Prudential Equity Group, Inc.

RESEARCH

January 21, 2004

CHINA FOR INVESTORS II: THE GAMES

Topical Study #63

All important disclosures can be found at the end of this report

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Prudential Financial

I. The Growth Imperative: A Houston Per Month

The outlook for China's economy has become a major issue among Wall Street's investment strategists and Main Street's portfolio managers. The pessimists warn that China's boom is unsustainable. They see signs that even the Chinese recognize this and are taking steps to cool their economy before the boom turns into a bust. Such a slowdown could depress the global economy, corporate profits, and stock prices.

I am not convinced. I believe that China is driven by a "Growth Imperative."[1] I believe the country must grow rapidly to absorb the huge number of new entrants into the labor force every year and to meet the needs of the large number of people who are leaving the rural areas and moving to the urban centers. To accommodate the roughly 20 million people per year migrating to the cities, the Chinese, in effect, have to build a Houston, Texas, per month (Figure 1)! This is why industrial commodity prices and ocean shipping rates have been rising ever since China joined the World Trade Organization (WTO) on December 11, 2001. In recent months both have been soaring, suggesting that China's boom is picking up speed rather than slowing down (Figures 2 and 3).

II. Big Bangs

In my "1990s Replay Scenario" I've listed the numerous similarities between the current decade and the prior one.[2] Both started with similar "Big Bangs." The end of the Cold War at the beginning of the 1990s unleashed globalization, i.e., more open and more competitive markets around the world. During that decade my major investment theme was that the end of the Cold War was wildly bullish.[3] I argued that globalization would bring down inflation and interest rates, boost global prosperity, and push stock prices higher.

I believe that another bullish Big Bang occurred on December 11, 2001, when China joined the WTO. This was a major milestone on the road to globalization. Globalization is bullish because free trade increases the prosperity of consumers around the world. Global competition promotes innovation and productivity. So it also tends to be disinflationary. The resulting "good times" tend to be good for profits and stock prices.

During the 1990s, the emergence of the so-called Asian Tiger economies helped to push global inflation down as their exports of inexpensive consumer goods soared. But their economic booms also pushed industrial commodity prices higher from 1993 through 1996. The Asian Crises of 1997 and 1998 caused commodity prices to tumble (Figure 2).

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[1] Topical Study #62, ***China For Investors I: The Growth Imperative***, November 7, 2003, http://www.cm1.prusec.com/yararch.nsf/(Files)/t_110703.pdf/$file/t_110703.pdf.
[2] "Fearless Forecast 2004: Rooting For Déjà Vu All Over Again," December 30, 2003, http://www.cm1.prusec.com/yararch.nsf/(Files)/FearlessForecast2004.pdf/$file/FearlessForecast2004.pdf
[3] Topical Study #20, ***The Collapse Of Communism Is Bullish,*** September 4, 1991, and Topical Study #23, ***The End Of The Cold War Is Bullish,*** September 10, 1993.

During the current decade, China is the main source of deflationary pressure on consumer goods prices and the main reason that commodity prices are soaring once again. China's exports are soaring, but so are the country's imports of raw materials, food, and machinery. While China's Growth Imperative is mostly demographically driven, the Chinese are also driven by their obsession with preparing the entire country, not just Beijing, for the Summer Olympics of 2008, which is the next bullish Big Bang, in my opinion.

China's Summer Olympics may be one of the main reasons why the Chinese are pushing their economy so fast. They are preparing the country to impress the world with their achievements. They have to find jobs and housing for all the masses of people moving into the cities to prevent the proliferation of shanty towns, disease, and social and political instability. Once the games are over, there could be a significant slowdown in China's economy that could be bad news for the global economy, which is becoming more and more reliant on China's economy. This outlook fits my 1990s Replay Scenario extremely well: There was an Asian Crisis in 1998 and there could be another in 2008!

III. Bottlenecks

Fall 2008 is still more than four years away. So does China's Growth Imperative mean that boom times might continue through 2008? I hope so. My bullish outlook for stocks in 2004 and 2005 would be more likely to happen. My targets for the S&P 500 are 1300 and 1440 for the end of 2004 and 2005, respectively.

What could go wrong between now and 2008? There could be shortages of key commodities necessary to sustain the China-led global boom. Too much of a good thing might not be so good. For example, let's have a look at steel. The Chinese need lots of it to build a Houston a month. Chinese steel production is estimated to have grown by about 22% last year, or almost three times the rate of its GDP growth of 9.1%.[4] The Chinese have built several steel plants to convert scrap steel into beams for office and apartment buildings.

The problem is that scrap steel is quickly becoming a very scarce commodity. When China joined the WTO at the end of 2001, a gross ton of scrap steel cost $57. The price more than doubled to $127 by the end of last year. In recent weeks it soared to $150 (Figure 4).

Chinese steel producers are scrambling to purchase more iron ore. So are other steel producers around the world who are also enjoying big orders from the Chinese. Japan is one of the leading suppliers of steel to China. In mid-January, BHP Billiton Ltd. and Rio Tinto Ltd. raised the price of iron ore exports to Japan's Nippon Steel Corp. by almost 19%. This matches the price increase negotiated recently between the world's biggest iron ore exporter, located in Brazil, and the world's biggest steelmaker, Europe's Arcelar S.A.

[4] "Iron ore feels the China effect," *Financial Times*, January 15, 2004.

Undoubtedly, steel industry analysts around the world should respond to soaring steel demand and prices by raising their earnings estimates. They've been slow to do so for the S&P 500 steel stocks. Nevertheless, steel stock prices are up 94% since March 2003 (Figure 5). The S&P 500 steel stock index includes Allegheny Technologies, Nucor, United States Steel, and Worthington Industries. The market capitalization of these steel stocks was only $10.7 billion at the start of 2004.

IV. Oil Rush

The Chinese are scrambling to obtain lots of other commodities, particularly oil, which they must have to sustain their Growth Imperative. Most oil analysts expected a big decline in the price of crude oil following the end of the Gulf War II. Some explained that was because Iraqi oil exports recovered more slowly than expected.[5] More recently, extremely cold weather in the U.S. Northeast pushed supplies to a 29-year low and the price of a barrel of crude oil to $35 (Figure 6).

These explanations make sense, of course. Some industry analysts believe that the Bush administration has contributed to high prices by adding roughly 100,000 barrels a day to the Strategic Petroleum Reserve, or SPR (Figure 7). In my opinion, that's not very much and not enough to boost oil prices.[6]

In the spring, more output from Iraq and warmer weather should push the price of oil back down. But how far down? In my opinion, oil prices might stay above $30 a barrel for quite some time given the extraordinary increase in Chinese demand for crude oil. Over the past 12 months through October of last year, total world crude oil demand averaged a record 78 million barrels per day (Figure 8). Over this same period, China's demand rose to a record 5.2 million barrels per day. Extrapolating the trend since 1995 suggests that China should be consuming at least 7 million barrels per day by 2010 (Figure 9). China became a net oil importer in 1993 and now imports one third of its oil consumption and it is expected to import more than half of its oil by 2020, according to the National Development and Reform Commission.

The Chinese are desperate to obtain reliable, secure long-term sources of crude oil. They seem to be competing with equally desperate Japanese buyers. Both are struggling to get Russian oil. This year China is likely to overtake Japan as the world's second-largest consumer of crude oil (Figure 9). China has been negotiating with Russia for a decade to build a pipeline from the Siberian oil fields to Daqing, China's major oil city. They thought they had a deal last year but

[5] Iraq's output was back up to 1.9 million barrels a day during November 2003 despite sabotage.
[6] After 9/11, on November 13, 2001, President George W. Bush directed the Secretary of Energy to fill the SPR up to its 700 million barrel capacity. At the time, there were 545 million barrels of crude oil in the reserve. Since it was established by President Gerald Ford at the end of 1975, the SPR has been used only once during Operation Desert Storm in 1991. The government is filling the SPR with oil from a royalty-in-kind program with producers who operate leases on the federally owned Outer Continental Shelf. http://www.fe.doe.gov/programs/reserves/spr/

Japan sweetened its bid, offering to put up $5 billion for pipeline construction and another $2 billion for oil field development. China and Russia have already agreed on a $17 billion project to build a 3,055-mile natural gas pipeline from eastern Siberia to northeastern China and South Korea.[7]

According to the December 10, 2003, issue of ***People's Daily***, since early winter, seven provinces have forced blackouts in selected areas because their power grid failed to meet demand. Electricity consumption rose about 15% last year and is expected to be up another 11% this year to 2,091 billion kilowatt hours (kwh).[8] In addition to a boom in energy-intensive industries, China was plagued last year with dry spells that have reduced hydroelectric output. Also coal supplies have been inadequate. This forced officials to curb coal exports to meet domestic demand. China is the world's second-largest coal exporter after Australia. Last year, the Chinese worked on projects with a designed capacity of 29.91 million kw and the delivery of 29 million kw of new generating capacity.

V. The (Not So) Good Earth: Beans In The Teens?

China is putting upward pressure not only on industrial commodity prices such as iron ore and oil but also on food commodities, particularly grains. Starting in 1995, the country had four consecutive years of very good harvests, pushing production to a record 512 million tons during 1998. Since 2000, annual grain output has lingered at 455 million tons. China's grain output dropped to 435 million tons last year while its consumption rose to an estimated 490 million tons (Figure 10). Domestic grain prices jumped in October and November for the first time in six years pushing the year-over-year CPI inflation back up over zero to 3% (Figure 11).

China has to feed one fifth of the world's population, but has only 7% of the world's arable land. Over the past seven years, available cropland has decreased 667,000 hectares per year, on average. Local governments have been using farm land for industrial and real estate development. Water for farming is becoming scarcer and two thirds of the country's irrigation facilities are badly run down. The government plans to enact legislation to protect farm land from development.[9]

The U.S. Department of Agriculture (USDA) expects China to import a record 808 million bushels of soybeans this year, up by 55 million bushels from its October 2003 estimate and more than double the amount China imported from all sources during the 2002 marketing year. As a result, soybean prices have soared in recent months, from a 2003 low of $5.38 per bushel to $8.36 in early January. I wouldn't be surprised to see "beans in the teens" by the end of this year (Figure 11). China's food imports boom is fueling a U.S. agricultural exports boom (Figure 10). The USDA expects China to import $5.4 billion of agricultural goods from the U.S. during the current fiscal year, up from $3.5 billion during fiscal 2003.

