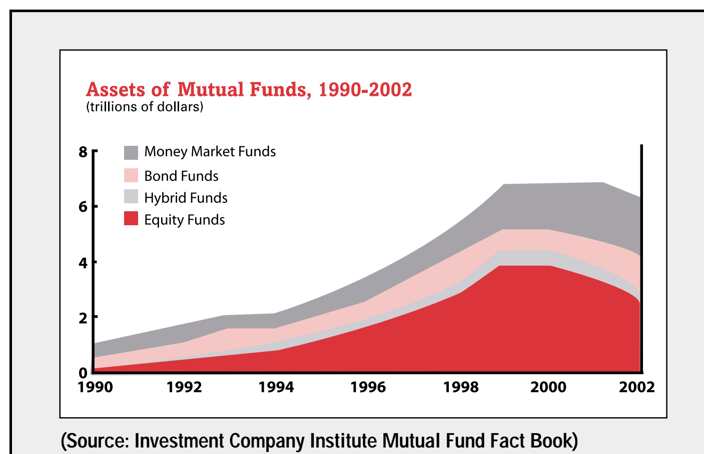
Not likely. The big boys, that is, the top institutional owners, will keep the price up until the shorts call it quits. Or they'll run the price up and "squeeze" the shorts—handing them bigger and bigger losses—until they give in.

And the situation is even worse for the vast number of put *options* holders.

So, sometimes it pays to poke your head up out of quarterly reports and valuation models and see what's around you. If you find yourself surrounded by a bunch of people who, like you, think they're about to make money… well, you're probably wrong.

The stock market is a game, pure and simple. And there's only one rule: money always wins.

Look at what happened in the 1990's. A very clear picture emerges from this chart. Just take a look:



(Source: Investment Company Institute Mutual Fund Fact Book)

As you can see, equity funds (stock funds) took a huge plunge from 2000 to 2002. Hybrid funds also took a nosedive. Bond funds took a much less severe hit, and money market funds dipped only slightly—along with the overall total in these funds.

What does this mean?

Well, if the total assets of all mutual funds didn't move very much, but individual ones did, then the money was simply rotating.

In other words, a lot of that money that "disappeared" from stocks (equity funds) simply moved into bond and money market funds. The money didn't "disappear"—it moved. Add to that the moves into gold and real estate, and you begin to see that—allowing for fluctuations in the "value" that we love to give to the market—money tends to *move around* more than it "appears" and "disappears."

Point is, all that money didn't just "vaporize," as the perennial bears like to claim. A lot of it simply moved. Now money is flowing back into stocks again. But beware—the market is set to fool investors and separate them from their money yet again.

But, if you follow Dynamic Market Theory, you're much better positioned to profit… no matter what happens in the stock market. It's a new and different way of investing that takes into account volatile market conditions and the many factors stacked against the individual investor.

Many stocks exhibit certain predictable behaviors before they make a large move… that is, before the money moves into or out of them. Over time, this behavior—shown by any number of indicators—gets recognized, and everyone begins to look for those indicators and act on them. Then the significant factors evolve into something else.

To turn this action into profits, you need a set of individual ways of looking at the dynamic market action of stocks (in other words, price action) to arrive at decisions about how to invest.

With these individual systems of looking at dynamic action, you can predict developments in stocks… in any market… by looking at the different indicators.

What's become obvious is that static theories or traditional views of the markets can't and won't work in the long run. Because there is no one set of principles—like value investing—that will always work. Since the market is dynamic and ever

changing, following one investing principle dooms you to failure. It may work for a short period of time, but once the market factors change, then so must your investing philosophy.

Plus, if everyone looked for "value" and bought "value" based on certain criteria, there would be only buyers for stocks one day, and only sellers another day. Markets just don't work like that. There have to be both buyers and sellers to maintain equilibrium in the markets.

