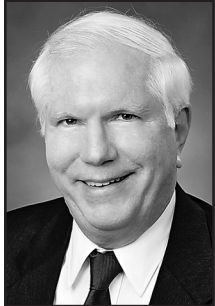

Investor's HOTLINE

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November 2007

Exclusive sound-wealth wisdom from the world's leading financial experts



Forenotes from JOE BRADLEY

November Guests

1. **Lew Rockwell**, the man in charge at the Ludwig von Mises Institute, joins us to discuss the interplay of government and economics, particularly with regard to current crises; he covers the blunders that he sees resulting from government interference with the marketplace.
2. The underlying philosophy of IH is a belief in the integrity of free market economics, of which the great economist Ludwig von Mises is the originator and cornerstone; an understanding of free market economics is not necessary to make money, but it sure does help.
3. **Robert Hsu**, a fund manager and newsletter editor who specializes in China, shares his insights for investing in that complicated market; he was born in China, speaks fluent Mandarin and maintains contracts in mainland China.
4. The highly volatile Chinese market is certainly not a favorite of value investors, but most IH guests agree that it is a key investment area that will undoubtedly surpass the US in growth opportunity.
5. Release date is Friday, Oct. 19; the interviews were completed the week previous.

Updates from the IH Roster

1. Atlas Mining (ALMI), one of Jim Kennedy's picks, recently took a big hit; at press time, Kennedy said the problem was uncertainty on some accounting issues and about the extent of some ore deposits; he believes that ALMI is a hold until new management provides clarification.
2. Mary Anne Aden notes that a strong C rise (the strongest up-move within gold's recurring cycle) is underway; the fact that gold has now reached a new bull market high and is on its way to test the 1980 peak near \$850 is super bullish; this is a time to buy new positions and hold the ones you have.

LLEWELLYN H. ROCKWELL, JR.

Ludwig von Mises Institute
518 West Magnolia Ave.
Auburn, AL 368432
Tel: 334-321-2100 Fax: 334-321-2119
Email: contact@mises.org
Web: www.mises.org
www.lewrockwell.com



The Philosophy of Ludwig von Mises

1. The Ludwig von Mises Institute is a non-political, educational organization dedicated to the position that government should not run people's lives or the economy; to the extent that government does interfere, everyone is less free.

3. An upcoming issue will feature David Swenson, manager for Yale University's endowment; meanwhile, Swenson shared the asset allocation with Joe that has earned a 15%–17% return for 20 years: in traditional assets—US, 12%, foreign 15%; US bonds 4%; and in alternatives—absolute return, 25%, real assets (real estate, timber, oil & gas), 27%; private equity, 17%.

Analysis of Fed Action

1. Money manager Peter Schiff declares Bernanke's 50-basis points cuts in the Fed funds and discount rates to be an irresponsible, cowardly act that will likely encourage America's creditors around the world to refuse to continue funding US deficits.
2. According to Schiff, the brave thing would have been to raise rates and allow market forces to purge the economy of the imbalances built up during the Greenspan bubbles.
3. Had the Fed done nothing or raised rates, the economy would have tipped toward a severe but cleansing recession; rate cuts set up something worse—the acceleration of the rise in consumer prices and eventually a rise in long-term interest rates.
4. Ironically, Alan Greenspan accepts no responsibility for setting up the problems while predicting double-digit interest rates and inflation; he has personally diversified out of the USD.

End-of-the-Year Resource for Gifts and Tax Planning

1. Mike Kuschmann of Fine Arts, Ltd. can help you with gift suggestions of fine art and collectibles and negotiate discounts for you from the retail prices posted by art galleries and stores; a number of IH members and associates, including Joe Bradley, have benefited from Mike's services.
2. Mike also has a successful tax strategy utilizing artwork that could reduce your income taxes if you act before the end of the year.
3. For a complimentary information package, contact Mike Kuschmann, Fine Arts, Ltd., 174 W. Comstock Ave, Ste. 101, Winter Park, FL 32789; (phone) 800-229-4322; (email) mkuschmann@cfl.rr.com.

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2. Mises was a champion of laissez-faire economics; his book *The Theory of Money and Credit* (1912) predicted that a central bank (the Federal Reserve came into existence in 1913) would inflate the currency and initiate the business cycle of recessions, depressions and artificial booms.
3. In the early 1920s, Mises was the first to explain why socialism/communism would of necessity be an economic disaster—because it provided no way to determine the proper use of resources short of controlling prices and nationalizing the means of production, ultimately resulting in chaos and destruction in the markets.
4. Libertarianism is a political philosophy that embraces Lord Acton's principal that liberty is the highest political goal; from freedom flows order, prosperity and all of human civilization.
5. Mises acknowledged government as the hangman, but a hangman is not often needed—certainly not needed in the affairs of daily life.