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[7] "The Asian Battle For Russia's Oil And Gas," ***The New York Times***, January 3, 2004, p. C1.
[8] The U.S. consumed 3,660 billion kwh of electricity in 2002.
[9] "China to ensure grain security by reserving production capacity," ***People's Daily***, January 8, 2004.

VI. The Accelerator Vs. The Brakes

There are very few, if any, signs in the commodity markets that the Chinese economy is slowing. The latest batch of economic indicators suggests that it is actually speeding up. Industrial output rose 17.9% in November from a year ago, the fastest since records began in 1995. The level of production is at a record high (Figure 12). China's steel output topped 200 million tons last year, the first country to ever achieve such a high annual output of steel. During the first 11 months of last year, auto production rose 32.7% from the same period in 2002, to a record 4 million units.

Merchandise exports of China and Hong Kong combined rose 25% from a year ago in November to a record $644 billion, using the 12-month sum. The merchandise imports of China and Hong Kong nearly matched the level and growth of exports (Figure 13). Various key categories of imports into mainland China are soaring, especially capital equipment and raw materials (Figures 14 and 15).

U.S. exports to China spiked to a record high in November of last year. Over the past 12 months, they rose to a record $27 billion, about twice as much as in 2000 (Figures 16 and 17).

Chinese officials have indicated that they are concerned that their economic boom is creating excessive capacity in several key industries, including autos, steel, and concrete. Too much capacity would put downward pressure on prices and profits, increase bankruptcies, and exacerbate an already bad bad-loan problem in the financial sector. Official figures show that 21% of loans extended by the nation's four largest banks were nonperforming at the end of September. Standard & Poor's estimates the bad-loan ratio of China's state-owned banks at 45%.

The China-is-slowing (a.k.a. the-sky-is-falling) crowd observes that the authorities have already taken some steps to curb lending and investment. In June, the central bank tightened lending rates to the property market. In September, the central bank raised banks' reserve requirements. Yet, China's M2 money supply measure is up 19.6% as China's international reserves soared to a record $406 billion late last year (Figures 18 and 19).

In my opinion, the Chinese are doing what they can to achieve their awesome Growth Imperative while reducing the risks of economic and financial excesses, which could upset their goals. The naysayers among the rapidly expanding pool of China watchers say that China can't grow rapidly without causing a speculative bubble that will inevitably burst. I believe the Chinese can do it, at least until the closing session of the Summer Olympic Games in 2008.

We should monitor the auto industry to help us assess whether the naysayers might be right or wrong. My working hypothesis is that Chinese officials won't step on the brakes to slow auto production. Instead, they are already making auto financing easier to obtain to boost demand. Eventually, overextended car buyers could pose a major problem for sustainable growth in China, but not for several years, in my opinion. (Last year, in November, 10% of South Koreans over the age of 15 were classified as credit delinquents.)

According to a January 7, 2004, Reuters story, “Oversupply Threatens Profit In China Auto Boom—S&P,” Standard & Poor’s estimates that if all of the manufacturers planning to expand in China realize their ambitions, production capacity for domestic and foreign makers will be roughly 8 million units by the end of the decade, with annual sales predicted to be 6 million units.

I believe that demand for cars could be much higher by 2010. Only 15% to 20% of China’s car buyers use credit compared to a global average of 70%. In December 2003, Chinese banking regulators permitted General Motors, Toyota Motor Corp., and Volkswagen to set up auto-financing operations. On the other hand, there is no nationwide credit system, yet.

* * *

Appendix A: S&P 1500 Percentage Sales Exposure To China And Asia

Symbol	Company	Index	China Only	China Mention	Asia Pacific Only	Asia Pacific Mention
TFS	Three-Five Systems Inc	S&P 600	39.7	-	-	-
INTC	Intel Corp	S&P 500	26.3	-	-	-
HTCH	Hutchinson Tech	S&P 600	21.2	-	-	-
CRR	Carbo Ceramics Inc	S&P 600	20.0	-	-	-
CTS	CTS Corp	S&P 600	18.9	-	-	-
IGL	IMC Global Inc	S&P 400	13.4	-	-	-
BBR	Butler Mfg Co	S&P 600	11.6	-	-	-
ANDW	Andrew Corp	S&P 500	6.8	-	8.2	-
DPMI	Dupont Photomasks Inc	S&P 600	-	33.3	-	-
AMAT	Applied Materials Inc	S&P 500	-	18.8	-	-
TTC	Toro Co	S&P 600	-	18.7	-	-
NVDA	Nvidia Corp	S&P 500	-	-	64.6	-
SMTC	Semtech Corp	S&P 400	-	-	60.9	-
ICST	Integrated Circuit Systems	S&P 400	-	-	53.2	-
VSH	Vishay Intertechnology	S&P 400	-	-	36.7	-
AMD	Advanced Micro Devices	S&P 500	-	-	36.4	-
TXN	Texas Instruments Inc	S&P 500	-	-	35.2	-
IDTI	Integrated Device Tech Inc	S&P 400	-	-	30.1	-
FEIC	FEI Co	S&P 600	-	-	27.9	-
SWKS	Skyworks Solutions Inc	S&P 600	-	-	27.5	-
PMTC	Parametric Technology Corp	S&P 500	-	-	25.1	-
ADSK	Autodesk Inc	S&P 500	-	-	22.8	-
EAGL	EGL Inc	S&P 400	-	-	22.6	-
AEIS	Advanced Energy Inds Inc	S&P 600	-	-	21.8	-
SLR	Solectron Corp	S&P 500	-	-	21.5	-
MMM	3M Co	S&P 500	-	-	21.1	-
AVP	Avon Products	S&P 500	-	-	20.9	-
LZ	Lubrizol Corp	S&P 400	-	-	20.4	-
ABI	Applera Corp Applied Biosys	S&P 500	-	-	19.8	-
ZMH	Zimmer Holdings Inc	S&P 500	-	-	19.7	-
WFT	Weatherford Intl Ltd	S&P 400	-	-	18.8	-
ENR	Energizer Holdings Inc	S&P 400	-	-	18.5	-
NATI	National Instruments Corp	S&P 400	-	-	18.5	-
CRTO	Concerto Software Inc	S&P 600	-	-	18.4	-
DCI	Donaldson Co Inc	S&P 400	-	-	18.3	-
KLAC	KLA-Tencor Corp	S&P 500	-	-	18.1	-
EK	Eastman Kodak Co	S&P 500	-	-	17.5	-
MRD	MacDermid Inc	S&P 600	-	-	17.2	-
DSS	Quantum Corp	S&P 400	-	-	16.0	-
MACR	Macromedia Inc	S&P 400	-	-	15.6	-
ALTR	Altera Corp	S&P 500	-	-	15.2	-
TYC	Tyco International Ltd	S&P 500	-	-	15.0	-
CYT	Cytec Industries Inc	S&P 400	-	-	14.7	-
XLNX	Xilinx Inc	S&P 500	-	-	14.4	-
EMC	EMC Corp/Ma	S&P 500	-	-	14.2	-
ATX	Cross (A.T.) & Co -Cl A	S&P 600	-	-	14.0	-
KEM	Kemet Corp	S&P 400	-	-	13.2	-
UTX	United Technologies Corp	S&P 500	-	-	13.1	-
ISSX	Internet Security Sys Inc	S&P 400	-	-	13.0	-
MNST	Monster Worldwide Inc	S&P 500	-	-	12.9	-
SCMM	SCM Microsystems Inc	S&P 600	-	-	12.8	-
RESP	Respironics Inc	S&P 600	-	-	12.4	-
ASCL	Ascential Software Corp	S&P 400	-	-	12.0	-
NCR	NCR Corp	S&P 500	-	-	11.7	-
AVT	Avnet Inc	S&P 400	-	-	11.3	-
NATR	Natures Sunshine Prods Inc	S&P 600	-	-	11.2	-
FMC	FMC Cp	S&P 400	-	-	11.0	-
CUNO	Cuno Inc	S&P 600	-	-	10.4	-
RSAS	RSA Security Inc	S&P 400	-	-	10.0	-
LEH	Lehman Brothers Holdings Inc	S&P 500	-	-	10.0	-
TSAI	Transaction Sys Archtcts -Cl A	S&P 400	-	-	10.0	-
CSCO	Cisco Systems Inc	S&P 500	-	-	9.9	-
JDAS	JDA Software Group Inc	S&P 600	-	-	9.7	-
SEE	Sealed Air Corp	S&P 500	-	-	9.6	-
LRCX	Lam Research Corp	S&P 400	-	-	9.3	-