Our new Dynamic Market Theory says that if you're concentrating on only one "sector" or one style of investing, you're going to fail. Money is constantly flowing from one stock to another, and from one sector to another. This dynamic action is what you must read to be successful.

Now, there a number of "lenses" you can look through to get a profitable view of the market, both on the macro level and the micro level. This month, our *Taipan* team has once again prepared half a dozen opportunities for you to take advantage of. So put up your feet and let them introduce you to some of the most profitable opportunities the dynamic markets have in store for you this fall. ■

The Bull's desires trump the Bear's necessities

Their cards may have been lousy, but the Bulls have taken the last two hands and may well take the next one

by Adam Lass and Ann Sosnowski

Why is the S&P 500 up 15.95% in the first half of calendar year 2003, what are the most probable scenarios for the second half, and how can you best capitalize on them? I would propose that the solutions to these questions lie in the answer to this one: What do people want?

And, right now, the answer to that one is *stock market growth.* And they want it in the worst way.

I frequently write about "the great herd." Some take this as derogatory, but that is a complete misconception. I strongly suspect that, aside from an unusual level of access to information, you and I, we *are* the herd.

Much like us, the people who make up that vast undulating mass have wives and kids and cars and mortgages. Many of them have very expensive cars, and while their mortgage rates may have declined considerably over the past few months, most have immediately traded in that largesse for cash. Few have used it to pay down bills.

Rather, they have engaged in a spending spree unrivaled in the history of recession. And thank goodness for them (or should I say us). If this market does continue to move up—and while I have expressed my doubts as to the probability, morality and wisdom of that possibility, it has happened and may just continue to happen—it will be thanks to them.

Up is up

That spending spree may be totally dependent on both personal and Federal deficit spending, but they have spent… and the market is up.

At a recent speaking engagement, I was challenged to put aside my knowledge of economics, politics, history and even physics, and examine the market from a state of almost Zen-like purity. Perhaps such a state is beyond my grasp in the face of such times and proclivities. But I can do the next best thing.

For the past year or so, I have been recruiting and training a few fresh young minds in the Byzantine ways of *WaveStrength.* Over the past few months, regular readers have heard me recommend gold for the first time. I must credit Brett Kendrick for that bold move. Today I would like to present the view of my young Athena, Ann Sosnowski, on the next eight weeks of the S&P 500's future.

Standing as she does at the beginning of her own voyage, her vantage point offers a remarkably different take: Where I have seen only the precipice that lies below, she notes the strength of the

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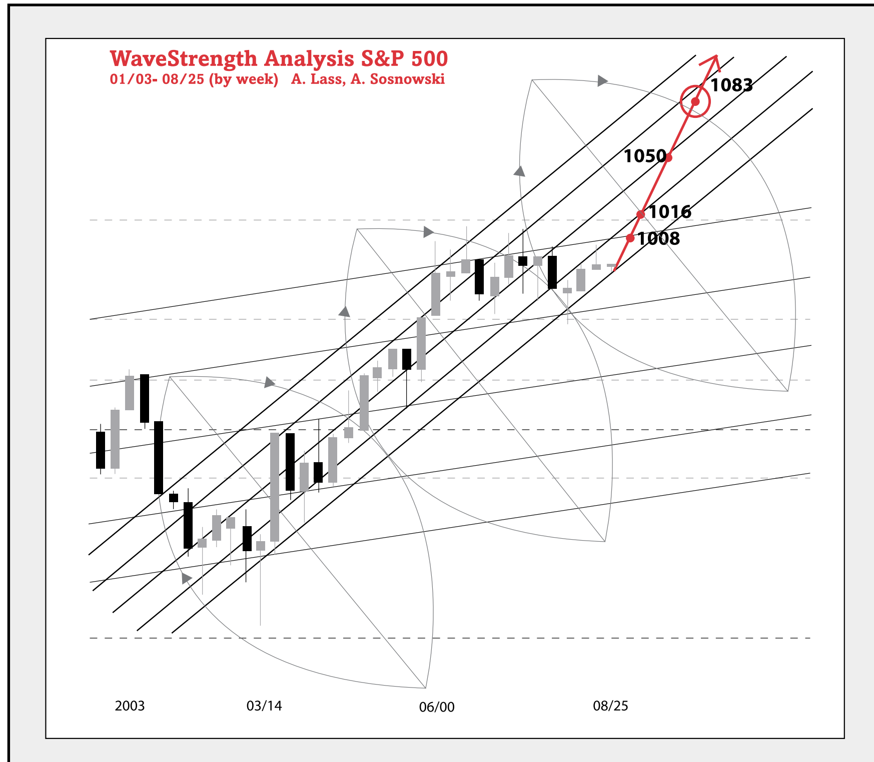
nascent bull as it vaults these seemingly impossible chasms, and declares that the market will continue its ride forward, drunk on the heady wine of its own success…