6. Despite the fact that government programs have consistently generated more of what they were created to eliminate (poverty, crime, drugs, etc.), both Democratic and Republican administrations have increased the size of government; government has failed the taxpayer, but it has satisfied itself and interest groups.

Ideal Foreign Policy

1. George Washington laid out the proper foreign policy in his Farewell Address—aim to have trade, commerce and honest friendship with all nations, but as little political connection with them as possible; Jefferson warned about having “no entangling alliances.”

2. The United States was designed to be a commercial republic, but today it is a world empire with many bad effects for itself and many other countries—Washington, D.C. would like to govern the world; that orientation means a lot of money for a lot of people.

3. People go into politics to seek power, which contradicts a politician being a more sober, limited magistrate as the Founding Fathers envisioned.

4. The vast military-industrial complex benefits from the waging of war whether successful or not; that fact accounts for the continuation of the Iraq war despite its failure to meet the standards the Bush administration set.

Changes Recommended for the Next President

1. The changes Rockwell would like to see would require that the next president be totally dedicated to the Constitution and not inclined to take dictatorial action.

2. The right president (a Ron Paul) would order the end of wars and bring home all American troops.

3. The president would repeal all unconstitutional executive orders—which have been plentiful since Woodrow Wilson.

4. The president should talk to the American people about what is needed to fix the economy and why—underlying factors are the need for a free market and a gold standard.

Climate for Change

1. The positive response to the candidacy of Ron Paul, especially among young people, indicates that the country is far more ready for a leader with integrity than most people, including Rockwell, thought.

2. The work of Libertarian intellectuals over the last 75 years plus the total disaster of the Bush administration in economics and foreign policy have plowed the field for Libertarian seed; many people, even non-intellectuals, have the correct feeling that something is fundamentally wrong in America.

3. High price-inflation already exists; the subprime mortgage crisis and the actions of Bernanke and the Fed pumping new money will make inflation worse; another business cycle is building up that means trouble for the future.

4. The US government has grown to be the biggest, richest, most powerful government in the history of the world; as such it is far more bureaucratic and far less effective; radical change is required.

Reemergence of the Inflation Threat

1. The problems of the 1970s are back but ten-times worse; inflation will have to come to an end at some point; after Nixon’s horrendous inflation of the 1970s, the Fed actually did cut back the money supply for a short time under Volker to good effect.

2. Serious reform is very possible again because even Bernanke does not want hyperinflation and the USD plummeting in international exchange.

3. Bill Gross’s recommendation that the government bail out homeowners

faced with foreclosure from the credit crisis is a fascist proposal; the US economy already has fascist, corporate-state elements.

4. If such a bailout does happen, there will be price and wage controls and hidden runaway inflation or open runaway inflation—with horrific effects either way.

5. The Fed probably has more tricks left, but they are laying up trouble for the future and placing vast burdens on present producers, savers and investors; when the end finally comes, it will likely be from an unexpected source.

The Place of Gold

1. Regrettably, gold is not money—the US and allies succeeded in demonetizing gold; however, it retains appeal in many other senses; holding some gold is prudent.

2. America’s empire depends on the USD remaining the world’s reserve currency, but that status is being endangered by Fed pumping and by the political hatred engendered by US foreign policy; the situation for the US and the USD is shaky.

3. At some point, some country will have political change toward a central bank that won’t follow the US pattern; gold would then really start to move.

The Health Care Issue

1. US Comptroller General David Walker has been trying to alert people to the severity of the problem; the prescription drug program dwarfs the Social Security problem; the offer to subsidize drugs for seniors will only serve to drive drug prices higher; if there ever were the political will, such actions of political theft would cease.

2. Hilary Clinton’s health care proposal will not solve the problem; however, since Lyndon Johnson, the Republicans are more responsible than Democrats for government intervention in medical care.

3. The solution is to get government out of health care to the extent possible; the ultimate solution is no government whatsoever involved in medicine (no government spending allowed); obvious obstacles to overcome are the ban on importing pharmaceutical drugs and the requirement to have a prescription to purchase drugs.

The Immigration Problem

1. Ron Paul believes that the Fourteenth Amendment has been illegitimately interpreted to mean birthright citizenship; many countries do not automatically grant citizenship to children born of non-citizens, especially of those there to get welfare.

2. Nobody should be able to come to the United States and get on welfare or receive any government-provided services, including public schooling and Medicaid; having open borders for our welfare state has created numerous problems.