continued…

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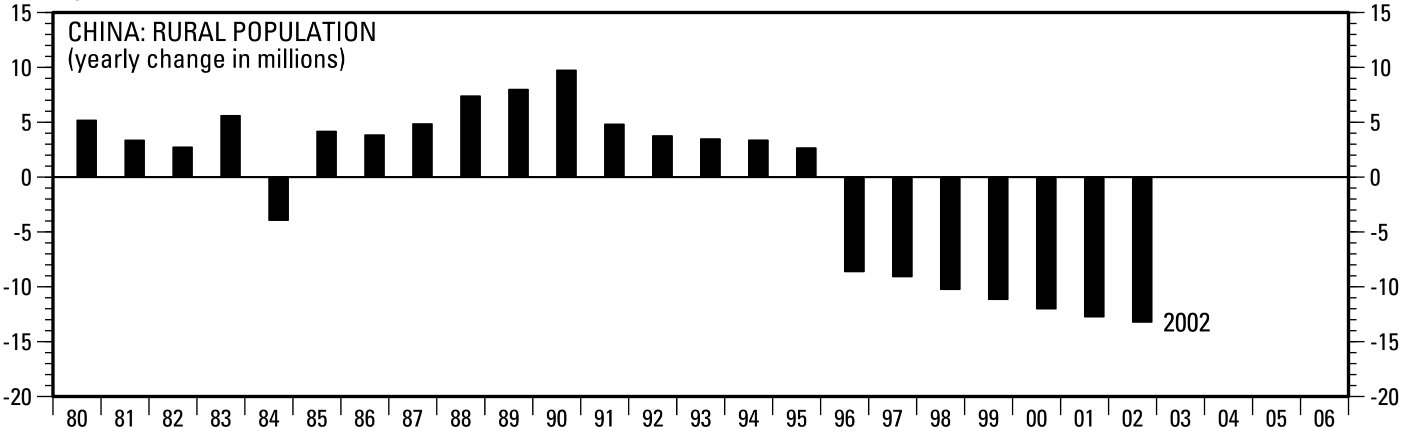
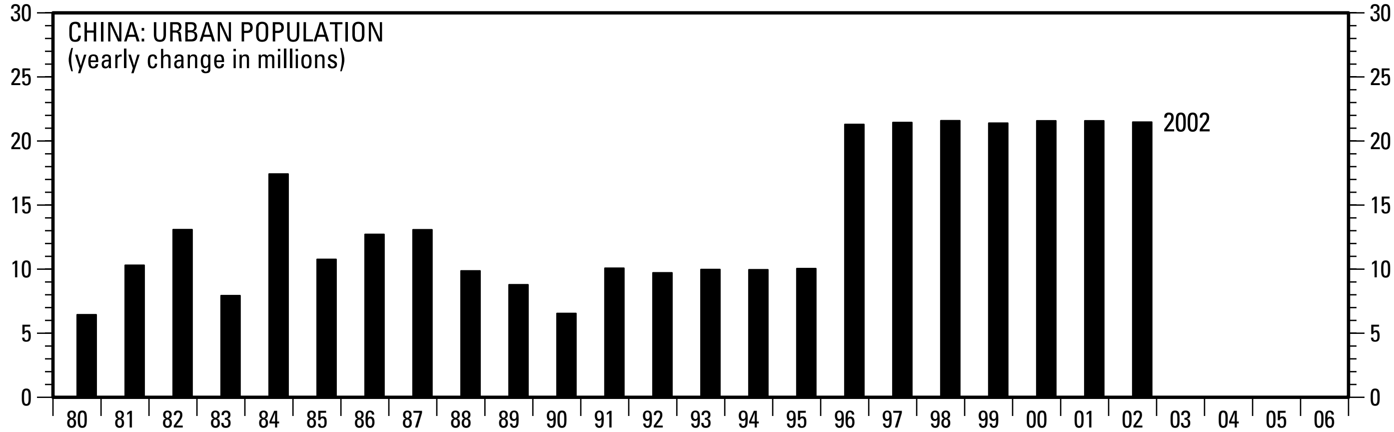
Symbol	Company	Index	China Only	China Mention	Asia Pacific Only	Asia Pacific Mention
MDT	Medtronic Inc	S&P 500	-	-	9.3	-
KFY	Korn Ferry International	S&P 400	-	-	9.3	-
CTXS	Citrix Systems Inc	S&P 500	-	-	9.2	-
ARW	Arrow Electronics Inc	S&P 400	-	-	8.9	-
CKP	Checkpoint Systems Inc	S&P 600	-	-	8.6	-
GTW	Gateway Inc	S&P 500	-	-	8.3	-
SXT	Sensient Technologies Corp	S&P 400	-	-	8.0	-
FUL	Fuller (H. B.) Co	S&P 600	-	-	7.9	-
SGP	Schering-Plough	S&P 500	-	-	7.7	-
TII	Thomas Industries Inc	S&P 600	-	-	7.7	-
ROK	Rockwell Automation	S&P 500	-	-	7.5	-
ACLS	Axcelis Technologies Inc	S&P 600	-	-	7.3	-
ITT	ITT Industries Inc	S&P 500	-	-	7.1	-
AXP	American Express	S&P 500	-	-	6.9	-
MROI	MRO Software Inc	S&P 600	-	-	6.8	-
MON	Monsanto Co	S&P 500	-	-	6.8	-
CSGS	CSG Systems Intl Inc	S&P 400	-	-	6.6	-
HSII	Heidrick & Struggles Intl	S&P 600	-	-	6.0	-
WDFC	WD-40 Co	S&P 600	-	-	5.9	-
SFN	Spherion Corp	S&P 600	-	-	5.8	-
SBL	Symbol Technologies	S&P 500	-	-	5.7	-
PRGS	Progress Software Corp	S&P 600	-	-	5.7	-
SEBL	Siebel Systems Inc	S&P 500	-	-	5.5	-
HYSL	Hyperion Solutions Corp	S&P 600	-	-	5.5	-
MIL	Millipore Corp	S&P 500	-	-	5.3	-
DIS	Disney (Walt) Co	S&P 500	-	-	5.2	-
FDS	Factset Research Systems Inc	S&P 600	-	-	4.6	-
METHA	Methode Electronics -Cl A	S&P 600	-	-	4.2	-
AG	Agco Corp	S&P 400	-	-	4.2	-
IVC	Invacare Corp	S&P 600	-	-	4.1	-
MERQ	Mercury Interactive Corp	S&P 500	-	-	3.7	-
IART	Integra Lifesciences Hldgs	S&P 600	-	-	3.7	-
ERTS	Electronic Arts Inc	S&P 500	-	-	3.6	-
FILE	Filenet Corp	S&P 600	-	-	3.2	-
CTV	Commscope Inc	S&P 400	-	-	3.0	-
DPH	Delphi Corp	S&P 500	-	-	2.8	-
C	Citigroup Inc	S&P 500	-	-	2.7	-
RSYS	Radisys Corp	S&P 600	-	-	2.6	-
SDS	Sungard Data Systems Inc	S&P 500	-	-	2.2	-
SGR	Shaw Group Inc	S&P 600	-	-	2.0	-
GD	General Dynamics Corp	S&P 500	-	-	1.1	-
INVN	Invision Technologies Inc	S&P 600	-	-	0.8	-
CL	Colgate-Palmolive Co	S&P 500	-	-	-	72.3
SLB	Schlumberger Ltd	S&P 500	-	-	-	70.2
BDX	Becton Dickinson & Co	S&P 500	-	-	-	46.1
AVO	Advanced Medical Optics Inc	S&P 600	-	-	-	40.5
CVX	Chevrontexaco Corp	S&P 500	-	-	-	29.6
AH	Armor Holdings Inc	S&P 600	-	-	-	19.2
KMB	Kimberly-Clark Corp	S&P 500	-	-	-	18.8
TECUA	Tecumseh Products Co -Cl A	S&P 400	-	-	-	16.1
FJC	Fedders Corp	S&P 600	-	-	-	13.9
CPO	Corn Products Intl Inc	S&P 600	-	-	-	13.4
UNM	Unumprovident Corp	S&P 500	-	-	-	11.7
JNJ	Johnson & Johnson	S&P 500	-	-	-	11.6
WMT	Wal-Mart Stores	S&P 500	-	-	-	8.9
K	Kellogg Co	S&P 500	-	-	-	8.2
AHC	Amerada Hess Corp	S&P 500	-	-	-	8.0
AXE	Anixter Intl Inc	S&P 600	-	-	-	7.1
ICN	ICN Pharmaceuticals Inc	S&P 400	-	-	-	7.0
BUD	Anheuser-Busch Cos Inc	S&P 500	-	-	-	5.9
AFG	American Finl Group Inc	S&P 400	-	-	-	1.0
EME	Emcor Group Inc	S&P 600	-	-	-	0.6

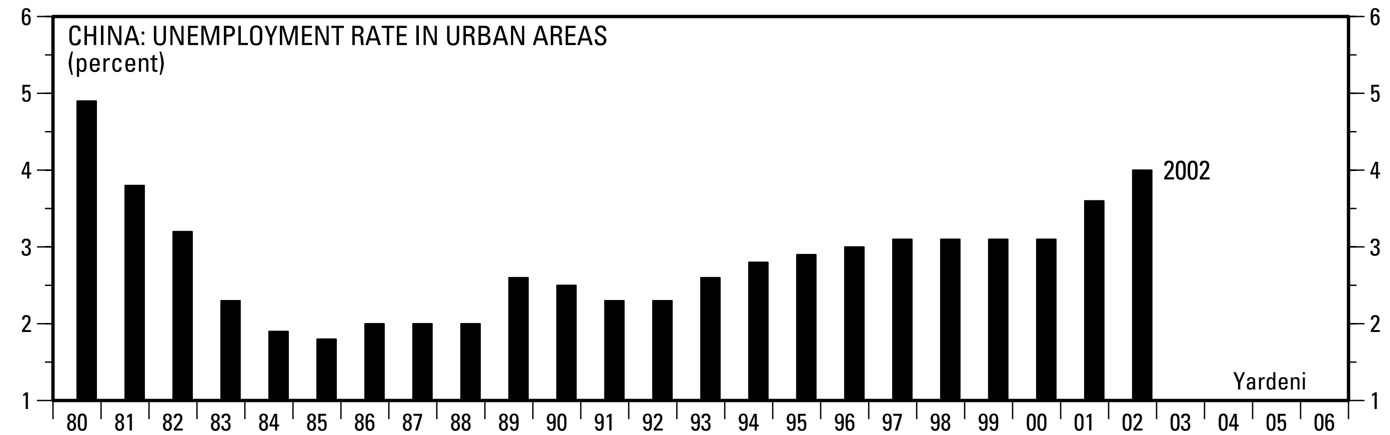
Source: Compustat, Latest Company 10K Filings, PEG Investment Strategy Research.

China: Population

Figure 1.





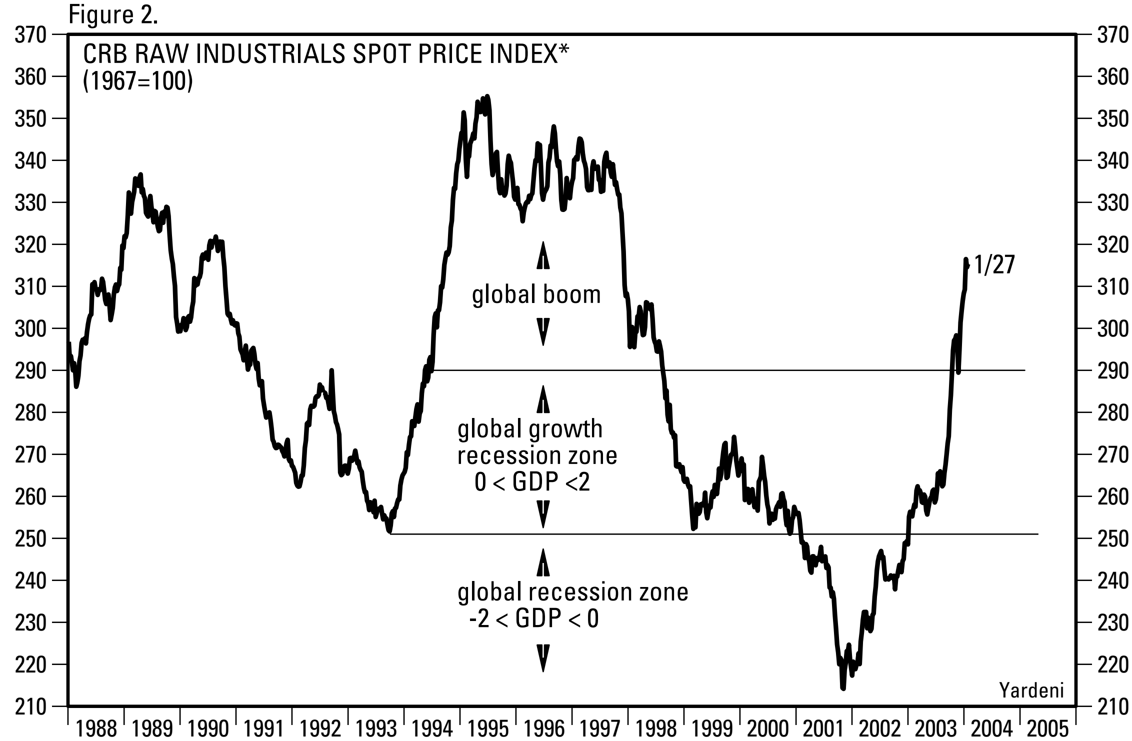


Source: State Statistical Bureau, People's Republic of China.