Evidence, apocryphal and otherwise

Watching out for the perfect waves on the indices has brought a mix of excitement and anxiety. Especially after one recent day's reaction to the market: everything dropping down into red, the sound of kerplunk silently echoing in the background.

But that sound has slowly faded away as I have found evidence of a bull rally. I'm talking about the S&P—the most recent index to experience what we might call the perfect wave.

Looking at the big picture, one cannot deny the reality: the S&P has been in a steady downtrend since September 2000. Recently, however, that downtrend seems to have competition.

The turning point

Looking the S&P 500 on a smaller scale (using weekly candlesticks in the accompanying chart), you can see that the recent five-month uptrend is showing signs of breaking through the Fibonacci -50% retracement line established after the ultimate high of 1,535 in 2000. This line has not been seen as a possible new support since 2002.

Focusing in on the recent five-month trend in weekly increments, one can see the support that this bull rally is receiving. The Japanese glyph created by the open, high, low and close of the week of 2/28/03 is known as "a hammer at the bottom of trend."

Its presence at the turning point of the uptrend's birth shows a consolidation of support at this key node, support which has remained intact through the five-month upswing and through two entire time ellipses of approximately three months each.

Upward mobility

The most telling evidence that the big bear downtrend—*Ursa Major*—has given birth to a bull that is destined to grow far beyond its adolescence is the consistent upward thrust of large positive candlesticks at all of the Fibonacci lines.

Observe how the five month uptrend has broken through all preceding Fibonacci retracement lines (-61.8%, -50%, -38.2% and -23.6%) and is now poised to break through the crucial 0% marker sometime in the next ten trading days.

As an added note, the increasing numbers of positive closes in the last five months also tend to show that this bull is just getting started… and could very well return the S&P to where it was during the dot-com days.

Now, you might look at this chart and ask, "Why are you so sure that this adolescent bull is going to end up getting a driver's license and cruising its way into teenage coolness? Really, there's no sure bet."

The limit

There are certainly a few potential accidents lurking. For example, when I apply Bollinger bands to the weekly S&P, I encounter a volatility band that is poised to pinch shut in a month or two, signaling (according to prior trend) that the S&P could dip back down to around 900.

In the weeks ending 6/27 and 8/01, as the S&P

500 tried to move up, the market pulled itself back down to its original position, stunting any progress made during that time. And others looking at the wave pattern between 2002 and the present might say that the recent uptrend is the halfway mark of an evolving triple top.

But the recent strong show of support and the amazing momentum established as the S&P 500 broke through those Fibonacci levels shows that this bull will, in all probability, surpass the double top that has already been established (note the highs of both July and August).

Passing the poison cup

Most recently, the Japanese glyph known as "the hanging man" formed by the open, high, low and close on 7/25 provided an opening for a new bear market over the following two weeks. But the market declined to bite on that poison pill. Instead, it recovered, and is now poised to overcome the resistance established by the hanging man.

