GOLD & ENERGY ZEALOT

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"Silver swings wildly after setting 16-year high!

"The wild price swings in silver show just how easily a small increase in demand can send the price dramatically higher.

"Silver is heading to $25 an ounce. Use this dip to load up on silver."

James DiGeorgia, Editor

- **3 reasons silver will skyrocket over the next 3–5 years**
- **Is the market manipulated? My surprising answer!**
- **How you can profit in the new bull market!**

It's started!

For over a decade, silver has been grossly undervalued. Despite its wildly bullish fundamentals, silver was handcuffed and restrained from showing its true strength.

For years, I've been watching silver...waiting for it to burst free of its manacles. Over the last few months, it's finally started—silver is breaking free! At its recent peak, silver had more than doubled its price in the last 28 months, exploding up 35% just in 2004.

Now it's growling and thrashing around like a wildcat. We'll see some wild gyrations in the months ahead, but the overall trend is up. I believe we're on our way to $25 silver, and beyond!

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Bullish Fundamentals: 3 fuses on the powder keg

For a long time, silver was like a barrel of gunpowder, with 3 different fuses leading into it. It sat there quietly, but the peacefulness was deceptive: light any of the 3 fuses, and off it would go.

THE GOLD AND ENERGY ZEALOT

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Now, all three have been lit, making this a great time to be a silver investor...

Lit Fuse #1: 14 years of supply deficits

Since 1990, silver has been in a supply deficit—each year, more silver is consumed than is produced. As a result, above-ground inventories of silver are being used up. The deficit varies each year—the highest amount recently was 221 million ounces in 1997.

Most people don't realize how vital silver is to modern society. Silver is used in photography, jewelry, silverware...electronics, electroplating, and solar energy...batteries, biocides, and ball bearings... and much more. Silver's malleability, ductility, and reflectivity make it tremendously useful in a wide range of industries.

As a result, about 800 million ounces of silver are consumed each year on average. And a key word here is "consumed": although some silver gets recycled each year, much of it doesn't. For that matter, a lot of it *can't* be: in many industrial uses, only a few grams of silver are used here and there, and it's not worth extracting it back out afterwards.

Even with the recycled metal added back to silver mining output, annual production of silver is far less than the demand. So the net drawdown continues: millions of ounces disappear every year.

Despite this, some analysts are bearish on silver. They usually point out that the increasing popularity of digital cameras means less of a demand for film, thus there'll be less demand for the silver halides that are used in the film. They're correct, but the point is irrelevant. Even though digital cameras are now ubiquitous, and demand for film has decreased somewhat, film manufacturers are still consuming hundreds of millions of ounces each year.

Plus, as film manufacturing decreases, the scrap supply of silver also decreases, as there's less film to recycle. Thus, although some demand has been lost, some supply was lost with it.

In any case, film is only one of the many uses for silver, and accounts for only a fraction of the demand. So the net deficits continue.

Some silver bears have also asked: if silver has been such a great investment this whole time, why hasn't a large investor stepped forward and bought a bunch? Well, that's exactly what happened a few years ago when Warren Buffett bought almost 130 million ounces. As the wealthiest, most successful investor in the world, his actions are a triumphant endorsement of the bullish case for silver.

So if there's been a 14-year deficit, why didn't the price of silver skyrocket years ago? Two reasons: first, some believe that the price of silver has been manipulated (more on this later).

Second, silver didn't go up because there was a huge above-ground supply to meet the demand. But this supply is almost gone now, leading to...

Lit fuse #2: Thin supplies of above-ground silver

The cumulative 14-year deficit is well over 1.5 billion ounces of silver. That's more than 1,500,000,000 ounces of silver, used up and gone.

Worldwide silver inventories were about 2.2 billion ounces in 1990: last year they were down to less than 500 million. It may seem like there's a lot remaining, but this is less than one year's consumption. We're running out of silver!

Even the big government stockpiles are gone. After World War II, the U.S. had 4 billion ounces of silver. By 1959, it was down to 2.06 billion ounces. Now it's gone—consumed. The only government left with any significant silver is India (they have 87 million ounces or so—maybe 6 weeks' worth of worldwide demand).