China-Led Global Boom

Industrial commodity prices are confirming a China-led Global Synchronized Boom.

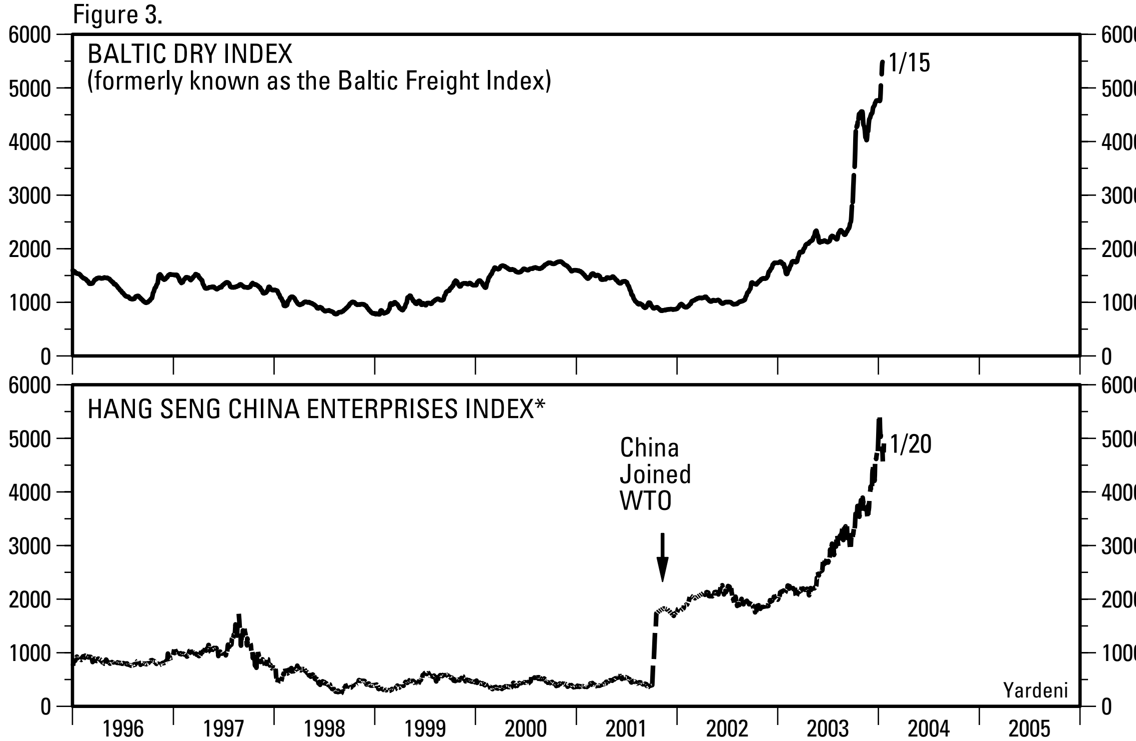
Figure 2.



* Includes copper scrap, lead scrap, steel scrap, tin, zinc, burlap, cotton, print cloth, wool tops, hides, rosin, rubber, and tallow.
Source: The Commodity Research Bureau.

China-led global boom is sending shipping rates straight up. Chinese stocks listed in Hong Kong have been soaring since China joined the World Trade Organization.

Figure 3.

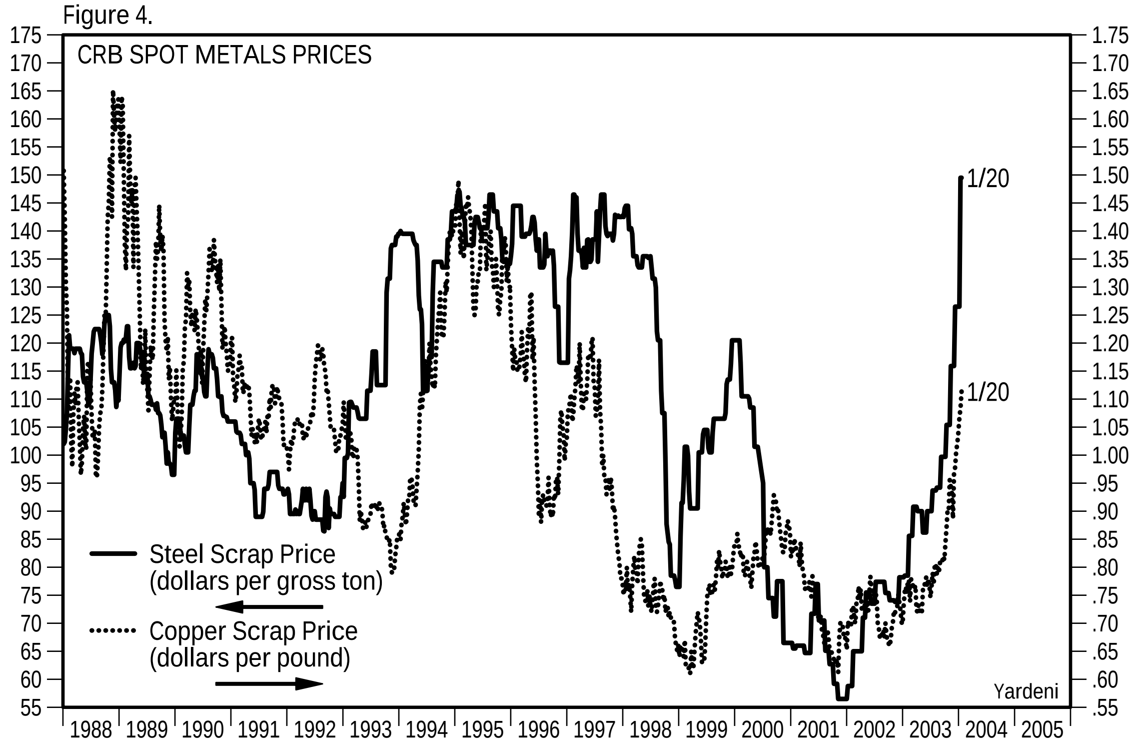


* Price index of 32 Chinese companies listed in Hong Kong.
Source: The Baltic Exchange and Hang Seng Exchange.

Steel

Steel scrap prices are in record territory.

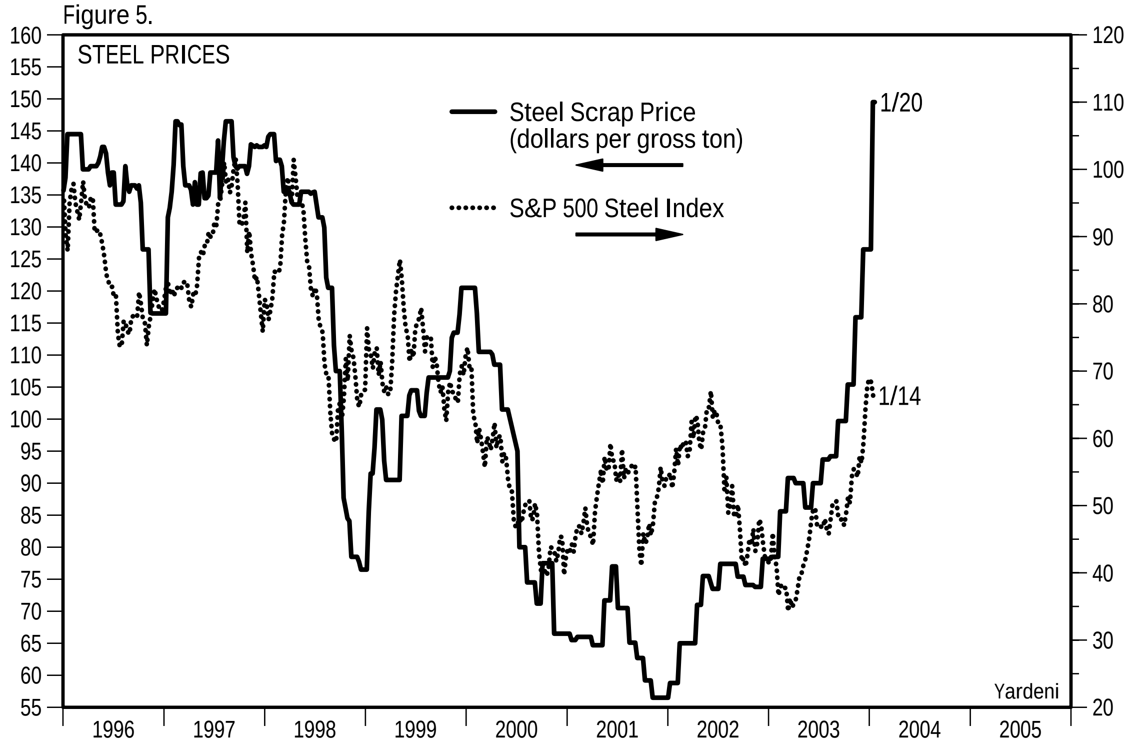
Figure 4.



Source: The Commodity Research Bureau and Investor's Business Daily.

The S&P 500 Steel Index is likely to head higher given the jump in steel prices.

Figure 5.

