GOLD & ENERGY ADVISOR

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"Al-Qaeda attacks Saudi oil—again! The pressure on oil is building...

"I'm looking for $100 oil in the next few years, and you can make a killing if you're positioned right. Here are 5 energy stocks that should blast off when the oil shock hits..."

James DiGeorgia, Editor

- **Up to 100,000 predicted dead in upcoming Saudi violence**
- **3 triggers for the coming oil shock**
- **Dallas Federal Reserve says: get ready for hundreds of billions of dollars in economic damage!**

Analysts, reporters, and global markets were shocked... but you weren't, if you read my last newsletter.

On May 29th, just three days after I warned you it was coming, four al-Qaeda gunmen attacked oil targets in Khobar, Saudi Arabia. They killed 16 people and took dozens of hostages.

After a 25-hour siege, Saudi police attacked. 22 people died in the shootout.

One of the terrorists was wounded and captured. But somehow, the other three got away... through streets *swarming* with police and elite commando units, and despite police helicopters circling above. They just casually strolled right out, and escaped. Saudi officials are at a loss to explain how this could have happened... and the terrorists still haven't been found, despite a "thorough" lockdown and search of the city.

Apparently the police *let* them go. Remember what I told you: the Saudi people *support* al-Qaeda terrorists.

Even though the Saudi government is our "friend," the people are **not**. They agreed with Abdulaziz al-Miqrin, the leader of al-Qaeda in Saudi Arabia (!), when he criticized the government for "supplying the United States with oil for the cheapest prices, according to their master's wish, so that their economy does not collapse." (Remember, Osama bin Laden wants oil at $144 per barrel—which would *devastate* our economy.)

Then, again on June 5th, Saudi police had a gun battle with Muslim militants in Jeddah. This time, al-Miqrin called on Saudis to overthrow the kingdom itself. He thundered that 2004 would be a "miserable and bloody" year for the kingdom.

THE GOLD AND ENERGY ADVISOR

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I warned you about the terrorist threat to Saudi oil, but Western media have largely pooh-poohed the idea. Now they're finally waking up. *The Economist*, the respected British newsweekly, said a week or so ago:

"By any measure, Saudi Arabia is in an unprecedented crisis. Terrorists bent on overthrowing the established order are plainly entrenched and fanatically determined."

Just in the last year, there have been five deadly car bombings in the Saudi capital of Riyadh alone. Plus, there have been numerous shooting rampages, assassinations, and gunfights with police.

The Saudi government is scared. In Dhahran, the home of Aramco (the big Saudi/American oil company), new security checkpoints are popping up around oil facilities. Sniper's nests are also appearing around town. (Stable societies don't build sniper's nests!)

Nevertheless, many analysts still downplay the threat. They point out that Aramco's facilities have 5,000 guards, along with fences, barbed wire, hydraulic barriers, night-vision goggles, and all sorts of fancy gear.

But the gear is only as trustworthy as the people. When even the *police* let murderous terrorists escape, how reliable are ordinary guards going to be?

Plus, many of the workers in the oil fields themselves are Shia Muslims, rather than Wahhabi Sunnis like the majority of Saudis. In the Middle East, Sunnis and Shias hate and fight each other more often than not. No doubt, many of these Shia workers have little or no loyalty to the Sunni government... especially since it keeps them in poverty, while the corrupt royal family lives in their glittering palaces.

A few days ago, the US State Department warned all American citizens to leave Saudi Arabia, for their own safety. And a recent article in the *Wall Street Journal* said, "'People have lost their confidence in the Saudis' ability to protect them. Even the oil people are in shock,' said an American executive, whose company has decided to relocate him to Dubai, United Arab Emirates. 'People used to feel that the attacks were random, that the

Saudis were addressing the threat in ways that we never knew. That illusion has been shattered. The bad guys seem able to attack at will.'"

And the wave of terrorist violence is just beginning. As *The Economist* said:

"'This is just the sunrise,' says a human-rights activist in Dammam. 'We're in for a rough five years,' says an American executive in Riyadh. 'I foresee an Algeria-type situation,' he said, alluding to the civil war in the 1990s which *left 100,000-odd dead.*"

The Saudi situation looks grim. And as I warned you last time, the fall of its government will mean skyrocketing oil, instantly.