3. On the other hand, immigration reformers who want to empower the federal government to put businessmen in jail for hiring the wrong people are on the wrong track; businessmen face a dilemma of needing to document legality without requiring too much ID, which is considered discriminatory.

4. The end of the housing bubble will resolve some of the problem because many illegal aliens will return home as construction jobs dry up in the US.

Effects of the “Flat World”

1. International trade and an emerging borderless economy are negatively impacting traditional, imperial nation states; the Internet is a major driver.

2. Libertarianism and Ron Paul’s campaign for president are doing well

largely because of the Internet; news and commentary are instantaneously available all over the world; this factor has been a huge advantage to people who want liberty.

Iraq Analysis

1. If events had worked out as the neo-conservatives anticipated—i.e., a cakewalk with Iraqis welcoming US soldiers, the war could have ended quickly; however, the population resented and resisted foreign occupation.
2. Bringing about fighting among various Iraqi groups is now in the interests of the US; the first contrived act of the occupation after the fall of Hussein was to grant in perpetuity 14 huge military bases to the US government—from the outset, the US has had no intentions of leaving.
3. The goal of the US is to remain in the Middle East forever in order to rule the oil as a control factor over nations around the world; with troops in 150 countries, the US has established a world empire.

Counter-Terrorism Tactics

1. Tactics such as phone surveillance (spying on the population) are totalitarian; every government will follow an impulse in that direction if the people allow it.
2. The counter-terrorist activities are part of government wanting the power to control people's lives.

3. Terrorism is the form of war for poor people who cannot afford more costly weapons; Robert Pape's book [*Dying to Win: The Strategic Logic of Suicide Terrorism*] finds the common denominator of suicide terrorism to be resistance to foreign occupation.

4. The answer to stopping terrorists is: "Don't stick a stick in the hornet's nest;" terrorism is the response to US foreign policy, so the US should leave other people alone in order to live in peace.

5. The government should also leave the American people alone; the concept of not interfering is the primary key to both peace and prosperity.

6. Since the government is not inclined to reform its policy, further terrorist attacks are possible.

7. Giving the government any more power to spy on its people and run their lives will simply make government even more bureaucratic; it will result in the loss of more liberty but not guarantee any greater safety.

The Reason to Be Optimistic

1. The positive response of hundreds of thousands of young people across the country to Ron Paul is cause to be optimistic; they understand free markets and that the Federal Reserve is not good; they support a policy of peace and non-intervention as the Founding Fathers intended.

2. The fact that the Libertarian movement is vast and growing is hopeful.

ROBERT HSU

Absolute Return Capital Advisors, LLC
1901 Avenue of the Stars, 2nd Floor
Los Angeles, CA 90067
Tel: 310-275-3731 Fax: 310-461-1419
Email: lucia@themoneyfactory.com
Web: www.themoneyfactory.com
Newsletters Tel: 800-539-8215
China Strategy: www.chinaprofitstrategy.com
Asia Edge: www.asiapacificedge.com



Investment History

1. Hsu began his career in the hedge fund world before hedge funds were widely known; he was among the first in his generation to pursue that avenue seriously; his China focus reports came later.
2. He has come full circle with the launch in July 2007 of the Pearl River Greater China Opportunity Fund, which he manages.

Risk Analysis

1. Hsu manages money for investors who conservatively aim for 10%–12% a year with no down year, as well as those who want to participate in China's economic growth aggressively; the contrasting approaches can easily be combined by focusing on truly good investments—the best defense is a good offense.

2. Conservative investors can benefit from having a small percentage invested in higher-volatility/higher return instruments like China to enhance portfolio returns.

3. The perception of risk is sometimes greater than the reality of risk; during the July–August financial meltdown, the Chinese market provided the only safe harbor because China is isolated from the credit market crisis in the US.

4. The Chinese stock market experienced no liquidity drain because it is fueled primarily by domestic investors; the Bank of China had about \$10 billion exposure to mortgage-backed securities, but most Chinese banks have none.

Hsu's China Strategy

1. China's economic development is being driven by the Chinese people; Hsu concentrates on private sector companies instead of state-owned enterprises.

2. He believes that private entrepreneurs will always win against bureaucrats, given a level playing field; however, heavily regulated industries where state-owned enterprises have monopolistic power are an exception to rule #1.

3. He looks for companies that have a long-term, sustainable, competitive advantage with ability to be a leader in its industry.

4. Hsu is essentially a growth investor because China is the fastest growing economy; therefore, he focuses on growth rate and profit margin rather than on valuation—the profitability of these companies can grow into a

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valuation; earnings are growing at an average of 30%–40% a year—many holdings are growing at 100%.