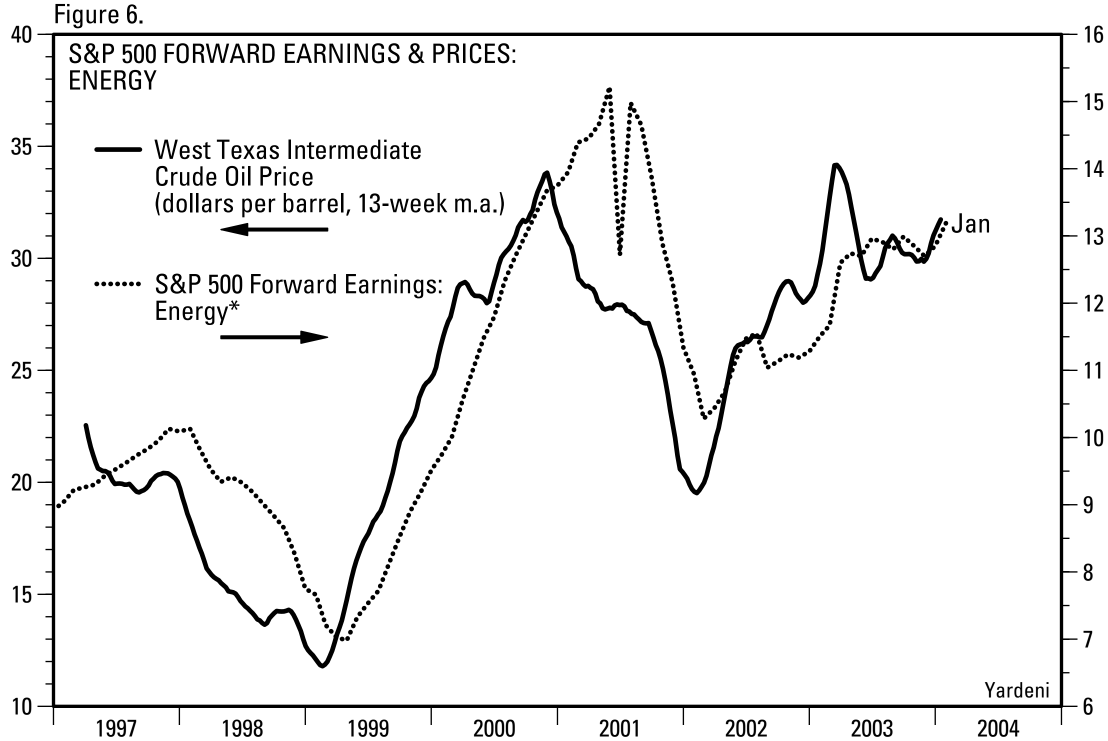


Source: Standard & Poor's Corporation, the Commodity Research Bureau and Investor's Business Daily.

Crude Oil

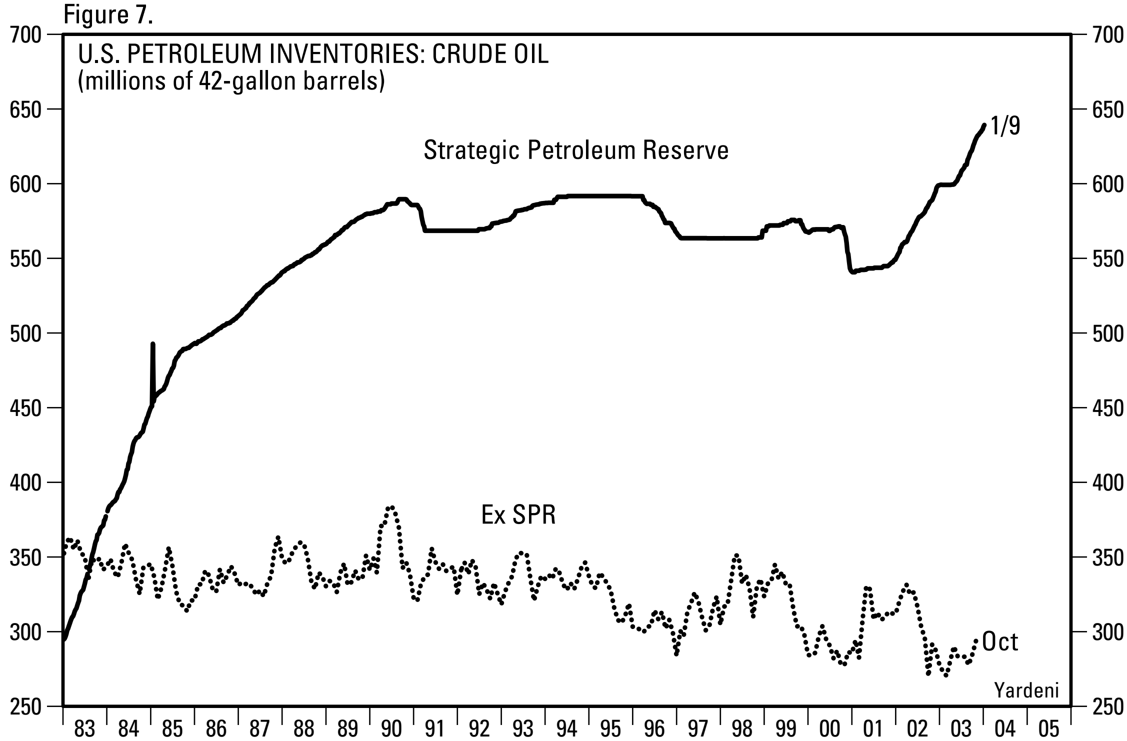
Crude oil prices have been boosted by the global boom, cold weather, and additions to the Strategic Petroleum Reserve (SPR).

Figure 6.



* 12-month forward consensus expected operating earnings per share.
Source: Platt's "Oilgram Price Report" and Thomson Financial.

Figure 7.

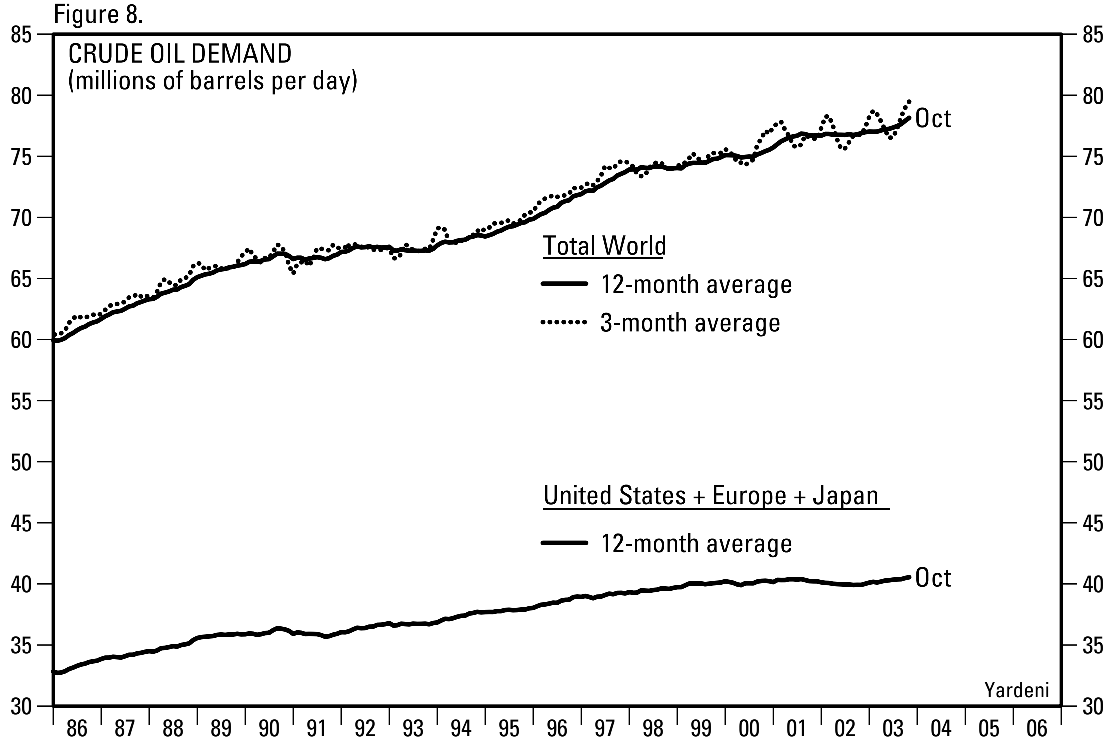


Source: U.S. Department of Energy, Energy Information Administration.

Crude Oil

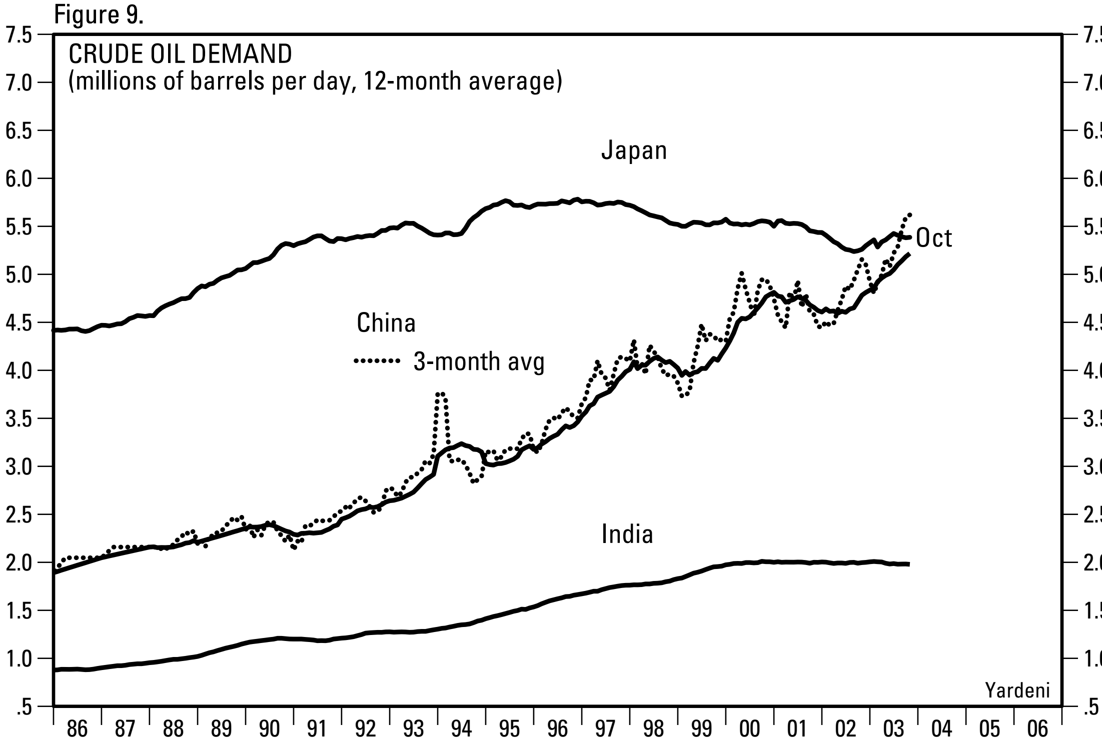
World crude oil demand is at a new high, led by soaring demand in China.