So will the silver mines ramp up production to replace it? Not until the price goes much higher—the mining companies have been mangled with the decade-long undervaluation of their product, and they've shut down all but their cheapest operations. Silver needs to go up a lot more before they can afford to bring substantial new capacity on-line (and even then, that's a multi-year process).

There aren't that many mines anyway: you can count all of the primary silver mining companies on the fingers of 2 hands. All together, they're only responsible for about a quarter of annual silver production.

The rest comes from "secondary" mines: those that produce silver as a byproduct while they mine for something else (zinc, copper, lead, etc.) This factor is also bullish for silver, since even if silver skyrockets (which I believe is inevitable), these mines won't necessarily increase their production. Silver produces only a fraction of their revenues, and their operations are driven by other factors. So an increase in silver's price won't necessarily translate to a large increase in mining production.

Another bullish factor is the inelasticity of the demand for silver. Many industrial processes use silver in only small amounts: even if silver's price explodes, this won't discourage its use. For example, silver is used in many components of a car—but a higher silver price might only add a few dollars to the cost of a $30,000 vehicle. Not a big deal, and I can't see this reducing the demand for silver in auto manufacturing.

By now, you might be wondering: how can all this be true? Surely, if the case for silver was so bullish, others would have noticed by now? Well, they have! That's...

Lit fuse #3: Investor Demand

Silver has been a quiet, unpopular investment for 20 years. I believe that's about to change.

Even with silver in the doldrums, and mostly ignored, investors still bought 8.7 million one-ounce Silver Eagles last year. This is in addition to all the silver rounds, bars, coins, certificates, and other forms of silver investments that were purchased.

Because of silver's huge jump over the last few months, many more investors are starting to pay attention. And rightly so. How much more will investor demand increase, as people start to jump on the bandwagon?

Plus, the continual debasement of the dollar is yet another bullish factor for silver. Much of the price dip this week was because of a spike in the dollar, especially compared to the euro. This proves my point—the price of silver is very sensitive to fluctuations in the dollar, both up and down.

But long term, the dollar is going down—way down. In last month's issue, I told you about 5 economic forces that will cripple the dollar. The U.S. currency is in real trouble, and I believe it's about to get much worse. As the dollar plummets, investors have always fled to precious metals… gold and silver.

And silver has a unique advantage here. With gold well over $400 an ounce, many small investors can't afford much of it. Not so with silver: even though it recently set a 16-year high, silver

Latest prices as GEZ goes to press— April 14, 2004

Comex spot contract: silver $7.00, gold $399.70
Nymex spot platinum: $925.00, palladium $309.00
Nymex Light Sweet Crude Oil $38.00

Silver coins			Dealer will buy at this price	Dealer will sell at this price
100 1 oz. silver American Eagles			$840	$895
100 1 oz. common rounds			$712	$795
$1,000 face value US pre-1965 coin bag (circulated)			$4,895	$5,300
$1,000 face value US circulated silver dollar bag (VG or better)			$6,900	$7,900
US Morgan silver dollars		PCGS MS64	$50	$65
		PCGS MS65	$110	$135
		PCGS MS66	$260	$310
Platinum coins				
U.S. Platinum Eagle:		1 oz.	$925	$995
		1/2 oz.	$470	$550
		1/4 oz.	$240	$325
		1/10 oz.	$105	$138
Gold coins				
Australian Kangaroo			$397	$415
British sovereign (Kings)			$92	$98
(Elizabeths)			$92	$98
Canadian Maple Leaf			$404	$415
Credit Suisse 1 oz. gold bar			$400	$412
Mexican 50 peso Centenario			$471	$496
South African Krugerrand			$404	$415
US Gold Eagle:		1 oz.	$408	$416
		1/2 oz.	$200	$219
		1/4 oz.	$101	$112
		1/10 oz.	$41	$49
US $20 double eagle:				
Liberty	Raw	MS60	$464	$510
	NGC	MS63	$650	$740
	NGC	MS64	$1,275	$1,450
	NGC	MS65	$4,250	$5,550
Saint Gaudens	Raw	MS60	$456	$500
	NGC	MS63	$530	$600
	NGC	MS64	$700	$795
	NGC	MS65	$1,100	$1,250

Prices courtesy of Finest Known, Boca Raton, FL. (800) 806-3468.

is still very affordable. You get a lot of metal for your money, and this is very appealing to a large number of smaller investors.