When all is said and done, the conflict between facts on the ground and the evident life in the market may indeed signal an impending personality disorder. It certainly is driving some "older" analysts to the edge of distraction. But the adolescent bull market doesn't seem to have a disorder at all. And it's his road to drive on. Who am I to put stop signs in front of him? He looks like he'll run right through them anyway.

In a nutshell: Go long the S&P 500 from current levels (993.71) to the next major tension point at 1,083.40.

Ride the momentum as long as you can

Bryan Bottarelli

If the Fed is indeed pumping more money into the market each day, why not profit off it?

At first, it seemed like this money-pumping scheme was just a fad. But after four months of watching the markets "buy the dips," I can't help but wonder whether the Fed's pumping plan has succeeded and allowed—indeed even forced—the markets to turn the corner.

Right now, it's too soon to tell. But it's unwise not to consider the possibilities, especially if there is a low-risk way to capitalize on them. Adam and Ann have both decided to go long the S&P 500 from current levels (993.71) to the next major tension point at 1,083.40. The easiest way to profit off this move is trading the **S&P SPDR Trust (SPY:AMEX)**, commonly referred to as Spiders.

The SPRD, which stands for Standard & Poor's Depositary Receipts, is an investment trust established to hold a portfolio of securities proportionally comprised of the Standard & Poor's 500 Composite Stock Price Index. Naturally, the movement of the SPRD directly corresponds to the performance of the S&P 500.

In other words, Spiders are the S&P 500's equivalent of the QQQ index, but "pure" chartists tend to prefer the SPRD because its underlying assets are such a strong proxy for the broader market. Better yet, the Spiders pay a quarterly cash dividend based on the accumulated dividends paid by the stocks held in the SPDR Trust, minus nominal expenses. This dividend is currently around 1.529%.

For example, the top 10 holdings that make up the SPDR are: General Electric (3.18%), Microsoft (3.05%), Pfizer (2.99%), Exxon Mobil (2.66%), Wal-Mart (2.61%), Citigroup (2.44%), Johnson & Johnson (1.70%), American International Group (1.60%), IBM (1.58%) and Merck (1.51%). The total allocation of these ten companies represents 23.32% of the SPRD. The remaining allocations are comprised of companies that break down into the following sectors:

Financials (20.22%), information technology (16.11%), healthcare (14.78%), consumer staples (11.59%), industrials (10.40%), consumer discretionary (10.17%), energy (5.76%), telecommunications (3.87%), utilities (2.97%) and materials (2.65%).

As you can see, owning the SPRD is the simplest way to play an overall uptrend in the market, especially since any particular security is subject to sudden downgrading (viz. Intel's recent punishment despite its relatively strong Q2 profits).

In recent trading activity, the SPDR's 52-week low is 77.07 and the 52-week high is 102.17. As I write, it's currently trading for 100.77… and looking to trend higher. So let's profit off this move.

As a play on the current upside momentum, buy the SPRD Trust (SPY:AMEX) on dips under US$100 per share. A continued rally could push it above its 52-week high, possibly as high as US$109.

For updates on this play, stay tuned to both the next few issues of *Taipan* and your regular 247profits e-Dispatch. ■

This old-school heavy industry company is up 25% in the past two months. It could easily double from here.

Chris Dehaemer

There is something wrong with accountants spewing forth daily treatises on the stock market. First, of course, because the stock market is itself a leading indicator. GDP, jobless claims, consumer sentiment, and an entire quivering multitude—a perennial army—of chest-pounding economic indicators tell you nothing about where the NASDAQ, DOW or S&P 500 are actually heading… only where they've been. It's like riding backwards in the Acela from New York to Baltimore.

Real-time sentiment

The market is a real-time indicator. It accurately gauges the "value" of stocks at any given moment. Don't get me wrong: I'm not an "efficient market" theorist. I make my money off the inefficiencies I discover lurking below the algae growth of Wall Street, not on the myth of index funds.