Figure 8.



Source: Oil Market Intelligence.

Figure 9.

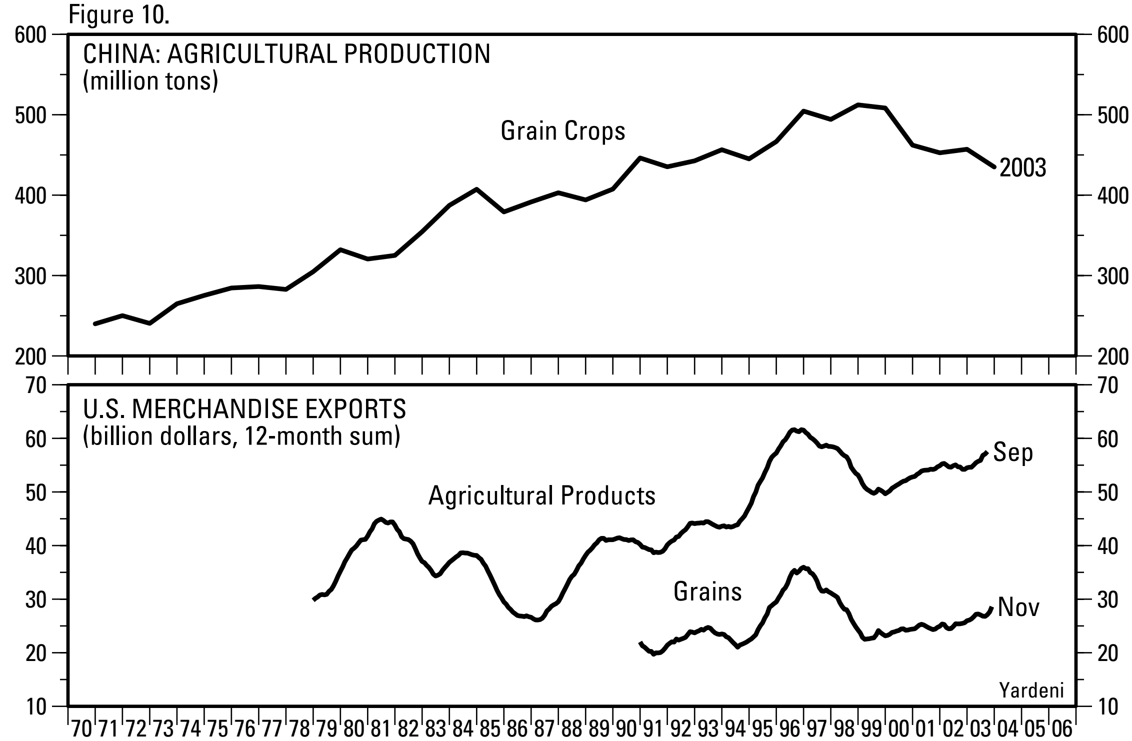


Source: Oil Market Intelligence.

Chinese Food

Chinese grain output has been disappointing recently. U.S. agricultural exports have been boosted by Chinese demand.

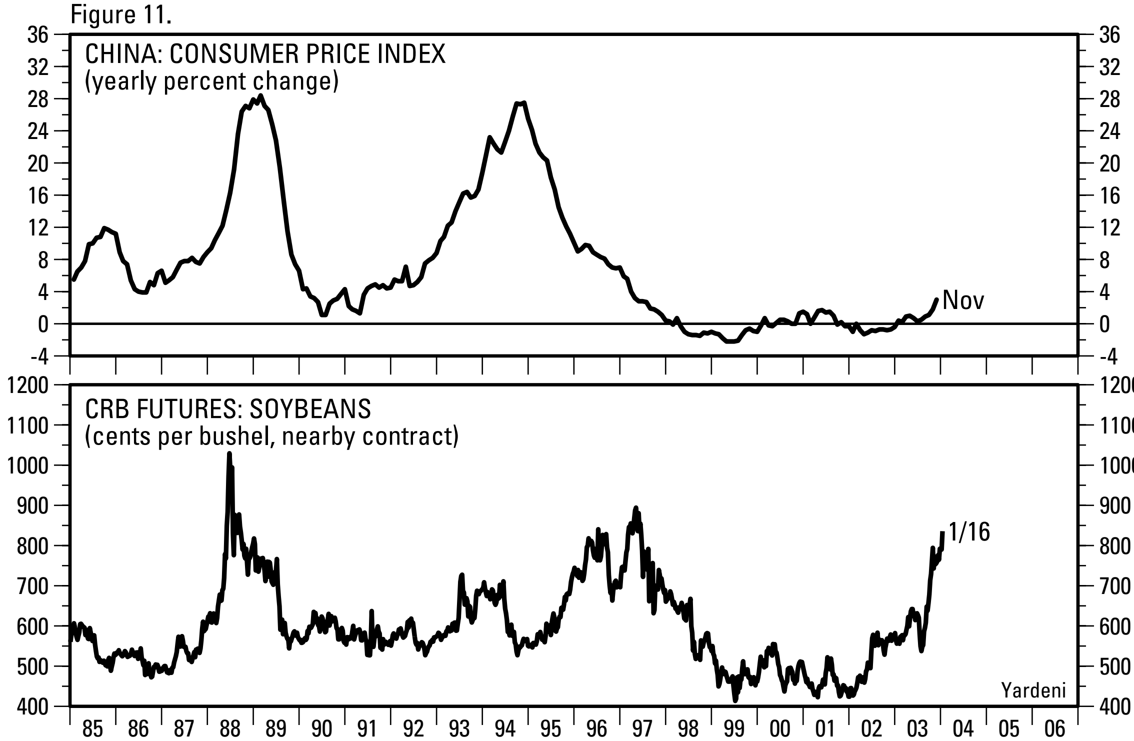
Figure 10.



Source: China National Bureau of Statistics and U.S. Department of Commerce, Bureau of Economic Analysis.

Rising food prices are the main reason that China's CPI inflation rate is back above zero. Chinese demand for grains could send "beans into the teens."

Figure 11.

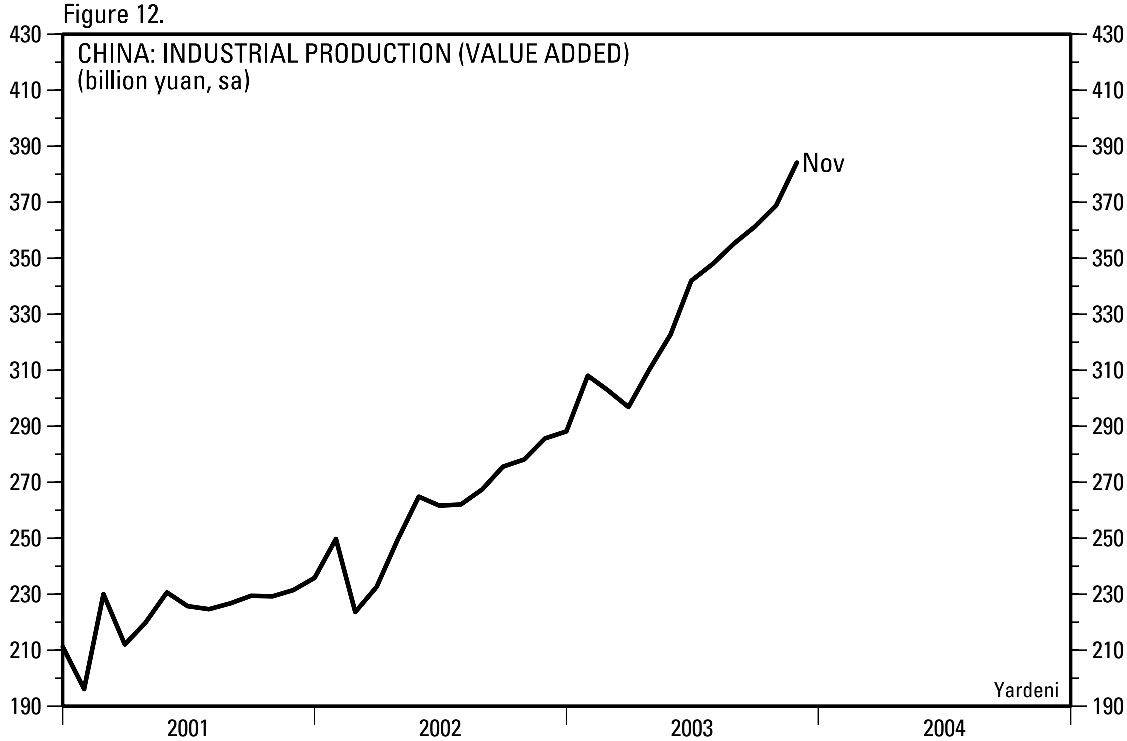


Source: China National Bureau of Statistics and the Wall Street Journal.

Chinese Economic Indictors

There's no sign of a slowdown in Chinese production.

