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"Greenspan boosts rates, as the US current-account deficit hits record high! This devastating combination will doom our fragile economic 'recovery'!

James DiGeorgia, Editor

"The dollar is gasping for air, and headed for a fall. Gold won't be this cheap for much longer!"

- **Rate hikes will hurt, not help, our economy!**
- **Greenspan is inflating the dollar at the same time he's "fighting inflation"!**
- **Famous Wall Street analyst confirms: buy gold now!**

The US dollar is in SERIOUS trouble.

Alan Greenspan's Federal Reserve just raised interest rates for the first time in four years. Normally this would strengthen the dollar—but not *this* time. We're facing a unique combination of events: several "crisis factors" for the dollar that, all together, will be a "perfect storm" for our currency.

Our current-account deficit is the highest ever in history—an annual rate of $580 *billion* dollars. At the same time, corporate profits are sinking and interest rates are rising. Inflation is now building up fast, and when it's fully unleashed, we're going to see a hurricane sweep through our economy.

Greenspan's interest rate boost is way too little, and far too late. He might have had a chance to steer us clear of the storm a couple of years ago, but not any more. Instead, rate increases will now just make the problem worse, as I'll explain shortly.

Even the mainstream press is waking up to the looming disaster. On July 1st, the *New York Times* said...

> **"Inflation and market interest rates are far ahead of Alan Greenspan's federal funds rate...Mr. Greenspan has opened wide the door to inflation in the United States."**

The article complained that the Fed held interest rates too low for too long, and has stoked inflationary fires in our economy. It said that Greenspan has "squandered" the gains that former Fed chairman Paul Volcker made in eliminating inflation in the early 1980's. This is a damning accusation, especially when you think back to how painful (but necessary) Volcker's clampdown was. Our economy was on the brink of runaway hyperinflation and collapse, and Volcker barely saved it. Now Greenspan has undone Volcker's work.

THE GOLD AND ENERGY ADVISOR

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The *Times* pointed out that corporate profits have been slowing, and only 3 times during Greenspan's tenure have rates risen while profits were weakening. Those rate increases brought us the recession of 1990-91, the financial crises of the summer of 1998 (when the entire global economy almost imploded), and the bursting of the stock market bubble in 2000. Now Greenspan is doing it again…

And this time might be *worse* than any of those. This time, there are other forces at work besides weakening profits. I'll start with…

The current-account deficit

The current-account balance measures the net inflow/outflow of cash across our borders from other nations. It includes the overall trade balance (goods and services that are bought across international borders), as well as net inflow/outflow of investment capital.

For years now, the US has been in a current-account deficit. More cash is flowing out of our country than is coming in. This is a sign of an unhealthy economy—we're buying and consuming more than we're producing. Much more, in fact—by hundreds of billions of dollars each year.

In the first quarter of 2004, our current-account deficit hit a record $144.9 billion, up 14% from the previous quarter. Annually, that's a staggering $580 billion. We're bleeding out a net $1.6 billion to other countries *every day*.

And the deficit balloons up bigger each month. March had already set a new record, then April was another $1.7 billion higher again: 3.6% above March's deficit.

Why is this such a big deal?

Imagine how long you'd last in your current household, if every month you spent more than you earned. First, you'd go through all your savings.

Then you'd start accumulating debt. You could do this for quite a while, assuming your credit rating was good. But the longer you did this, the bigger and more spectacular your implosion would be once you finally maxed out your credit.

One way or the other, whether it took a short time or a long time, you'd be bankrupt eventually.

And that's just where the US is headed—bankruptcy. Our current-account deficit is more than 5% of our GDP; double the amount that most economists say is sustainable.

Even the top government officials and insiders are forecasting doom. For example, Gerald Corrigan is the former President of the Federal Reserve Bank of New York, and recently spoke at the Boston Federal Reserve Bank conference. He said that if we don't fix the deficit "in the next two or three years, then the chances of a financial disruption rise in an alarming way." Corrigan spoke of "international financial market liquidity drying up," comparing it to the stock market crash of 1987 and the worldwide financial crisis of 1998.