That might happen tomorrow, or 5 years from now. But when it does, oil (and gold) will explode. I expect most other investments will get slaughtered.

But last time, I also said oil would soar even *without* the terrorist threat in Saudi Arabia. I promised to tell you why in this issue. So, as promised, here are...

3 triggers of the coming oil shock

Even without the problems in Saudi Arabia, oil looks incredibly bullish. Most analysts are looking for oil prices to come down, and that's very possible in the short term. However, I think that long-term, over the next few years, oil is one of the most explosive investments I've ever seen.

If you remember the OPEC oil embargo in the early 1970's, you know how devastating an oil shortage can be. But I think we're in for a shock far worse than that one, complete with skyrocketing inflation and stock market crashes. Here's why...

Trigger #1: Piracy and Terrorism

Terrorists are planning to crash the global economy... and they aren't limiting themselves to Saudi Arabia to do it.

Oil is the lifeblood of the world's economy. Take away the oil, and the global economy craters. We know it, and the terrorists know it.

How could you take away the oil? One way is of course to go after the producers like Saudi Arabia. But most producing countries aren't as ripe for collapse as the Saudi government is.

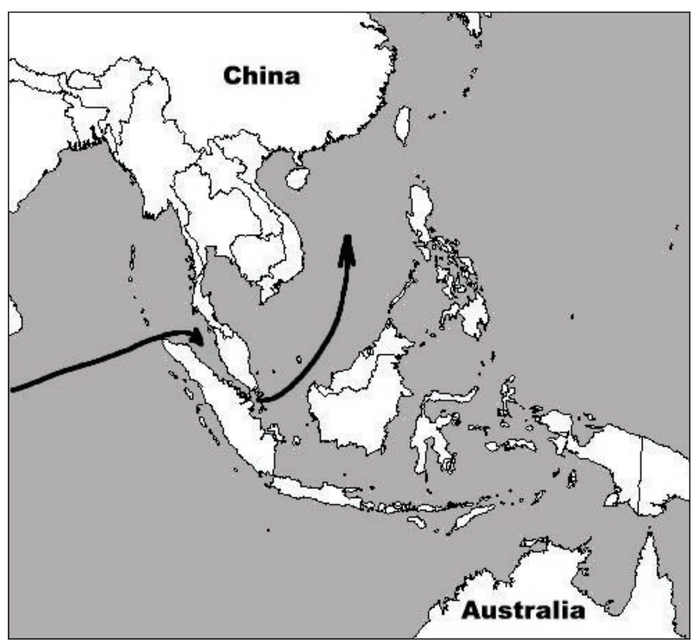
So another way is to go after the oil once it's been produced. The easiest way to do this is to prevent it from being delivered to the refineries... and the easiest way to do *that* is to go after the tankers the oil is shipped in.

If you were a terrorist who wanted to attack oil tankers, where would be the best place to do it?

The Malacca Straits

The Malacca Straits is a narrow, 550-mile long waterway bordering Indonesia, Malaysia, and Singapore. **One-half** of the world's seaborne oil supply passes through it every year: millions of barrels of crude each day, moving from the Persian Gulf to China, Japan, and South Korea. Japan is especially dependent on this traffic: 80% of Japan's oil passes through the Straits each year.

And oil isn't the only good target here. 50,000 commercial vessels pass through the Straits every year. The geography of this area means that all



The Malacca Straits

Chokepoint for half the world's oil tankers, and one-fourth of its commercial traffic. Arrows show Asian oil route.

Latest prices as GEA goes to press—June 14, 2004

Comex spot contract: silver $5.89, gold $387.30
Nymex spot platinum: $796.00, palladium $225.00
Nymex Light Sweet Crude Oil $38.45

Silver coins		Dealer will buy at this price	Dealer will sell at this price
100 1 oz. silver American Eagles		$730	$845
100 1 oz. common rounds		$579	$675
$1,000 face value US pre-1965 coin bag (circulated)		$4,100	$4,600
$1,000 face value US circulated silver dollar bag (VG or better)		$7,000	$8,900
US Morgan silver dollars	PCGS MS64	$50	$65
	PCGS MS65	$110	$135
	PCGS MS66	$260	$310