The Information Challenge

1. Getting reliable information from smaller Chinese companies is difficult, but the industry leaders that are listed on NYSE or NASDAQ or Hong Kong usually put out good information and are easy to monitor.
2. Hsu avoids Shanghai and Shenzhen listings because their regulation is more lax.
3. Hsu's firm has a team of analysts in China who gather intelligence; Hsu goes to China several times a year and always visits companies.

China Funds

1. Of the 25 stocks in the iShares China index (FXI), all are state controlled—a number of them are monopolies or near-monopolies; Hsu approves of about six or seven components of the index but would stay away from the rest; FXI was developed by China's propaganda ministry in conjunction with the *Financial Times*.
2. The closed-end fund, Morgan Stanley China A Share Fund (CAF), is a play on the Shanghai stock exchange boom; one of the few ways non-mainland investors can access the Shanghai bull market, it provided a good hedge in early August against the US liquidity crisis.
3. Most mutual funds investing in China are using Chinese stocks listed in Hong Kong, not Shanghai; globalization of capital has resulted in global equity markets becoming increasingly correlated—Shanghai is the only major market negatively correlated with the S&P 500; over the last five months, CAF is up 65%–70%.

Market Forecasts

1. Awareness of risk has increased, and appetite for risk has decreased among global investors; the liquidity crisis will probably take two or three years to play out and is likely to be painful in the credit markets; there should be a real economic slowdown in the US.
2. Equity markets may not be affected too much because the Fed will be ready to provide liquidity.

Advice on Taking Positions in China

1. An investor's strategy depends on timeframe, risk tolerance and other personal issues.
2. Given that China appears to be in a long-term bull market, every correction should be viewed as a buying opportunity; corrections can be as large as 20%–25%; Hsu sees no risk of a bear market over the next year.
3. Depending on the Beijing summer Olympics to keep the Chinese market strong is too conventional; Hsu's edge in investing is beating the pack by thinking unconventionally.

Top Pick for China

1. Mindray Medical (NYSE:MR; around \$42) is China's leading medical device company; earnings and revenue have grown at 50%+ for five years—most recent quarter earnings were up 100%; MR is a low-cost producer and a technological leader, especially in ultrasound equipment.
2. MR is at the epicenter of three major trends: aging population globally (demand for health care), China's economic emergence and pressure to control health care costs; the stock is a buy as long it maintains annual earnings and revenue growth; downside volatility could easily be 25%.
3. Do not be concerned about a drop resulting from reasons that have nothing to do with the company; if a drop occurs because of company-specific issues, don't wait for a 25% drop to get out; growth investors need to keep their money in companies that are growing.

More China Favorites

1. Hsu's favorite sector in China is consumer cyclical companies; Chinese consumers have been saving at a 35% rate, and credit card penetration is only 3%—but Chinese consumers are going to start spending money.
2. CNOOC (NYSE:CEO; around \$150), the China National Offshore Oil Corporation, has a monopoly on drilling rights in the South China Sea, where there are likely undiscovered oil and gas reserves.
3. Any company drilling there must partner with CNOOC and give the company 51% of profits; the stock is a buy as long as the oil price moves higher; the stock benefits both from higher energy prices and appreciation of the Chinese yuan.
4. Ctrip.com International (NASDAQ:CTRP; around \$53) is up 200% since Hsu recommended it in March 2007; the company makes money by booking airline and hotel reservations; it is the leader in its field in China; the stock taps into China's consumer spending boom.
5. China Mobile (NYSE:CHL; around \$82) is the world's biggest wireless communication operator; the company is a state-owned enterprise with a 75% share of the cell phone market in China; it is growing rapidly from expansion into rural parts of China.

Thoughts on Indirect Plays

1. Although some analysts recommend playing China by taking positions in companies that do business there (such as Caterpillar and Siemens), Hsu thinks that the amount of business many of these companies do in China is not enough to make them a true China play.
2. A number of mining and semi-conductor companies that do get a lot of business from China are real China plays; one example is Companhia Vale do Rio Doce (NYSE:RIO) a Brazilian iron ore-nickel giant that gets 20%+ of its business from China; RIO also benefits from a run up in commodity prices; RIO has doubled since March 2007.
3. Yum! Brands (NYSE:YUM; around \$35) is the holding company for Kentucky Fried Chicken, Pizza Hut and Taco Bell; YUM is the single biggest restaurant operator in China (22% of YUM's business); buy on dips because YUM is not growing as fast as other picks.
4. The Chinese companies may be considered buys as long as the Chinese yuan keeps appreciating and the companies keep delivering earnings growth of 30%–50%.

Potential Ten-Bagger

Hsu's choice from his favorites of the one stock that has the greatest potential over the long haul is Mindray Medical; it would be a stock he would select for the portfolio of his children.

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