But for some reason, those who carry letters after their names… suffixes like bulwarks against thought… continue to propagate rehashed Accounting 102 lessons.

I've been listening to money supply arguments since I became a professional trader seven years ago. I have yet to make a single dollar based on M1, M2 or M3 arguments. Perhaps I have a short attention span and can't maintain focus on decade-long investment theories.

Maybe it's just that I have yet to trade that long. You need to be an adept thinker with a fortune already made or lost to fully comprehend such glacial movements in world economic affairs.

Still, I'm not opposed to a stark fact when it stands in front me, hands on hips, like a freshman college girl wearing nothing but spandex and a smile that curls up at the corners. The U.S. dollar is that femme fatale, and it is worth contemplating the drama that will surround her fall.

Everything has an edge from which, once passed, it cannot return—a tipping point, to use the vernacular—and we are likely in the very early stages of a redoubtable teeter-totter that will send real, hard, pulsating assets to the heavens… even as it sends currencies across the plank and down to the depths.

Major trends run with generations. For the past 20 years, we've seen an era of solid equities. During this time, an entire generation has grown up never having made any money in gold, silver or copper. That's a lot of potential buyers.

Remember the Gipper?

For the last twenty years, the United States has been buying goods from other countries and exporting debt. For the past five years, this trend has taken on epic proportions. In the Reagan years of the late 1980's, trade was a hot issue. It was a time when the Japanese could do no wrong. They were buying Rockefeller Center and their cars had put Detroit out of work.

America became a debtor nation, and its current account deficit exceeded 1% of GDP for the first time. From 1984 to 1989, the cumulative current account deficit totaled 16% of GDP. Over those five years, the dollar declined by half.

Comparing today's current account deficit to that of the mid 1980's is like comparing Vinnie Jones to Ralph Macchio. In the six years from 1998 to 2003, the cumulative current account deficit totaled 23% of GDP. That's 50% more than the worst years of the 1980's.

The trade deficit in 2003 will be twice that of 1989, and next year's deficit looks to be even bigger.

A race to the bottom

Part of the problem is that China, from a political standpoint, can't afford to increase the value of its currency. There is a de facto deal between the Chinese leaders and the people. The people will continue to make more every year, and in return they won't overthrow the government and replace it with a democracy.

This has historical precedents in Indonesia, Thailand, South Korea, Japan, Singapore, Hong Kong and Malaysia. (Of course, it only works for about 30 years before a popular uprising occurs.) The only way China can continue its ersatz miracle of 10% annual GDP growth is to be the exporter of last resort to America's buyer of last resort.

If the dollar falls and the RMB goes up, the US

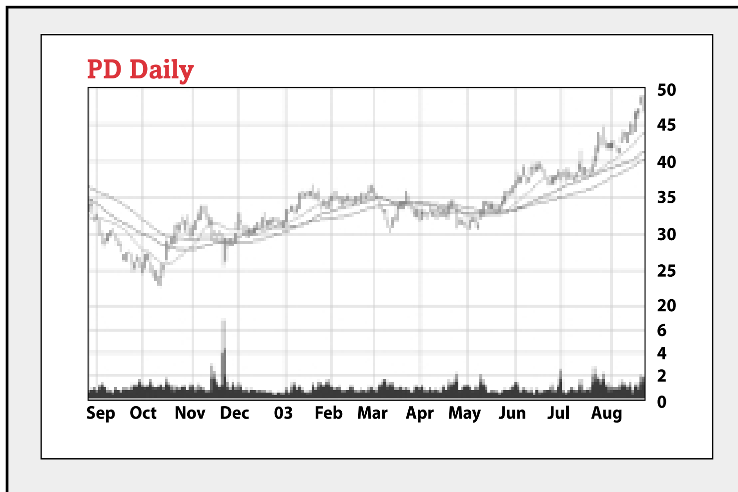
consumer, already carrying a massive debt load, will no longer buy those no longer cheap Chinese goods. This will cause political instability in China.