Plus, many investors that can't imagine investing in gold can picture themselves owning silver. To many, gold seems like a rich person's investment: but silver is much more accessible. This will greatly increase silver's investment demand.

Even with only a slight surge in investor interest, there are already signs that the silver market is starting to crack. I've already explained how there's very little silver left to meet demand, and recently there have been some disturbances in the markets. Apparently a number of wealthy investors contacted the CPM Group (a precious-metals consulting firm), interested in buying $100,000 to $5,000,000 in silver. These clients had a hard time getting a large quantity of silver at a reasonable price.

Plus, there are rumors swirling about Central Fund of Canada (ticker symbol CEF). CEF is a closed-end fund that buys gold and silver. Last year, CEF bought several million ounces of silver, and rumor has it that they still haven't been able to get delivery on the last 1–1.5 million ounces. Plus, a couple of weeks ago they announced that they were arranging to buy even more. Will this purchase be the one that cracks the market open?

So you see that, even at the beginning of the new bull market, the silver market is looking very fragile. What will happen when the general public starts to stampede into the market? How high will the price go? I can hardly wait to find out!

So that's why I'm waiting breathlessly for silver to explode. I think the recent price moves are just the beginning. But there's one big question about silver that I haven't answered yet...

Is silver being manipulated?

Maybe you've seen articles on the Internet written by certain analysts, claiming that silver is being manipulated to keep the price down. These analysts say that the price of silver has been ruthlessly suppressed, by traders playing games with the price on the COMEX futures exchange. Since the price of physical silver is derived from the price of futures, manipulating the price on the exchange translates to controlling the price of the metal itself.

Are these analysts right? Here's my take on this issue—starting with a brief review of how a healthy, non-manipulated futures exchange should work.

200 years ago, before there were futures markets, buying and selling commodities was very risky. During harvest time, farmers had to race each other to get their crops to market first: since the entire harvest showed up at the market at the same time, the farmers who got there last often found that there were no more buyers for their crops. Chicago was a large agricultural market, and its streets would sometimes be littered with rotting produce...as tardy farmers dumped their now-worthless crop on the ground rather than transporting it home.

This situation wasn't ideal for the buyers, either. They had to forecast their entire year's consumption, and buy it all at harvest time. An inaccurate prediction left them with either too much or too little for their needs.

Farmers and buyers could both reduce their risks if they struck agreements ahead of time. This assured the farmers of better and more stable prices, and allowed the buyers to buy what they needed over time, rather than all at once. However, these agreements varied from person to person, and were difficult to create (and enforce). So, in 1848 the Chicago Board of Trade was founded—the first futures market in the United States. Now producers and buyers could enter into "futures contracts": standardized agreements for a producer to deliver a commodity for a certain price, at a specified future date.

Centralized futures exchanges smoothed out the bumps between buyers and sellers, but there were still wild swings in price volatility—and liquidity could be a problem as well.

Today, modern exchanges also allow speculators: traders who have no interest in either buying or selling the actual commodity, but instead just trade the contracts. Speculators don't care about the commodity itself—they just bet that the price of the contract will move in a certain direction. Speculators "lubricate" the markets, by providing liquidity and assuming a lot of the risk in price movements. In return, they can profit substantially.

Now, almost all of the trading that occurs in futures exchanges is done by speculators—of all the contracts that are bought and sold, only a small percentage of them actually end in the delivery of the physical commodity. The rest of the contracts are settled in cash, marked to the price of the commodity at the time of settlement.

Since speculation is allowed, contracts can be created at will without any relation to a physical commodity. For example, you can buy a contract for 5,000 bushels of corn even if you don't *want* any corn. You can sell the contract later to someone else who does. In the meanwhile, you're hoping that the value of the contract rises, so you can make a profit.