Platinum coins			
U.S. Platinum Eagle:	1 oz.	$766	$830
	1/2 oz.	$378	$450
	1/4 oz.	$182	$225
	1/10 oz.	$70	$99

Gold coins				
Australian Kangaroo			$383	$413
British sovereign (Kings)			$90	$97
(Elizabeths)			$90	$97
Canadian Maple Leaf			$384	$406
Credit Suisse 1 oz. gold bar			$376	$401
Mexican 50 peso Centenario			$444	$492
South African Krugerrand			$387	$415
US Gold Eagle:		1 oz.	$389	$416
		1/2 oz.	$189	$219
		1/4 oz.	$89	$112
		1/10 oz.	$34	$49
US $20 double eagle:				
Liberty	Raw	MS60	$440	$510
	NGC	MS63	$650	$740
	NGC	MS64	$1,100	$1,450
	NGC	MS65	$3,500	$5,550
Saint Gaudens	Raw	MS60	$425	$500
	NGC	MS63	$515	$580
	NGC	MS64	$600	$785
	NGC	MS65	$970	$1,250

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

shipping is funneled into the Straits—it's either that, or add more than 1,000 miles extra to your trip by sailing all the way around Indonesia. Overall, **one-fourth of the entire world's commerce** passes through this narrow waterway.

As you can guess, all this concentrated traffic means easy pickings for pirates. This area has been a pirate's paradise since the 1800's, and lately it's been drastically increasing. Worldwide, piracy has tripled in the last decade, up 20% last year alone: and a full **one-third** of all 445 recorded pirate attacks last year occurred in Indonesia.

Some people are surprised to learn that piracy still exists. Yes, the days of the cutlass and the Jolly Roger are long gone, but piracy is still big business. Today, pirates tend to drive modern speedboats with .50-caliber machine guns. They speed up to a vessel, shoot until the crew surrenders, climb aboard and steal whatever they can, then leave.

Piracy is bad enough. But for the last year or so, some frightening trends have emerged. Terrorist groups, especially al-Qaeda, have been active in the Straits as well, but not in the ways you'd expect...

For the last year or so, ships have been getting hijacked rather than plundered—but only temporarily. For example, the chemical tanker *Dewi Madrim* was hijacked by ten "pirates" with machine guns and speedboats off the coast of Sumatra. The pirates didn't steal anything: they just drove the ship for an hour, changing speed frequently, then left. They took the captain and first officer with them (and these officers are still missing).

This is one of many examples where the "pirates" drive the ships, and kidnap the officers, without being interested in plunder. Apparently the terrorists are teaching themselves to operate and navigate large ships. Just like the 9/11 terrorists trained to fly jetliners for a while before crashing them into large buildings!

What could they be planning?

The Malacca Straits has a massive chokepoint in it: at its narrowest point in the Phillips Channel, the Straits are a mere 1.5 miles wide. Also, at one point the Straits are only 82 feet deep. Many large ships barely skim above the bottom here. One or two sunken ships would stuff up the entire Straits, preventing any ship from passing through. For each month the Straits were blocked, over 4,000 ships from all over the world would have to be re-routed... and 1,000 miles added to their voyages.

Global trade would be disrupted for months. This is just the kind of math that al-Qaeda likes: one small effort equals enormous impact.

Some officials fear that even worse attacks are coming. They fear the terrorists will hijack a tanker transporting dangerous chemicals, such as LNG (liquid natural gas), and drive it into a major port like Singapore...

A supertanker full of LNG, if successfully ignited, would become a floating bomb equivalent to 700 kilotons of TNT. That's 46 times as big as the atomic bomb that destroyed Hiroshima!

And this isn't all:

- There have been at least ten cases of pirates stealing tugboats for no apparent reason; officials worry that terrorists are planning to tow a hijacked tanker into a port, then blow it up.
- US intelligence officials say that dozens of acoustic sea-mines have disappeared from a high-security North Korean naval base. Many believe they are now on al-Qaeda ships.
- Meanwhile, some terrorists are learning how to scuba-dive, apparently to attack ships from below. The Abu Sayyaf group in the Philippines kidnapped a diving instructor back in 2000. A couple of weeks ago, he finally escaped. He said his kidnappers wanted diving lessons. Also, the owner of a diving school near Kuala Lumpur has recently reported a number of ethnic Malays wanting to learn about diving, but being "strangely uninterested in learning about decompression." Aren't they planning to re-surface after their dives? Or maybe they'll be slapping some of those mines on the bottoms of ships, and don't think they'll survive?