But, he also said that we can't reduce the deficit too abruptly, since that might cause "systemic risk" of other disruptions. Basically, we're between a rock and a very hard place—world markets are threatened if we don't reduce our current-account deficit, but their stability is also threatened if we reduce it too fast.

Corrigan is not alone in his ominous predictions. Former Secretary of the Treasury Robert Rubin said, "The risk is that the large current-account deficit and our large fiscal deficit so undermine confidence in our policy regime that the providers of capital no longer do so except at *much higher interest rates*." And skyrocketing interest rates would of course immediately crash financial markets all around the world. (Except for precious metals, which would boom.)

What's the best-case scenario? There isn't one! As economist Catherine Mann of the Institute for International Economics said, "*There is no good outlook*."

The current-account deficit is a grave crisis, and it's growing worse each month. This alone would cast a gloomy shroud over most conventional investments (along with being wildly bullish for gold). But there's more to the picture than this…

Economic Slowdown

As the *New York Times* mentioned, we're now entering a period of rising interest rates, at a time when corporate profits are sagging.

In a healthy economy, this wouldn't be. We've had rock-bottom interest rates for several years, which should have stimulated wild economic growth. In fact, the growth should be so spectacular that rates need to rise just to restrain it.

But that's not what's happening. Rates are rising for other reasons (which I'll get to shortly). In the meanwhile, the economy is weakening.

For example, real estate is one of the few sectors actually stimulating our economy right now. Yet in April, home-building declined by 2.1%. This shocked economists, who expected 1.3% at the worst. According to the Mortgage Banker's Association, mortgage applications in early June were down a staggering **68%** compared to last year.

A week ago, Reuters said that companies issuing negative earnings outlooks outnumbered those that upgraded their earnings forecasts by **two to one**.

The *Houston Chronicle* recently ran an article about older Americans who were "opting out of retirement," because they had to go back to work to support themselves. According to the US Bureau of Labor Statistics, 2 million more older workers (age 55 and above) are now working compared to two years ago.

And overall employment is hurting too. Analysts were expecting 250,000 new jobs to be created last month, but the Labor Department just announced there were only 112,000—less than half the expected amount. (The Labor Department also revised April and May's figures downwards by 35,000 jobs.)

Then, we were hit with *another* economic shocker. The Chicago PMI (Purchasing Managers Index) is one of the most widely-accepted barometers of the overall economy. For June, the overall Index dropped 20.6% in one month, the biggest drop in almost **30 years**. All the individual components were ugly: employment fell 2.2%, prices paid jumped up 5.6%, new orders collapsed by 31%, and production plummeted by 32%.

As I said, this shouldn't be happening. Years of in-the-basement interest rates should have lit a fire under the economy. They didn't.

Something else was ignited instead…

Latest prices as GEA goes to press—July 15, 2004

Comex spot contract: silver $6.63, gold $403.60
Nymex spot platinum: $818.00, palladium $224.00
Nymex Light Sweet Crude Oil $40.70

Silver coins			Dealer will buy at this price	Dealer will sell at this price
100 1 oz. silver American Eagles			$720	$835
100 1 oz. common rounds			$610	$685
$1,000 face value US pre-1965 coin bag (circulated)			$4,040	$5,290
$1,000 face value US circulated silver dollar bag (VG or better)			$7,000	$8,700
US Morgan silver dollars	PCGS MS64		$50	$65
	PCGS MS65		$110	$135
	PCGS MS66		$260	$310
Platinum coins				
U.S. Platinum Eagle:	1 oz.		$792	$839
	1/2 oz.		$391	$428
	1/4 oz.		$189	$221
	1/10 oz.		$72	$94
Gold coins				
Australian Kangaroo			$404	$424.66
British sovereign (Kings)			$98	$104
(Elizabeths)			$98	$104
Canadian Maple Leaf			$401.10	$424.31
Credit Suisse 1 oz. gold bar			$398	$410
Mexican 50 peso Centenario			$460	$485
South African Krugerrand			$392	$415
US Gold Eagle:	1 oz.		$401.10	$426.35
	1/2 oz.		$198	$218.92
	1/4 oz.		$96	$111.48
	1/10 oz.		$37	$45.81
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	$580
	NGC	MS64	$700	$785
	NGC	MS65	$1,100	$1,250

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

Inflation!