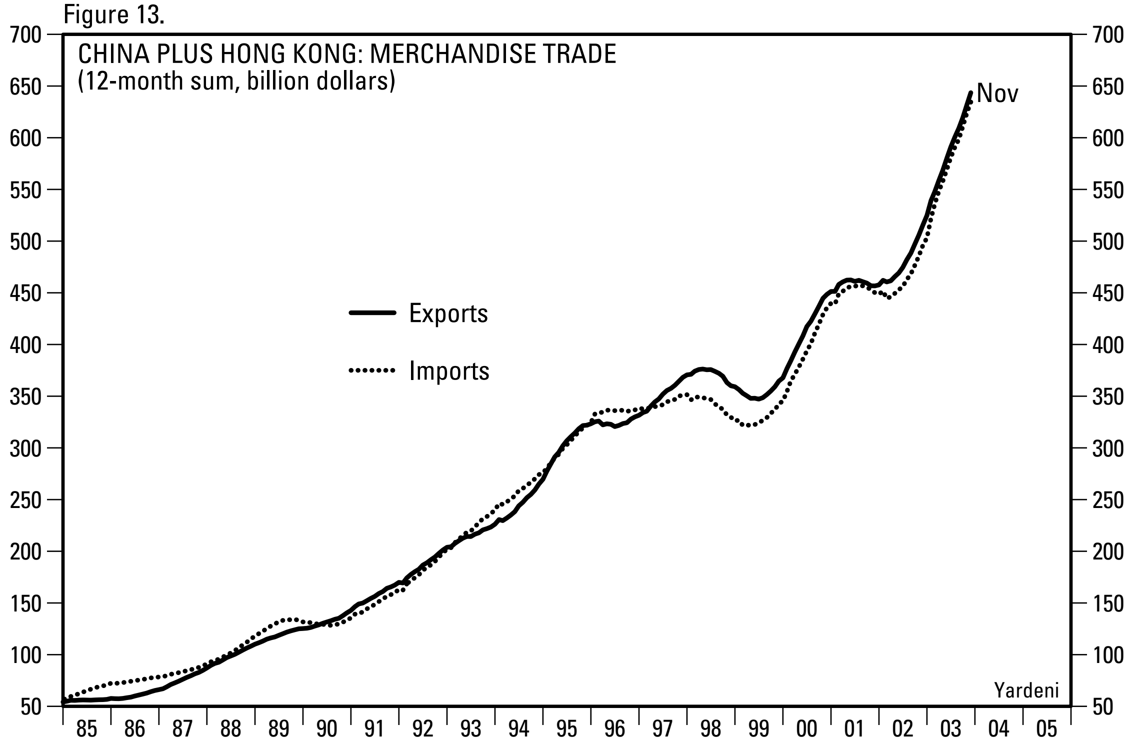
Figure 12.



Source: China National Bureau of Statistics/Haver Analytics.

Chinese exports and imports are soaring.

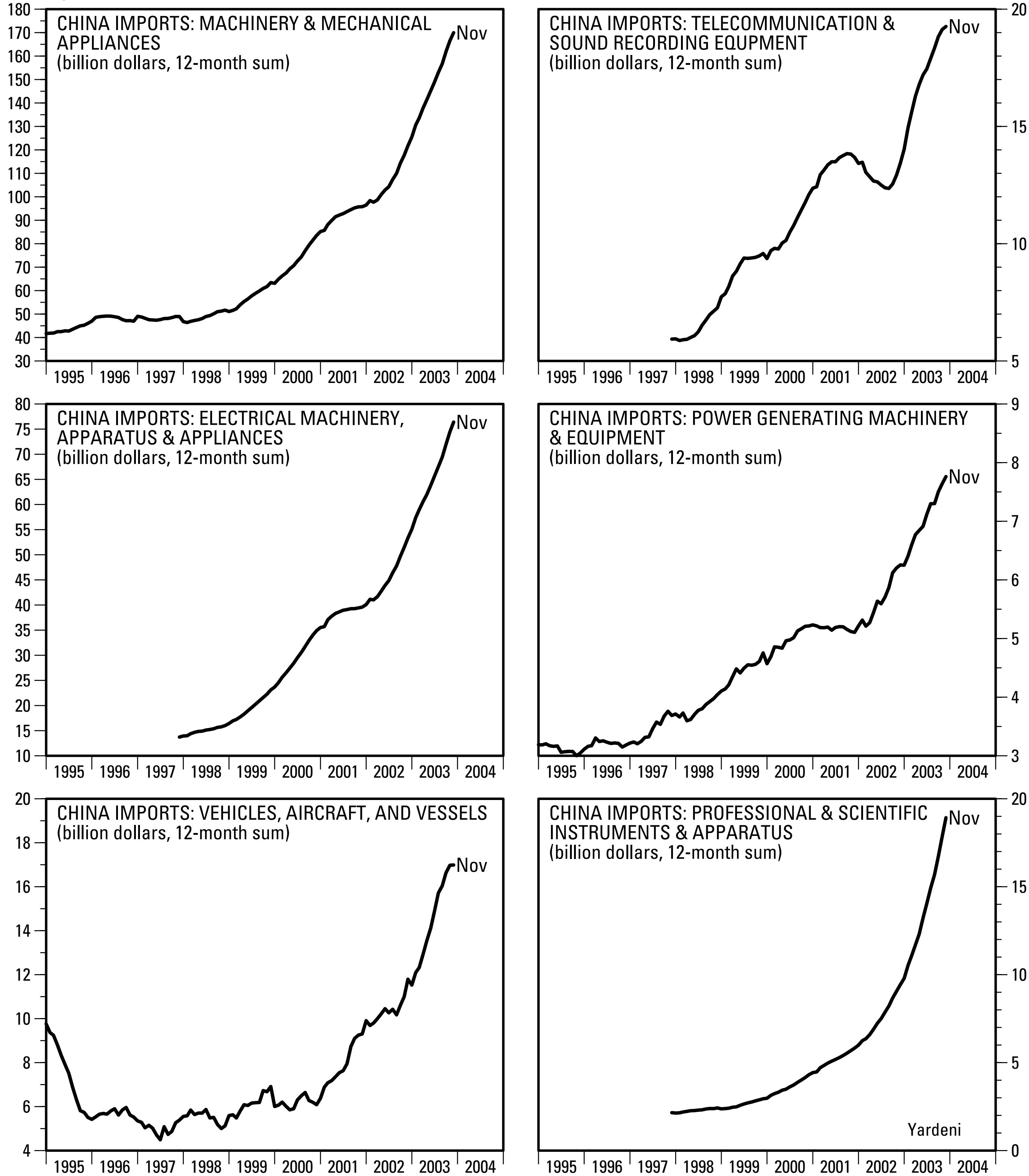
Figure 13.



Source: China Customs/Haver Analytics.

China: Imports

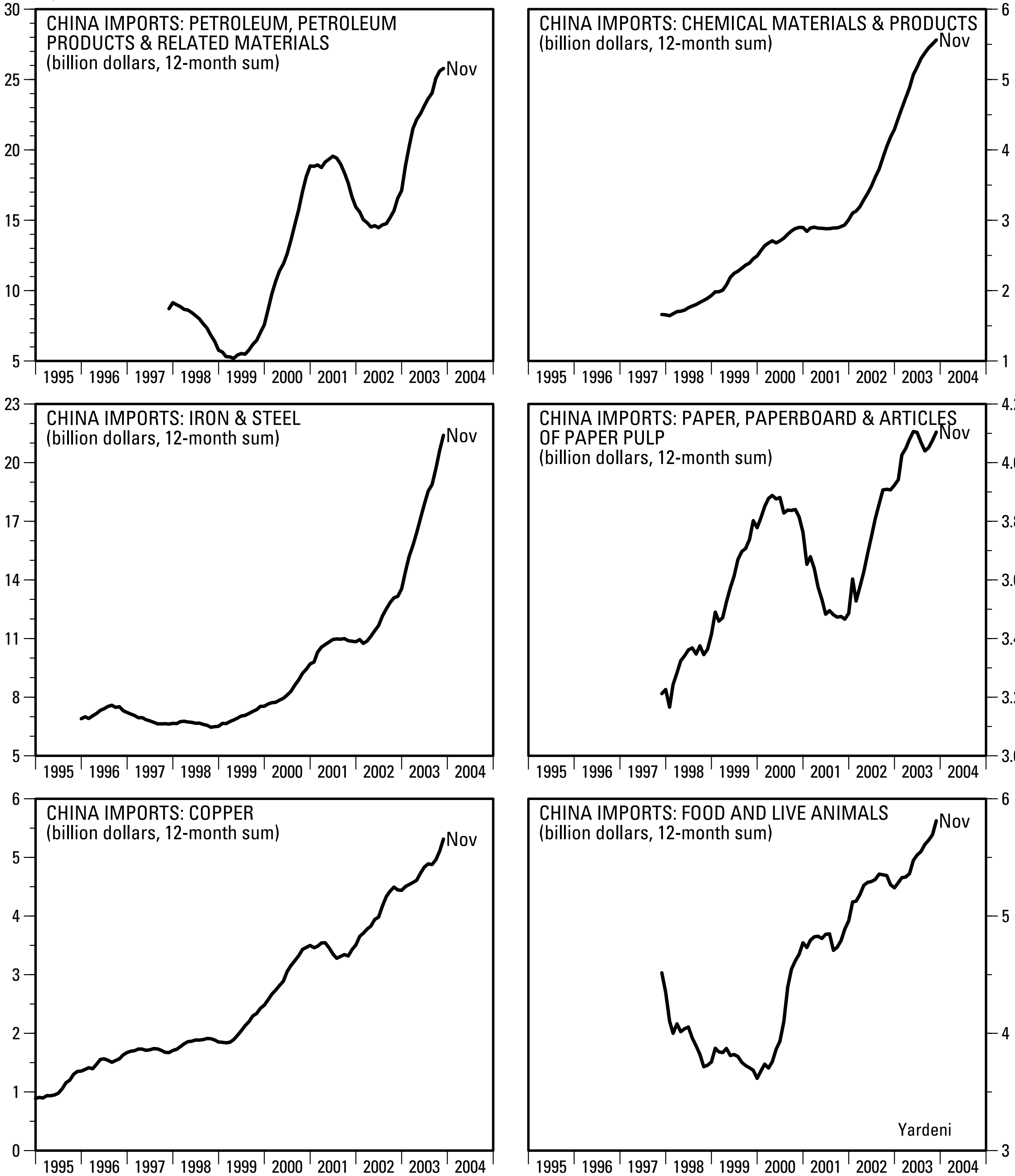
Figure 14.



Source: China Customs/Haver Analytics.

