

**AFTER THE SNOW COMES THE THAW ...  
AND, THEN, THE TROUBLES !**

Assessing the extent of the damage, caused by the violent blizzards that lashed the People's Republic of China (PRC) since January 10, 2008, will determine, without question, the magnitude of the gyrations of the key indices of The Shanghai Stock Exchange, The Shenzhen Stock Exchange, The Stock Exchange of Hongkong Ltd ... and, then, those violent gyrations are quite likely to cascade down to other equity markets of most parts of the world.

The financial losses, during the Chinese New Year holidays, in terms of lost retail sales, disruptions in industrial production in the People's Republic of China (proper), as opposed to the Hongkong Special Administrative Region (HKSAR) of the PRC, the known, massive damage to crops and livestock, the estimates with regard to the cost of rebuilding and/or extensive repairs to roads, bridges, and airports, and rethinking improved infrastructure of all kinds will hug the headlines.

The estimated losses, which will trickle out of Beijing in dribs and drabs, are almost certain to frighten investors, right down to their knickers.

A retraction in corporate profits will, undoubtedly, be one of the legacies on the blizzards, which were the worst of the past 50 years or so.

The forecasted costs of the cleanup of the Middle Kingdom will take place in the next few months and, during that period of time, the key indices of the equity markets of the PRC and the HKSAR will rise and fall, probably violently, as suggestions and guesstimates make the rounds of trading floors.

The snowstorms of January were bad; the thaw in February, in terms of investor confidence and real losses on equity markets as well as in other investments, will be much worse.

In the final week of January, alone, insurance claims of more than 3.50 billion renminbi were filed, according to The China Insurance Regulatory Commission.

PRC-domiciled insurance companies are in for a hard time.

Their bottom lines for this financial year will be dented, considerably.

And this is just the beginning.

The PRC Government, no doubt, will institute new or revised policies, aimed at ameliorating the situation in the country, and with the intent to make certain that the country shall be well prepared for a repeat performance from Mr Snowman in coming years.

One salient factor must have been driven home to the PRC Government, during the middle of January: Without adequate communication and transportation from one part of the country to another, things come to a standstill.

And, in such a scenario, civil unrest is easy to be fermented by the estimated one billion, frustrated plebeians.

One may expect to learn of tens of billions of renminbi, being spent on upgrading the country's transportation network, increasing the number of new airports in order to accommodate the more-affluent, Chinese commuter, improve the flow of information from one corner of the country to another via the

Internet and other high-technology telecommunication facilities, both new and old, increase the level of mobile telecommunications, available to everybody, the etc, etc, etc.

The aggregate effect of the January blizzards will be to see a significant slowdown in the growth of the **Gross Domestic Product (GDP)** and the **Gross National Product (GNP)** of the fastest-growing, major economy of the world, today.

GDP = The annual total value of goods produced and services provided in a country, excluding transactions with other countries.  
GNP = The annual total value of goods, produced and services provided in a country.

The economic slowdown will, invariably, affect equity valuations, but, probably, this will become more evident in the second quarter of the year.

While the pace of economic growth in the PRC will slow, appreciably, in 2008, relative to the pace of growth in 2007, it will, still, be growth, nevertheless.

And the growth in the economy of the PRC will, still, be the envy of most industrialised countries of the world – because it will be growth, not a retraction from growth.

Psychology determines the direction of the key indices of all equity markets, more so than fundamentals – sadly.

As such, as the PRC Government digs deeply into its brain bank in order to find solutions to the new challenges of today, so it could well unnerve the more unsophisticated investors of the country, most of whom will fret as to how severely the country's many problems will affect them where it hurts most: In their pockets.

Substantial selling spurts on The Shanghai Stock Exchange and The Shenzhen Stock Exchange will frighten investors in the HKSAR and, in the US and Europe, the selling sprees of the PRC's equity markets could well be the talk of boardrooms, from one country to another.

Tens of billions of renminbi will be wiped off the market capitalisations of many, if not most, of the 'darlings' of the equity markets of the PRC, proper; and investors of the HKSAR, seeing what is happening to the A Shares (those shares that are listed in the PRC, proper, being distinct to those shares, quoted in the equity markets of HKSAR) will seek to sell off part or all of their holdings in the H Shares (those shares, representing part of the equity of PRC-domiciled companies, whose shares are quoted on The Stock Exchange of Hongkong Ltd).

The total effect is likely to be to drive price-earnings multiples down to more realistic levels than in the past, but, in the process, many investors, in both the HKSAR and the PRC, proper, will suffer substantial financial losses.

This seems inevitable.

Corporate earnings of PRC-listed companies will fall, to be sure, and this will come to be known, more fully, probably by the third quarter of this year.

The main reason for this state of affairs is that, during the 2007 Fiscal Year, corporate earnings were boosted, to some extent, at least, by one-off gains, brought about by stock-market operations and successful **Initial Public Offerings (IPOs)**.

With regard to many of the IPOs, pitched during a large part of calendar 2007, their share prices were Offered at prospective price-earnings multiples, in some cases, as high as 68 times.

Which made little sense – and **TARGET** () was not loath to state as much on frequent occasions.

In an atmosphere where one-off profits are not readily available on equity markets, which is almost certain to be the case from hereon, corporate profitability must wane.

**And Meanwhile ...**

While the PRC, proper, deals with its domestic problems, in the US, the economy is quite likely to continue to weaken.

One may expect, soon, to witness the first quarter of negative growth.

Investment psychology will play a role, here, too, and the '*rabbits*' of the many equity markets of the US will try to burrow into their respective warrens.

On Wall Street, the key indices of The New York Stock Exchange and The NASDAQ could well fall, substantially, with each successive shock announcement.

The knock-on effect will be felt, round the world, for certain.

However, in the PRC, proper, while many investors might well be frightened and toilet paper might be in short supply, from time to time, the country's economy, actually, is somewhat insulated from many of the problems with regard to the US economy.

The domestic economy of the PRC is strong; it is getting stronger, month after month.

By the second quarter of this year, January's blizzards will be relegated to a chapter of history; and, it will be back to business as usual.

The blizzards were a nuisance, but they were not a long-term disaster: A short-term, economic hiccup, if you will.

However, having said that, PRC exporters, especially in the garment and textile trade, could find things a little more difficult, this year.

As US consumers tighten their purse-strings, there will be a definite reluctance by the majority of them, even to visit the High Street.

US inventory levels will rise and new-order cancellations will be rife in the PRC, proper.

**TARGET** is not, completely, convinced that the PRC is completely immune to the vagaries of the economy of the US because it stands to reason that there must be some fall-out from the problems, confronting the largest economy of the world.

Certainly, the effect of homeowners' negative equity in the US housing market is going to be felt for months to come and **TARGET** does not believe that the US President's \$US150-billion-plus, tax-relief package will be the balm to cure the problems, confronting a large proportion of 300 million citizens of the US.

As unemployment rises in the largest and most-important, single economy of the world, it must have a detrimental effect on Mr and Mrs America.

The PRC will not be completely immune from the problems, confronting US economy of today.

Probably, starting in April, things will become clearer in the PRC, proper, in respect of its overall economy.

In a nutshell, what one is likely to view as the year winds on is slower production levels, leading to lower corporate growth.

Inflation will rear its ugly head, again, and the PRC Government will take remedial action to contain it.

Price controls will, surely, follow.

Valuations of 2007 will be looked at comically as they come off, dramatically, in the second half of the year.

Equity prices will wilt, for a while, at least.

Like the blizzards of the PRC, proper, however, after the storms always comes the thaw.

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