The inflationary fires are starting to roar. And, as the *New York Times* article commented, "Inflation is exceedingly difficult to bring under control once it has gained a foothold."

Many companies are now raising their prices: among them are Clorox Co., Goodyear Tire and Rubber, Hormel Foods, La-Z-Boy Inc., even Krispy Kreme Doughnuts. Medical costs are up 3% since December—this is 3 times the "official" inflation rate.

According to the Commerce Department, 12-month finished goods prices have leaped by the highest amount in 14 years. The Institute for Supply Management's PPI (Index of Prices Paid) jumped 5.6% in just one month, and is up a whopping 47% just since December. More companies reported higher prices than at any time since August 1988.

Consumer prices popped up at an annual 4.4% during the first 4 months of this year—more than double the 1.9% of 2003. Core prices (excluding food and energy) are up nearly *triple* the rate of increase in all of 2003. The consumer price index hasn't been this high since September 1990.

Why are prices climbing? For several reasons. First, although oil has softened recently (temporarily, I believe), fuel prices are still in the stratosphere.

This ripples through our entire economy. For example, the US Post Office recently reported that it's getting clobbered by high fuel costs. No surprise, since the USPS has a fleet of 210,000 vehicles, driving over a billion miles and burning 800 million gallons of gasoline and diesel each year.

Of course, FedEx, UPS, and DHL are suffering too. When their costs are up, everybody else feels it in higher freight rates.

Second, raw materials have been soaring. For example, steel is up 57% just since January. Hot-rolled steel has zoomed up 120 percent in the last 12 months. Even steel *scrap* is up 90%.

Why? A recent article in the *Detroit News* blames it on "China's seemingly insatiable need for raw materials." China's economy is roaring, and consuming commodities and raw materials at a feverish rate. Worldwide commodity prices are up—*way* up—as a result.

The article focused on our auto industry. High steel prices are killing auto-parts supply companies, and the article said:

"We will see multiple bankruptcies of suppliers within the next 90 days."

One supplier admitted, "Somebody is going to die in this thing." Another said grimly: "Our goal is to be the last man standing."

The typical US car/truck contains more than $1,000 worth of steel. When steel goes up 120%, as it has in the last year, this adds another $1,200 *to each new car and truck sold in America*. Transportation costs leap up through our entire economy.

Of course, that's assuming any new cars are sold at all. Auto manufacturing is a delicate system, with many just-in-time interactions in a complicated dance between suppliers and manufacturers. If a few key auto-part suppliers go under (and the article said this is just a matter of time), the whole machine grinds to a halt. As the article noted, "Once the supply chain breaks, the whole system falls apart. You can't build a car if one part's missing." Fewer cars manufactured will mean the supply is restricted, and their prices will explode—yet another inflationary factor.

Then there's the real estate bubble. Few media people want to call it that, but that's what it is. Even the huge global bank/financial services company HSBC recognizes this: they recently published a report called, "The US Housing Bubble—The case for a home-brewed hangover." It said, "Expectations of future house price appreciations are spectacularly, and unrealistically, high."

Housing prices have skyrocketed. In the last four years, New York and Florida prices are up 50%. California, up 60%. Washington D.C. housing is up an amazing 70%.

In California, the median home price (where half the houses are above this price, and half are below) is now a ridiculous $453,590. To get a mortgage for this amount (even at a low 5.4% interest), you'd need a verifiable annual income of $102,550… and that's if you can make a $90,700 down payment! House prices in certain areas are climbing $150 or more *per day*.

It's not surprising that hardly anybody can afford a house in California any more. According to the California Association of Realtors, a mere 20% of the households in the state can buy a house now. (This is down 7% from the previous year, showing how fast the prices are climbing.)