The boxers, round two

Currencies have to fall against something, and the US dollar can't fall against the RMB or the 40-odd other currencies that are chained to it. Add to this the historical fact that currencies fail about once every 35 years—think Richard Nixon and the end of the gold standard, or the 1944 Breton Woods Accord.

Since global currencies must go down against something, they will have to fall against things that have intrinsic value. In my mind, these things are commodities like gold, copper and palladium.

Today I want to talk copper, specifically **Phelps Dodge (PD:NYSE).** As you can tell by the chart, Phelps has finally broken its downtrend. This chart looks decidedly bullish over the past year.



As you would expect, money flow has climbed from the negative into the 250 million dollar range. This is because operating income went from a loss of 10.2 million in Q2 2002 to a gain of 17.2 million in Q2 2003.

The company continues in a lean and mean phase of operation in which it is attempting to bring production costs down below 60 cents a pound. This has already helped save US$76 million in Q2 alone.

But the real story here is the other side. The New York Commodity Exchange (COMEX) averaged 74.7 cents and 74.1 cents in Q2 of 2003 and 2002, respectively—and 75.4 cents and 73.2 cents in the respective first halves.

Copper deficit

More importantly, Phelps Dodge sees a global copper deficit in 2003 as the U.S. and European economies grow. Chinese copper consumption alone has been growing at rates above 15% year-on-year. This would indicate a copper price between 75 and 78 cents a pound going into the second half. Recently, COMEX saw September copper futures at 81.50 cents a pound.

Add to this the fact that Iraqis have scavenged their telephone wires and sold them for scrap.
They will have to be replaced.

Furthermore, the entire electric grid in the U.S. will now have to be buttressed to prevent further blackouts. All this takes copper. PD is the one to sell it to them.

Buy Phelps Dodge (PD:NYSE) under US$47 as a conservative contrarian play on the global economic rebound. ■

KVH Industries up 84%, Orbital Sciences up 80%, and DHB Industries up 12%... all this year!

Let's make it 4 for 4: Buy this US$0.75 military tech stock I think will be worth US$20 by 2008

Brian Hicks

The Value Stock Screen has been destroying the market. This year in the pages of *Taipan*, I've recommended KVH Industries (KVHI:NASDAQ), Orbital Sciences (ORB:NYSE), and DHB Industries (DHB:AMEX). All were selected by the Value Stock Screen system, and all were indirect plays on the surging defense budget.

On August 18, I recommended selling KVH

over, please...

Industries in the 247profits e-Dispatch. If you sold, you should've reaped a profit of about 84%. Not bad, considering we held this stock for just about two and a half months.

KVH Industries was an indirect play on the US military, as the company's GPS navigation units are installed in every M1 Abrams battle tank and every Bradley fighting vehicle.

But that's not the only reason why I recommended the stock. I also recommended it because of its growth prospects in the satellite television market for automobiles.

In early 2003, I recommended satellite stock Orbital Sciences for US$5 a share.

Orbital Sciences will be instrumental in the US ground-based missile defense system, which, after the recent saber-rattling by the North Koreans, is now a priority in the Pentagon.

Then, in the June issue of *Taipan*, I recommended shares of DHB Industries (DHB:AMEX) for US$4 a share.

DHB makes "battle rattle"—combat vests for the US military. The company has an 80% share of the military market, and considering that Iraq is slowly slipping into a quagmire, that will probably increase in the coming years.

If you see a theme in these recommendations, you're right. I love defense stocks. In fact, I'm a raging bull on defense. Here's why:

Welcome to Fortress America

A few weeks ago, the defense budget for the second quarter was released. *Mind-blowing* is all I can say.

Next year, the Defense Department will receive a budget of US$399 billion.

To give you an idea of how big that is, if you add up the defense budgets of the next 21 largest countries (in terms of their defense spending), America's is bigger than all of them… combined!