That seems clear enough, but many people have trouble understanding speculative selling. How can you *sell* such a contract if you don't have the corn? How can you create corn out of thin air?

The answer is—you don't. You aren't creating corn, you're creating a *contract* for corn. The mere act of selling creates a contract that didn't exist before. Then, sometime later, you'd buy an identical contract from someone else. Since the contracts are standardized, for the same amount of the same commodity, you have now sold and bought the same thing. Your net position, and obligation, is therefore zero. If the corn went down during the time that you held the contract, then you received more money than you paid—therefore, you profited. If the opposite is true, then you lost money instead. Either way, you have no obligation to provide actual corn.

So, as I said before, almost all contracts are settled in cash. Traders who think the price of the commodity will go up, "go long" and buy contracts: those who anticipate a downturn "go short" and sell contracts. Later, regardless of the actual movement of the price, both traders will need to exit, and either buy back or sell their positions.

This presents some opportunities for mischief. Imagine you're the CEO of Kellogg's, and you've come up with a great plan for selling more corn flakes. If you can get the corn much cheaper, you'll lower your costs, and can sell your cereal for less. Let's say you were planning on buying 10,000 contracts of corn this month—why don't you just sell 80,000 contracts all at once, thus tanking the price of corn...buy the 10,000 contracts you need once the market has bottomed...and then slowly close out your short position over time? If you do it carefully, you'll torpedo the market with your initial blast of contracts…and the market psychology will stay down in the dumps long enough for you to close out your positions at a low price.

Sound like a good plan? It might be, except that you're not the only big player in the market. What do you think will happen once other corn-flake makers like Post and General Mills—not to mention canned-vegetable suppliers like Del Monte and others—figure out what you're doing? They'd be likely to buy all those contracts you're selling, maybe even do a little market-rigging of their own to the upside...blowing your short positions out of the water, and causing you to *lose* money on the whole play.

So this is what a healthy market looks like. Lots of small speculators, mixed in with some larger players—but since everybody is competing against each other, no shenanigans can take place.

But what would happen if all of the big players colluded together? What if they all agreed (secretly) to sell huge numbers of contracts, to keep the price low...so that the small numbers that they wanted to buy (and take delivery on) were dirt-cheap? Since contracts can be created out of thin air, market-riggers could easily bury the market in paper, squashing any price move that goes against them.

That's what some analysts say has been happening in silver...

What's going on at COMEX?

COMEX is the primary futures exchange where silver is traded. This is where the alleged manipulation has been taking place.

Along with the other exchanges, COMEX regularly publishes a COT (Commitment of Traders) report. This tells you the net positions (long or short) of all the small speculators (taken as a group), along with the net positions of the large players that are commercially involved in that market (the "commercials").

This is very useful information. For example, companies like Kellogg's and General Mills are among the "800-pound gorillas" in the grain markets, and are much more influential than individual traders. If you were trading in their markets, you'd want to know what they were doing.

Market conditions change, and commercial players take different positions in the markets over time. Sometimes they're net long, other times net short. This is true for all commodities and all markets...

Except silver!

I ran the numbers for all commodities traded in significant numbers on COMEX, going back to 1986. In all that time, in every market, commercials were sometimes net long, and sometimes net short...*except* in silver. In silver, going back to 1986, the commercials have always been net short. Usually, *massively* short.

What do I mean by "massively"? Let's compare silver to other commodities. The current COT numbers for wheat show commercials are long by 63,654 contracts and short by 108,898: net short ratio is 1.7 (1.7 contracts short for every 1 long).

Corn has 300,645 to 466,759—a net short ratio of 1.55. Soybeans, net short of 1.7. Feeder cattle, net **long** ratio of 1.87. Cocoa, net **long** of 1.19. Sugar, net short of 1.65. Cotton, net **long** of 1.03.

Get the idea? Almost all commodities have the commercials net short—or long—by a ratio of 2 or less. (COMEX gold is unusual, with a net commercial short ratio of 4.33. But it's widely believed that this market is orchestrated by the bullion banks—more on this in a later issue).