I've already noted that mortgage applications have collapsed recently. The blowoff in the housing bubble might finally be upon us. Whether the bubble bursts now, or later, it will be catastrophic when it happens. Many, many real-estate "investors" and even owner-occupants are highly leveraged, with fully-mortgaged properties. Even a slight decline in prices will put these people "underwater" on their loans, and then the foreclosures will start. A wave of foreclosures will push prices down even further, which will blow even more people out of their properties… and so the downward spiral begins.

Cascading defaults and repossessions are a hideously ugly situation. We haven't seen these in nationwide real estate for several decades, and many investors have no clue that this scenario is even possible. When the housing bubble bursts, these people are in for a rude shock indeed.

Even non-leveraged homeowners will be hammered when the balloon pops. Untold numbers of people were suckered into ARMs (adjustable-rate mortgages)—30% of all mortgages are ARMs now. These are *not* the types of debt instruments to buy at the bottom of an interest-rate cycle, when the only direction rates can go is *up*.

Most ARMs have a lifetime cap on rates, but these can be high—often 5% above the starting rate. When rates zoom up high enough, that's an extra $536 per month, for every $100,000 on the loan. In a country that's already drowning in debt, with a miniscule personal savings rate of 2.2%, where will people get an extra $500 a month from? (And woe to the new homeowners in California who owe $300,000, maybe even $400,000 or more on their new houses! Can you imagine your house payment going up by $2,100 a month?)

Maybe you're thinking that Greenspan won't raise rates that high. I think he must, and will, for reasons I'll explain in a moment. But even if he doesn't… homeowners are *still* going to be steamrollered by ballooning mortgage rates. Most ARMs base their rates on US Treasury notes, and *those* rates have been soaring lately, way beyond Greenspan's hike. Just in the last few weeks, Treasury rates exploded upwards by a *full percent*. (The carnage in the markets was unbelievable; bonds lost 10% of their value in less than two months.)

Even if you're *not* a homeowner, you'll be affected by all this. One of the few engines driving the economy lately has been consumer spending, and a lot of that was fueled by low mortgage rates. Untold millions have refinanced their homes, and many of them pulled out some of their equity in the process. This sudden windfall of "free money" has been driving a lot of personal spending over the last few years. Now that refinancing activity is drying up (remember, mortgage applications were down by more than two-thirds), this spending is going away.

Consumer spending won't stop completely, but it will start to sputter very soon. In an economy with a fragile "recovery," any interruption of personal spending will be deadly.

So what is this all adding up to?

The collapse of the dollar!

The dollar has been sucking wind for several years now. For example, since February 2002, the US dollar has crashed 41% against the euro. Against all world currencies, it's down 4% in trade-weighted terms just since May of this year.

Now the plunge will accelerate. I've already told you about the $580 billion current-account deficit, but we're also adding another $500 billion to our national debt in 2004. Even worse, we're at the bottom of the interest rate cycle—our economy is supposed to be at its *strongest* right now, not groaning under these deficits.

As rates go up, the pain gets worse. For every 100 basis points that short-term interest rates rise (remember, they're up by 25 already), annual net interest cost on government debt and liabilities rise by $30.5 billion. A good portion of this debt is owed to foreigners, so this will just increase the cash that the US is bleeding out overseas. This makes the fiscal deficit *and* the current-account deficit much worse.

How high are rates likely to go?

Many analysts are predicting rate increases of at least another **400** basis points. As the British newspaper *The Times* recently said, "US interest rates are now far below the appropriate level for this stage of the economic cycle and will need to rise much farther and faster than financial markets currently assume." *The Times* explained that the American economy is less sensitive to interest rates than the British economy, and since the Bank of England is aiming for a target of 5% to control British inflation, the Fed will have to raise rates even higher than *that* to control it here.

Normally, rising rates would strengthen the dollar. Higher interest rates make saving (rather than spending) more profitable; plus, borrowing (which is inflationary) becomes more expensive, so people borrow less. So usually we could look forward to the dollar firming as rates increased.