In fact, if the Department of Defense were a country, it would have the 18th largest economy in the world!

Over the next six years—between FY04 and FY09—the US will spend an estimated US$2.8 trillion on defense.

Now, three defense contractors will get the lion's share of the booty: Lockheed Martin, Northrop Grumman and Boeing. But there are smaller companies that will also get a share of the pie. These are the companies that are developing high tech systems to push the US light years ahead of its enemies.

The Pentagon's "Land Warrior" project

The Pentagon is currently working on something called the Land Warrior project. One of the goals of Land Warrior is to turn US combat troops into fully digitized, fully wired soldiers.

By 2008, all US soldiers will be outfitted with "wearable" PC's that'll connect them to commanders back at headquarters.

When this happens, an outfit called **Xybernaut (XYBR:NASDAQ)** will be one of the companies supplying the DoD with these wearable computers.

It's already in the works

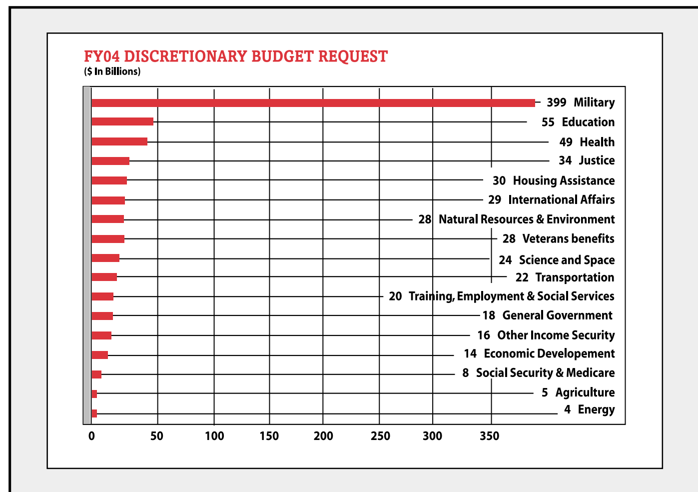
As with all new technologies, there's a lot of hype about commercial uses for wearable PC's. But it's usually the military that actually tests the systems and proves them as viable technologies. This is the case with wearable computers.

The Army has spent US$400 million developing this program over the past five years, so it's pretty much a done deal. And many units in Iraq have been testing these systems. If you've seen soldiers in news footage wearing headsets, visors, and microphones, then you've already seen the early versions of Xybernaut's wearable PC's.

Quite frankly, I can't do justice to Xybernaut's technology in just a page or two. I urge you to visit their website and see for yourself how dramatic the technology is.

More importantly, you'll see that Xybernaut's wearable PC technology also has broad applications in the private sector.

So, like the systems from Orbital and KVH Industries, Xybernaut's technology will penetrate



markets other than the military, giving them multiple revenue streams.

The stock currently trades for US$0.75 a share. But, given the broad appeal of its technology, I look for this stock to go to much higher levels in the years to come.

I'm recommending Xybernaut (XYBR:NASDAQ) at current levels. My 12-month target is US$2.00 a share. ■

A Chinese gem under US$4!

Siu-Yee Ng

There are abundant opportunities for investing in international securities. And many investors around the world are looking to diversify their portfolios in the global market. But creating offshore accounts or finding a broker overseas is complex and in many cases costly. That's why the American Depository Receipt (ADR) is a great way to add global investments to your portfolio.

ADR's offer many other benefits. One important one is that an ADR publicly traded in the US must be registered with the SEC. That means the company must file on time and follow certain US rules and regulations.

And, as we've seen in our China Yuchai (CYD:NYSE) play, dividends must be paid promptly and in US dollars. Dividend payments from Yuchai are coming in September, even if you sold for a gain of 288% following our alert in the 247profits e-Dispatch and on the *Taipan* website.