The US Government is worried about these threats. Defense Secretary Rumsfeld met this month with Asian officials to discuss joint patrols in the Straits—and to propose US Marines stationed permanently close by. (So far, his proposals have been rejected.) Other governments are scared too; the chief of the Philippines Coast Guard recently announced that heavily armed "sea marshals" will now be deployed on passenger ships.

And that's *still* not all:

- After 9/11, US-led forces in Afghanistan found a video showing plans to attack US Navy warships headed toward the Middle East, in a narrow "kill zone" in the straits.
- We also captured Ahmad Belai al-Neshari, the chief of al-Qaeda naval operations. He had a 180-page dossier that listed large cruise liners leaving from Western ports as "targets of opportunity." Owners of the *Queen Mary 2*, the largest cruise liner in the world (it cost $1.3 billion), have confirmed terror threats to the ship.
- We even found terrorist plans to attack the British aircraft carrier *Ark Royal* as it traveled through the Gibraltar Straits! If they're willing to attack modern aircraft carriers—the mightiest naval fortresses ever in history, bristling with guns, missiles, fighter planes and bombs—then an oil tanker would be a soft target indeed.

Don't forget that al-Qaeda has already successfully attacked several ships (besides the ones they've hijacked). The *USS Cole* had an enormous hole blown in its side by suicide bombers, killing 17 of our sailors. And the French tanker *MV Limburg* was torpedoed off the Yemeni coast. (Strangely, the *MV Limburg* was hit by only one torpedo—the terrorists didn't try to sink it. It seems to me that it was just a test—they wanted to know how much damage a torpedo would do to a tanker...)

Naval officials think that al-Qaeda now has as many as 28 ships. Nobody knows where they are, either: they left their home ports in the Horn of Africa last September, and haven't returned.

All we know for sure is that the terrorists have been practicing for a lot of different possible attacks, and have a lot of material and ships to work with. I think there's a good chance that they're planning to attack several targets simultaneously, just like they did on 9/11. First of all, that wasn't the first time they had planned multiple, simultaneous attacks (they had an earlier plan for multiple hijackings, which didn't go through)—so they seem to favor this approach. Also, they saw how quickly we clamped down on air travel security after 9/11: no doubt they figure that multiple sea attacks need to go all at once, otherwise the later ones might not succeed.

Maybe you're thinking such attacks wouldn't affect us much here at home. Not true: first of all, cruise ship passengers are at risk, as are the crews of American freighters. Second, a successful attack on any large port or vessel will almost certainly crash the financial markets, as the public finally wakes up to the threat to global trade (although you, as a reader of this newsletter, are much better informed).

Finally, the closing of the Straits would mean immediate inflation, around the world. When oil tankers have to add another 1,000 miles to their routes, obviously each trip takes far longer. That means fewer voyages per vessel per year, restricting the amount of oil delivered to the world—and skyrocketing the price.

Trigger #2: Increasing demand

The global economy burns through 80 million barrels of oil each day. And the thirst for more oil grows every year.

The United States is the biggest oil consumer in the world, at 20 million barrels last year. Consumption in 2004 is projected to grow by an additional 420,000 barrels per day.

But our growing demand is nothing compared to other countries. China and India are starting to have massive impacts on the global oil economy. And their growth is just beginning—their economies are expanding at 8-9% per year. Both countries are only in the early stages of economic development and industrialization

China has already replaced Japan as the second-largest oil consumer in the world. Chinese consumption is exploding; today, China consumes over one million barrels per day more than in the year 2000.

China and India combined will have three billion people by 2010. This will be 40% of the world's population, concentrated in just two countries—and both are just beginning their journeys into heavy industrialization. (China alone consumes a staggering *40%* of the world's cement!)

The number of cars in China is increasing by 50% each year. Billions of people want to trade in their bicycles for automobiles—and gasoline consumption is going to explode.