But not this time…

The US economy isn't ready for rising rates!

Corporate profits should be healthy before rates rise, since higher rates reduce them (by raising the costs of borrowing). But they're not—instead, profits are weakening, as we've seen.

The budget deficit should be low before rates rise, since higher rates will inflate it (by increasing the government's cost of debt). But it's not—instead, we're adding over a billion dollars *every day* to our national debt.

The current-accounts deficit should be small before rates rise, since higher rates will increase it (by encouraging other nations to accept and hold dollars, and making imports less expensive.) But it's not—instead, it's the highest it's ever been in history, with $1.6 billion gushing out of our country per day.

Rate hikes will be a disaster. All of these factors are completely the opposite from what they need to be before rates go up, yet Greenspan is raising rates anyway. As a result, businesses will tank, and the budget and current-account deficits will explode upwards from their already catastrophic levels.

But Greenspan doesn't have a choice—he *has* to raise rates. The collapse of Treasury bonds means that he's already way behind the rate curve—the market knows it, and he knows it.

At the same time, Greenspan knows that the economy wasn't (and isn't) ready for a tight rate policy. High rates will strangle the economy, and send it into a deflationary tailspin. That's why the Fed injected $4.5 billion into bank reserves (an inflationary activity) *on the same exact day* they raised rates. Greenspan is stomping on the brakes *and* the gas pedal at the same time, desperately hoping he can fool people long enough for the "recovery" to really start.

But it's hopeless. The dollar is in a trap from which there's no escape. Richard Russell, the legendary Wall Street analyst, recently said:

"It will require *massive inflation* to keep the US economy from sinking into recession and deflation."

He continued, "There's an irony in the current situation. The weaker the US economy, the more the need for the Fed to increase liquidity and the greater the need for the government to spend and run deficits—both processes calculated to ward off the forces of deflation.

"But the more the Fed inflates, and the larger the government deficits, the weaker the dollar. If the Fed and government are successful in warding off deflation, the dollar's fate is still in question. If deflation takes over, the international value of the dollar could cave in—since deflation would crush the US economy and turn foreigners bearish on the dollar."

He concluded:

"Either way, the dollar would be in danger. Which is one of the important reasons to hold gold."

Richard Russell is one of the most-respected analysts on Wall Street. And unlike most others, he deserves his outstanding reputation—he's been successfully calling market tops and bottoms since the late 1950's. Now, even this "conventional" analyst is recognizing that dollar-based investments are dangerous places for your money, and gold is where you should be.

Gold is up 60% in the last couple of years. So why do I, and Russell, and many others believe that it's still only at the beginning of a long bull market? Why does gold still have such a long way to go?

Gold is strongly countercyclical to the dollar. In other words, when the dollar goes down, gold goes up, and vice versa.

This means that usually, a period of rising interest rates wouldn't be a great time to invest in gold. A strengthening dollar would mean sub-par performance for gold.

But, as I've already explained, the dollar is trending downward, and boosting rates won't help. Not when we're fighting a long-term global war against terrorism, going a billion dollars further into debt each day, bleeding out our capital overseas, and fighting desperately with China and other wildly-growing nations for commodities and resources.

Plus, there's a more ominous angle to this. Greenspan is trying to (secretly) inflate the dollar at the same time he's boosting rates, and the last time we saw high inflation *and* high rates was the "stagflationary" 1970's. Our economy is looking more and more like stagflation every day: a stagnant/declining economy, sky-high oil prices, expensive commodities, a plummeting dollar, high inflation, and an expensive quagmire of a war.

Many remember the 1970's as a gut-wrenching time to be an investor. But I remember that gold's price multiplied by *more than 20 times* during that period! I think we have another great opportunity in gold today! As I've said before, I'm looking for at least $1,000 gold before this is all over.

So what's the best way to invest in gold?

First of all, DON'T fall for the seductive sales pitches you'll get from brokers about "leverage." They always forget to tell you that leverage works both ways—you can make more on the way up, but you'll get slaughtered on the way down.