What's the ratio for silver? Commercials in the silver market are net short by a ratio of ***9.34***! Almost 10 contracts short for every contract long!

Does this make any sense? How could the large players in *any* market be short for 18 straight years? Even more bizarre—a market that's been in a structural deficit for almost that entire time? This makes no economic sense whatsoever...

Until you understand who those players are. Silver is unusual among commodities: it has a "user's association," an organization made of companies that use silver in their products. Companies in the Silver User's Association account for 80% of all the silver used in the United States: they make film, jewelry, electronic components, etc.

Obviously, these companies have an economic incentive to keep silver cheap. The question is: do any of them have a behind-the-scenes agreement to orchestrate the price, by dumping contracts on the market whenever the price gets too frisky?

Analysts argue about this vehemently. Some say there's no manipulation, others angrily insist there is. Accusations have been flying back and forth for years. Who's right?

Here's my answer...

It doesn't matter!

I don't bother participating in the arguments on this issue, because I don't care. Maybe there *is* a cartel of sorts to suppress the price—silver wouldn't be the first commodity to have this happen, nor would it be the last. But it doesn't matter either way, because...

The market will overwhelm any manipulation anyway.

Yes, a cartel could suppress the price of a commodity for a while by shorting futures. And yes, this would make the physical price cheaper. (For example, 37.6 *billion* ounces of "paper" silver traded through COMEX and London markets in 2002, while less than 800 million physical ounces were produced. The paper contracts overwhelm the trade in the actual commodity itself.)

But cheap physical creates conditions that would eventually overwhelm the cartel's ability to manipulate the price. This recently happened in copper: the commercials were net short, but the demand for the physical overwhelmed them and flushed them out of their positions. Once the dam cracked, it quickly burst and the shorts were forced to cover (commercials are still net short, but the ratio is only half what it was last fall). The longs stampeded all over them on the way up, and now copper is at an 8-year high.

In the case of silver, the price has been sitting in the basement for over a decade. As a result, silver mines have been bleeding red ink. Unprofitable mines don't work all of their claims: operations that would be profitable at a higher silver price, but aren't at the current price, are shut down. Only the cheapest, easiest-to-extract deposits are worked. This reduces the amount of silver available on the market, putting more upward pressure on the price.

Plus, cheap silver encourages industrial usage. Alternative materials aren't used because silver is so inexpensive. This increases demand for the metal, again stoking the pressure.

And, as I mentioned earlier, a lot of silver is consumed and not recycled. When silver is cheap, it's often not worth the expense to recover it. Again, this reduces the available silver and supports the price.

So, as we've already seen, that puts us in a 14-year structural deficit. Tens, even hundreds of millions of ounces have disappeared each year. Normally, the price would go up in this situation—the consumption would thus be reduced, and the production increased, until everything's balanced again.

But, the price *hasn't* gone up. That means that the pressure cooker has been getting more and more pressurized, and the explosion is coming. The recent price gain is only the whistle from a crack in the seam...and it doesn't matter if somebody is trying to sit on the lid or not. It's going to explode either way.

So how can you profit?

Investors who get in now will, I believe, be in for the ride of their lives. We've seen wild gyrations already just this week—this market will be anything but dull.

But you have to play it correctly. Don't get caught up in the paper games on COMEX or other exchanges, chasing after leverage. In the best of times, any futures market is a snakepit for small investors. And, as we've seen, there's reason to suspect that silver futures are being puppeteered by the large players anyway. Stay out of their territory.

Many silver investors are discouraged about the recent dip, but I'm happy. When silver jumped above $8.00, I started cautioning everybody to ease back from taking new positions—I knew silver went too far, too fast, and a pullback was imminent. And just as I expected, that's what happened.

I believe the main shakeout is now behind us. Silver will still be volatile, but I think anything below $7.00 is a great opportunity. As I mentioned earlier, I'm looking for $25 silver in 3–5 years. It won't be this cheap for much longer.

Silver stocks

If silver goes as high as I expect, you can make a killing if you're positioned in the right mining stocks.