Our other ADR plays include Zindart (ZNDT:NASDAQ), up 27%, Quinenco S.A. (LQ:NYSE), up 55%, and SGL Carbon (SGG:NYSE), up 62%. Just by adding these positions to your portfolio, you've invested in China, Germany and Chile. So you see, ADR's offer a simple way to diversify and invest in the international market without having your cash leave the US.

Another important benefit of ADR's is the interest they elicit from institutional investors. You see, many institutions are restricted from investing in companies that don't trade on the US exchanges. So ADR's are the best way for them to participate in the global market. With the support of institutions, US listed ADR's are a good bet.

And this month I've found another Chinese gem that's both profitable and trades for under US$4. But I'll get to that in a minute.

QVC junkie

First, let me tell you that this is no mom-and-pop business. First-quarter 2003 sales came in at US$11.1 million. North America accounts for 75% of its sales. Twenty-seven of the largest jewelry retailers in the US are among its customers, the biggest being QVC.

QVC is nothing to laugh about. It has an audience of 73 million households in the US alone, with another 7 million in Germany and 7.8 million in the United Kingdom and Ireland. I know a number of people who are addicted to buying on QVC.

Other big-name customers include JC Penney, Macy's, Helzberg Diamonds, Wal-Mart, Mervyn's, Ben Bridge and Zales. And this company also has a

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strategy for taking over the European market.

But what gets me really excited is that this company is strategically positioned to seize marketing opportunities in China now that that country has joined the World Trade Organization. On top of that, the company has just announced that it is opening its first sales and marketing facility in the US to further its expansion.

A girl's best friend

LJ International Inc. (JADE: NASDAQ) is based in Hong Kong with production facilities in southern China. Its "mine-to-market" strategy eliminates the middleman to ensure tighter and more efficient quality control.

What this means is that LJ does everything, from designing and branding to marketing and distributing a complete range of fine jewelry. Its vertically integrated structure gives it significant advantages over its competitors. Because LJ International has cut out the middleman, all profits from value-added processes are captured internally, rather than shared with third-party manufacturers. Not only does this increase profits for the company, but retailers also benefit from the competitive pricing.

You may have seen its Lorenzo brand name with retailers in Europe and North America. The US and Canada account for nearly 75% of sales. Although the company specializes in the semi-precious jewelry segment, it also offers high-end pieces set in yellow gold, white gold, platinum or sterling silver and adorned with semi-precious stones, diamonds, pearls and precious stones.

The company offers finished jewelry (some 5,000 styles of earrings, necklaces, pendants, rings, watches and bracelets selling for US$30 to US$999) and loose gemstones (more than four million carats annually).

Turning a profit

When the market was good, LJ International's sales were, too. But when the market went sour, so did the company's profits. In 2002, it actually recorded a loss after years of profitability.

But for the first quarter of 2003, LJ has already seen sales rise by 5%. And its gross profit margin rose to 30%, from 28% in the same period last year.

LJ International recently added several major national accounts and booked US$15 million in early Christmas orders from new and existing clients.

Management was obviously thinking about shareholder value when it announced that it has the option to repurchase up to 1,000,000 shares of common stock. Since March 31, 2003, it has repurchased 318,200 shares.

JADE had a huge run-up in July ahead of its earnings announcement. Prior to the announcement, the stock had been trading in the US$1 to US$1.50 range since the beginning of the year.

In July there was heavy accumulation of the stock. And after it broke US$5, there was profit-taking. But looking at the chart, you can see that the buying volume in July surpassed the current selling volume. Because JADE has a market cap of only around US$28 million, the wave of selling was enough to make it pull back to the US$3 level.

There seems to be support at US$3. After a strong quarter, and with lots of orders on the books, the stock has been on a tear since June. Even institutions are beginning to take notice.

Take advantage of this healthy pullback and buy LJ International (JADE: NASDAQ) under US$3.75.

TAIPAN

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