Most people know enough to be wary when brokers pitch highly-leveraged gold "investments" like futures and futures options. The futures and options markets are dangerous even for highly sophisticated investors, and I recommend you stay out.

But other investments such as junior gold stocks sound much less risky. Yes, they're safer than futures (which isn't saying much), but you can still lose your shirt.

For example, gold hit $427 earlier this year. As I write this, it's at about 95% of that peak… but many gold juniors are down **50%** from their January highs!

It's heartbreaking when you correctly predict the direction of a market, and then watch your investments get stomped on because you chose the wrong vehicle. I'm not saying you should never buy a gold junior (I've recommended some in the past, and will do so again), but you need to be very cautious.

Plus, there are much safer ways to play the coming gold bull market, while still getting great leverage. My favorite way is…

Gold coins!

Gold coins are really two investments in one. First, you're buying the gold. Second, you can profit from the coin itself. I'll explain both parts separately.

Before 1933, when gold coins were in circulation, the dollar was pegged at $20.67 per ounce of gold. So a $20 gold coin contains almost a full ounce of gold—worth about $400 at today's prices. A $10 coin has about $200 worth of gold. A $5 coin, about $100.

You can buy bullion coins for pretty close to this inherent worth of the gold. (There's a small markup to pay for the minting of the coin and dealer costs.) And gold bullion is a great investment in times like these—I recommend you have some. Many people are happy to use bullion as their only investment vehicle for gold.

This 1926 Gem Uncirculated MS-66 $20 Saint Gaudens, graded and certified by PCGS, is not only a beautiful coin but also should be a great investment. Note the clear plastic "slab," and the PCGS label.

But others go one step further, and buy rare gold coins also. With these, you get an additional benefit. A good rare coin will be worth more than the gold it contains—for the best coins, **much** more. This additional value is called the *premium*, and it can be substantial.

Also, and most importantly, the premium can rise *far faster* than the underlying gold itself. When gold itself surges, good rare gold coins can explode. So this is your leverage—your investment can go up by multiples of what gold itself does.

Here's a specific example. I really like $20 gold coins dated from 1908-1928 (see picture). Specifically, I recommend MS66 PCGS- and NGC-graded coins (I'll explain what that means in a moment.)

I like them because they have explosive 4 to 1 leverage. With gold at $1,000 an ounce, I feel these $2,750 coins could be worth over $11,000 each. So a 150% spike in gold could net a 400% jump in value of these coins.

Now I'll explain the coin jargon, in case you're not familiar with it. Coins are graded for quality and appeal, and of course the most desirable coins have the highest premiums. (But, as I've already said, high premiums get even higher when gold itself rises. That means that the highest-graded coins should be stellar performers when gold soars.)

There are many companies and dealers who grade coins. BUT—I'd advise you to run away from almost all of them, and DON'T buy coins they've "graded." Many of these people are incompetent—or unethical—and will "grade" your coins at much higher than their true value.

You should only trust PCGS (Professional Coin Grading Service) or NGC (Numismatic Guaranty Corporation) graded coins. These companies are the industry standard, and are universally trusted by dealers. The picture shows a PCGS-graded coin: note that it comes in a plastic "slab" that's clearly marked "PCGS." NGC slabs look very similar.

Also, I said to look for coins graded as "MS66." The "MS" means "Mint State"—a coin that's never been circulated, and has excellent eye-appeal. The "66" refers to a numerical rank on the scale of 1 to 70. A coin graded as a "1" is little more than an ugly disk of metal, while a "70" is essentially perfect. As you can guess, the higher the number, the (much) higher the price. MS66 is high enough for great price appreciation, but is still relatively affordable.

If you have any questions about coins, I recommend Chuck Aultman of Finest Known. You can reach him at 1-866-697-GOLD (4653).

I'm out of room for this issue. For more recommendations on gold, see my book, *The New Bull Market In Gold: $1,000 Gold and How to Profit From It!*