If you're going to invest in a silver mine, I recommend **Coeur d'Alene Mines Corporation (ticker symbol CDE)**. CDE is the world's largest primary silver producer (and incidentally, a significant producer of gold as well).

CDE owns two of the largest primary silver mines in the U.S. (in Nevada and Idaho). In addition, some of their South American properties are among the lowest-cost silver mines in the world.

Last year, CDE produced 14.2 million ounces of silver, at an average cash cost per ounce of $3.27. Total gross revenue, including silver, gold, and other income, was $109.7 million.

Unsurprisingly for a mining company, CDE has not been profitable for several years. However, I expect great things for 2004. Last year, CDE completed a major debt restructuring. It was expensive, but well worth it: CDE is now much stronger financially, and is in a great position to take advantage of rising silver.

Plus, (and this is crucial), in 2003 CDE received an average price per ounce of only $4.87 for their silver. But silver is now several dollars higher, at $7.00 or so as I write this. Even if silver doesn't go any higher, and even if CDE doesn't increase production over last year, $7 silver over 12 months would still give CDE an extra $30 million...which is an increase over last year's entire gross revenue by *more than 27 percent*.

You see why I like CDE so much. Every dollar that silver goes up gets multiplied over millions of ounces, and has a huge effect on the bottom line. (Incidentally, this leverage is even more pronounced with some other mining stocks, but as the largest producer CDE is the safer and more stable bet.)

Are there still risks involved in CDE? Sure—there's no such thing as a mining stock that's guaranteed to go up. That's why I don't recommend putting more than 10–20% of your precious-metals portfolio into mining stocks: for the rest, I recommend that you consider...

Investing in physical silver

My favorite way to profit from silver is to buy and hold physical silver. Silver in your possession can't be defaulted upon, or manipulated in a paper market. It's yours, to do with as you please. The "physical" in your hand is the safest way to profit from your silver.

Here are my recommendations...

100-ounce silver bars that are hallmarked by Johnson Math or Engelhard. These are available for about 35 cents per ounce over the spot price of silver, and a few thousand ounces can be stored easily in most large safety deposit boxes. These bars are extremely liquid and can be sold immediately if necessary.

In a hot silver market, investors should look forward to seeing the premiums on these bars expand. Basically, in a sizzling market the refineries can't make enough bars to keep up with demand, so dealers raise the price of what they'll pay for bars. At $20 silver the premium could expand from 75 cents to as much as $1.50 on the buy side.

Next, I like **Gem Proof Silver Eagles**. These are limited mintage U.S. Silver Dollars that weigh 1 ounce and have been struck every year from 1986 to 2003.

You can buy a complete 19-coin set, graded by PCGS and NGC as Ultra Cameo PR69, for $5,250. This set includes the coin struck at the West Point mint in 1995—this is a spectacular and very popular rarity, only 30,125 of these were struck.

Here's why I like this set so much: since only 30,000 of the 1995s were ever struck, only 30,000 complete sets are possible. So these sets have explosive upward price potential—with millions of collectors coming into the market (thanks to the U.S. Government's ongoing commemorative programs), and a hot silver market, I fully expect that $10 silver will make these sets jump to over $10,000. $15 silver should make them pop to over $15,000.

An 18-coin set graded PCGS or NGC Ultra Cameo, but without the rare 1995 coin, can be had for just $1,850. I think this set should jump to $4,750 when silver hits $10.

Warning: Avoid PR70 (so called "perfect coins")—they're overpriced and I expect their price appreciation to lag dramatically as silver rises. The PR69 quality coins are just as nice, and are only a fraction of the price.

I also like **Gem Uncirculated MS65 U.S. Morgan Silver Dollars** struck from 1878-1921, and graded by PCGS and NGC. They're currently selling for about $120 a coin. They are just shy of an ounce of silver but these coins have a nice upside in a hot silver market. With Silver at $15 an ounce I'd expect these coins to be worth about $400 each—so they offer potentially better leverage on a silver investment than just plain silver bullion.

All of my rare coin recommendations can be viewed at http://www.FinestKnown.com.

I believe we're in for a wild ride with silver. Get on board now while it's still cheap!