It's easy to see what will happen when billions more people start bidding for oil. Especially since there's...

Trigger #3: Global oil production is straining

In modern history, there has always been a "swing producer": one or more countries with extra, unused oil capacity.

Up until 1970, the United States didn't produce to full capacity. During a crisis, we could make up for any shortfall by increasing our own production. So for example, we were able to ignore the Arab oil embargo in 1967: when Saudi Arabia and Libya refused to sell us any oil, we just pumped more of our own out of the ground.

By 1971, this had changed—US production peaked and started to fall, and we've been dependent on foreign oil ever since. So the Arab oil embargo in 1973 hurt us badly, as many will remember.

Since the early 1970's, Saudi Arabia has been the world's primary swing producer. When oil shocks threatened, the Saudis could (and usually did) crank out more oil onto world markets, to keep things calm. The Saudis want a stable, secure market for their oil: wild swings and disruptions would encourage the development of alternative energy sources, and they don't want that.

But recently, all this has changed. Every year, the world demands more and more oil... and even Saudi Arabia is running at full capacity now. There are no major swing producers left... no extra capacity available (and no more oil for growing new consumers such as China and India.)

All of the OPEC countries combined have only 1.5 million barrels per day of spare capacity left. This sounds like a lot, but it's less than 2 percent of global daily demand. If world demand goes up by another 2-3% (which is expected by the end of 2004)... there's no more oil!

Oil exporters are desperately trying to produce more crude. Saudi Arabia is pumping an extra 500,000 barrels per day starting this month, which means they're now running full-out. They're working to increase capacity by another 800,000 barrels, but that won't happen until the autumn. After that, there's another 700,000 barrels scheduled to come on-line 18 months from now.

But all of this adds up to maybe 2 percent of daily demand... and the demand gets bigger each year, and will outgrow the extra production quickly. Plus, this will actually *decrease* the overall amount of oil long-term: Saudi Arabia's new capacity was originally designed to replace some of the stress on the existing oil fields, and extend their life. Now that won't happen: everything will still be running at full capacity, which damages the fields and reduces the overall amount produced.

Why isn't anybody trying to find more oil? Well, they are, but they aren't finding any. In the last 30 years, there's only been one "elephant" strike (industry jargon for a huge field): the Kashagan field in the Caspian Sea, off Kazakhstan, which was found in 1999. All other discoveries have been minor.

Meanwhile, the big established Western fields are all in decline: Alaska, the North Sea, and Texas. And they aren't being replaced by new ones.

I'll have a lot more to say about this in a future issue. For now, I'll just say this: oil companies are getting desperate.

They need to replace the millions of barrels that they pump every day, but they aren't finding any major deposits. As a result, they're buying other companies instead, to get *their* deposits. Somehow, they need to get more oil, and this is the only oil they can find.

The recent frenzy of oil mergers and acquisitions tells us that the industry is badly scared. BP just spent $8 billion for 50% of TNK International Co., a Russian oil company. Also, don't forget that BP merged with Amoco... Exxon merged with Mobil... Chevron merged with Texaco... and Conoco merged with Phillips. And this isn't limited to American companies: for example, the French company Total SA merged with Belgium company Petrofina SA, then the combination merged with the French company Elf Aquitaine SA.

So we've talked about terrorist threats to production and delivery... increasing demand... and falling production.

All of this means an explosion in oil prices is coming...

What will happen when the oil shock hits?

Since World War II, the US has had 10 recessions. High oil prices preceded or coincided with 9 of them.

But those were all mild compared to what's coming.

Any one of the triggers I've described could have oil shooting up over $50 per barrel. If more than one trips at the same time... oil goes as high as $100. Al-Qaeda might even achieve their target of $144!

Oil at $38-$40, where it is today, is already strangling our economy. High oil prices make everything else much more expensive. For example, fuel is 10-15% of the total operating costs for a typical airline. Each additional penny-per-gallon boosts costs by $180 million across the industry. If oil stays around $40, the US airline industry could lose as much as *$5 billion* this year. (United Airlines alone expects to spend $425 million more in fuel for 2004.) And remember, several airlines are already in bankruptcy!

And other industries are getting clobbered just as badly.