China: Imports

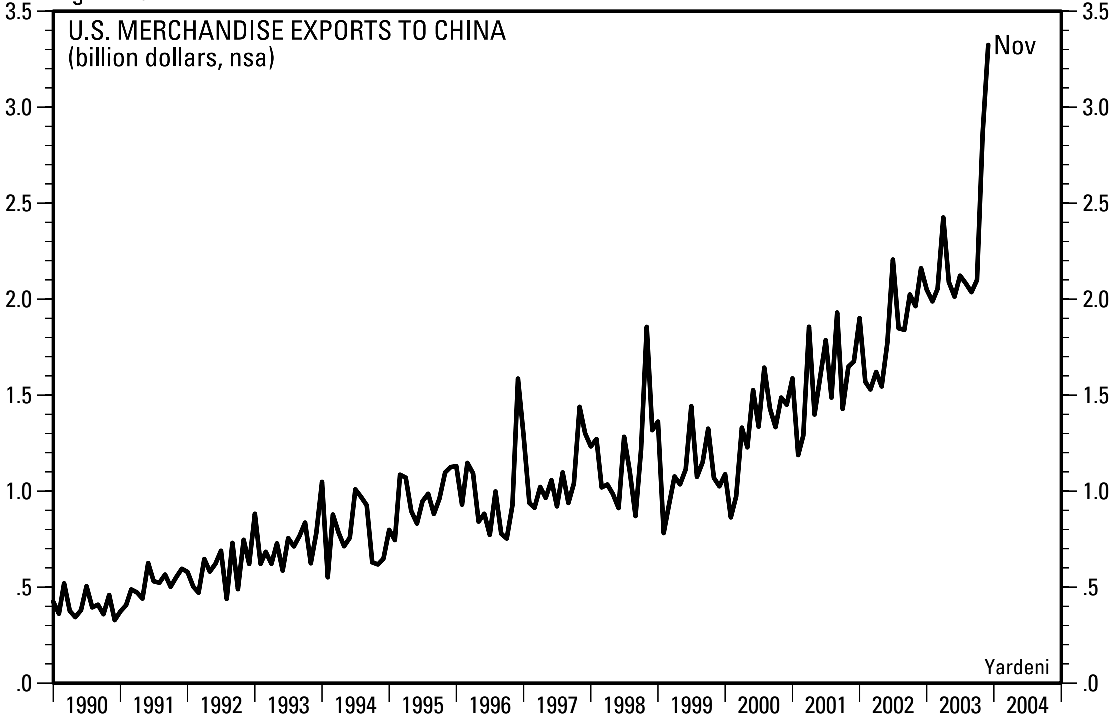
Figure 15.



Source: China Customs/Haver Analytics.

U.S. Exports to China

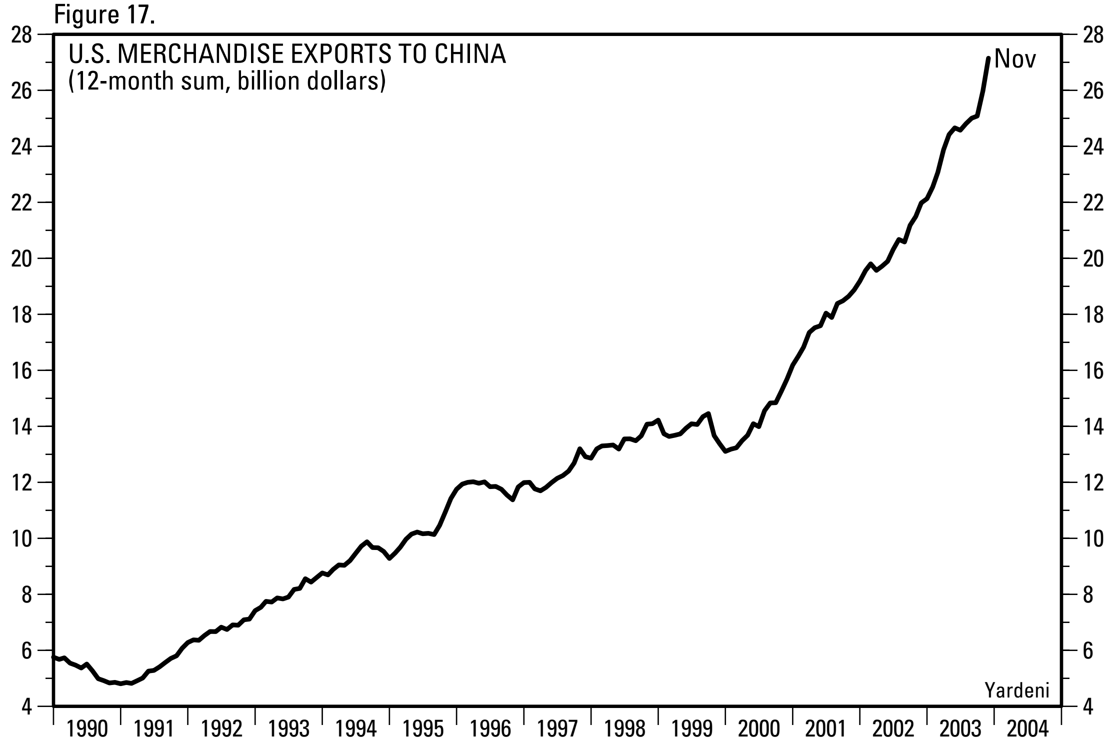
Figure 16.



Source: U.S. Bureau of the Census/Haver Analytics.

U.S. exports to China are taking off.

Figure 17.

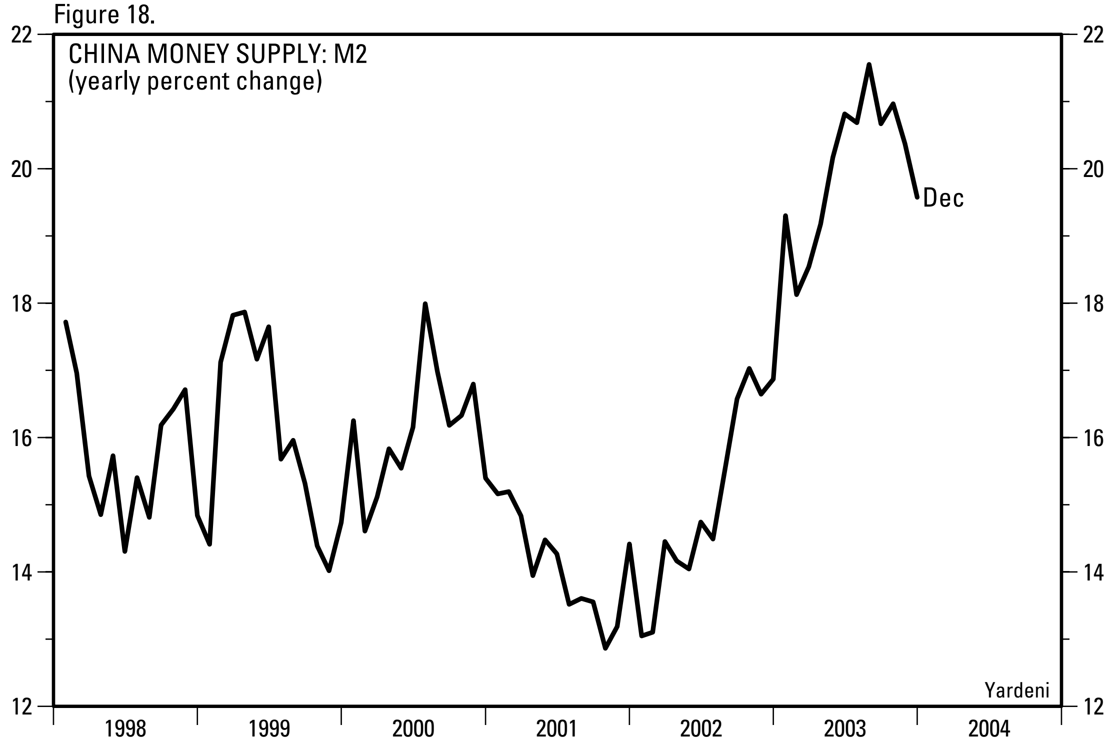


Source: U.S. Bureau of the Census/Haver Analytics.

China: Finance

China has seen rapid money supply growth.

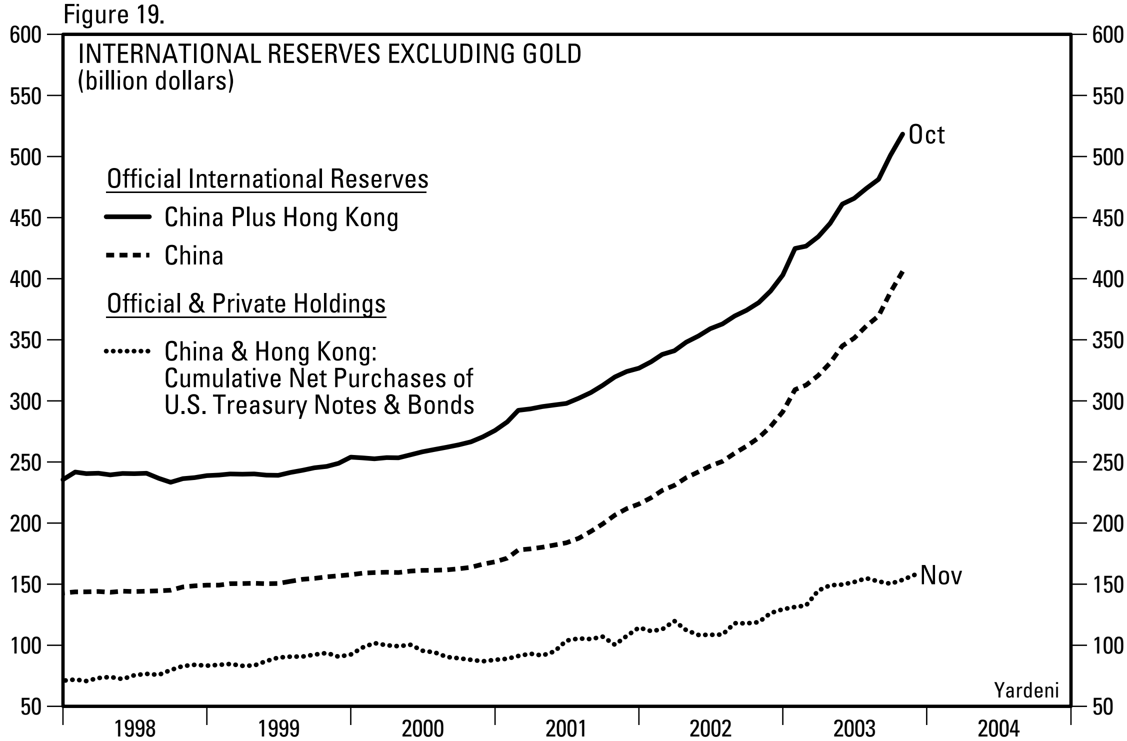
Figure 18.



Source: People's Bank of China.

China's international reserves have soared to a record $406 billion.

Figure 19.



Source: International Monetary Fund and U.S. Department of the Treasury, Office of International Affairs.

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Prudential Equity Group, Inc.
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