Oil is so high that even a 20% decrease would still leave us suffocating. A recent study by the Dallas Federal Reserve said that even if oil goes down to $30, and natural gas goes down to $5 (it's currently above $6)... the US will lose a whopping $115 billion of economic output over the next 3 years.

If oil and gas stay at their current prices, we're looking at a staggering *$210 billion* loss. Imagine what will happen when oil hits $100!

We can't prevent it... but we can profit from it!

Most "conventional" investments are going to be crushed when all this hits. But others will be very lucrative.

First of all, make sure your foundation is sound. Gold should be the core of your portfolio; I expect gold will boom over the next few years even if oil somehow stays flat. There are many other bullish factors for gold besides oil, and I'm looking for $1000 gold whether or not oil takes off. So make sure you're well positioned in gold before you do anything else.

Also, don't be flushed out by the recent gyrations in precious metal prices. Remember, my recommendations are for large, macro-trends that are still developing. I'm warning you ahead of time so you can get on board now, while it's still cheap to do so. Don't take a "day-trader" approach, as so many others do—prices are sure to fluctuate in the short-term, but over the next few years I think these investments can make you very wealthy.

Once you're positioned properly in gold, I strongly recommend increasing your holdings in energy stocks. I've described some grim scenarios in the last couple of issues (and I certainly hope they all can be avoided)—but even if none of them come to pass, I expect energy prices will stay strong. World-wide demand is booming and supply is lagging, so energy should be a strong investment.

I've previously recommended these energy stocks: Murphy Oil (ticker symbol **MUR**), Devon Energy (ticker symbol **DVN**), and Transocean (ticker symbol **RIG**). I still recommend them, especially on pullbacks. For this issue, I'll also add…

Energy Select Sector Spyder (Ticker Symbol **XLE)**

A good way to invest in energy is through an Exchange Traded Fund (ETF) that invests in energy companies. ETFs are similar to mutual funds: they're a diversified portfolio of stocks, professionally selected. (There are differences, of course: ETFs normally have lower management fees, you can buy and sell during the day, and they don't have end-of-day pricing like mutual funds.)

I recommend XLE, which is invested in companies from oil, gas, energy equipment and services. The price is currently in the low $30's.

BG Group (BRG)

My next recommendation is BG Group, a British integrated gas company. In 2003, its revenues were approximately $6.4 billion. Its key businesses include exploration and production, liquefied natural gas, transmission and distribution, and power generation. I like BRG because its capital expenditures budget is focused on natural gas, so the company's reserves should increase. This will make the company more valuable. Its current price is in the low $30's.

Burlington Resources (BR)

I also like US oil and gas producer Burlington Resources. BR is a holding company, with subsidiaries operating in oil and gas exploration and production worldwide. It has proven natural gas reserves of 8.074 trillion cubic feet, and proven oil reserves of 282.1 million barrels. Plus, unlike many others, BR has been replacing its reserves at a low cost and strong rate. Last year's revenues were $4.3 billion. Currently the price of the stock is in the mid $30's.

Golar LNG Limited (GLNG)

My next recommendation is the riskiest: Golar LNG Limited. It owns and operates 8 LNG vessels, with 4 more under construction. It's headquartered in London and is listed on the Oslo and NASDAQ stock exchanges. Revenue for 2003 was approximately $133 million, and earnings are expected to be very strong over the next few years.

As I mentioned, oil and gas cargo shipping is vulnerable in the world right now. If there are continued piracies and GLNG is not impacted, these shares can become very valuable. But, if they *are* involved, the stock price will suffer (although their insurance could mitigate some of their losses). The stock price is currently in the mid-teen level.

Chicago Bridge & Iron Company (CBI)

My last recommendation is Chicago Bridge & Iron Company. CBI is a publicly owned Dutch company founded in 1889, and trades on the NYSE. The company is one of the world's leading engineering, procurement and construction companies and has specialized in the natural resources industries, especially energy and LNG. Revenue has more than doubled in the last five years, and earnings in the same period are up approximately 70%. Financial performance is expected to remain strong. The stock price currently trades in the mid-teen level.

Again, strong energy prices should continue to benefit these companies, and these stocks can hedge your portfolio against any energy disruptions. In our modern economy, energy shocks can be brutal—so I strongly recommend protecting yourself!