GOLD & ENERGY ADVISOR

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James DiGeorgia, Editor

"Gold Bursts Up Through $500, as Russia Declares It Will Start Hoarding Gold!"

"Supply is plunging, demand is screaming. And the yellow metal just hit a 25-year high.

"But this rip-roaring bull market is just beginning!"

- **Fed announces plan to cover up its coming inflation of the dollar!**
- **Massive gold scandal brewing among central banks?**
- **The best ways to invest**

No doubt you've seen what gold is doing lately. But now it's hitting the "wall of worry." People are wondering: surely it's gone too far? Will it come down just as fast as it went up?

Nonsense! There will be short-term corrections, of course. Any bull market has them. But the bull market itself is gaining strength, instead of losing it. I predict we'll see $1,000 gold before it's through!

Here's an interview I just gave on this very subject. It did a good job of summing up our situation, so I've included it for this month's issue.

Enjoy!

James DiGeorgia on the New Bull Market in Gold

Q: James, we've just seen gold break through the $500 barrier. It's doubled since 2001. Do you think the gold bull has run its course?

Not at all. There are several forces pushing gold up, and those forces will be operating for several more years, at least.

Q: What forces are those?

It all comes down to fundamentals: supply and demand. Gold's supply has been falling, and demand has been accelerating. And neither trend has shown any sign of cooling off. Instead, both trends are gathering steam.

Plus, there's a political aspect to gold as well. Gold is unique: it's a financial asset that's valued all over the globe, but it's not the liability of anybody else. Unlike a stock, its value isn't dependent on the performance of a company. Unlike a bond, it doesn't rely on the performance and creditworthiness of the issuer. Unlike a currency, it doesn't depend on the fiscal prudence of a government (which is always a bad bet anyway).

In fact, when stock markets get overvalued, or governments go on massive spending binges, or bubbles form in real estate or other places, that's when gold flourishes. Investors flee to safety, and run to gold. That's why gold is doing really well, and will go up from here.

THE GOLD AND ENERGY ADVISOR

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Q: OK, you raised a lot of points there. Let's take them one at a time, starting with supply.

Gold mines are really hurting, and the supply of gold coming onto the market has fallen sharply. This surprises a lot of people—it seems mining companies would be raking it in right now, with the price of their product hitting 25-year highs. But that's not the case.

South Africa is the largest gold-producing country in the world. For 2005, its gold output is anticipated to be the lowest level in 80 years. Total output has fallen by 30 percent just in the last five years.

Mines there are getting clobbered by higher operating costs: fuel, steel, and labor. Plus, the South African currency (the rand) doubled against the dollar a few years ago. Since gold is priced in dollars, that slashed the rand price of gold in half. So the mines have received less rand for their gold, despite gold's higher price.

Note that some of the world's biggest gold producers are in South Africa: Anglogold Ashanti (the second biggest), Gold Fields (the fourth biggest), and Harmony (the sixth biggest). They've gotten hammered by all this.

But South Africa isn't the only country experiencing problems. Across the industry, mining costs are up about 30 percent over the last five years. For example, Newmont is the world's largest producer, and isn't much affected by problems in South Africa. But Newmont just announced its third-quarter profit fell 2.3 percent, as output dropped 6.8 percent.

All this is no surprise to those of us who follow the gold industry. A few years ago, when everybody wanted Internet stocks and nobody wanted gold, the metal's price plunged. Many mines went bankrupt, and those that survived had no money to explore for gold, or to develop any finds they had. So they "high-graded": they lived off their existing high-grade ore, without spending any money to develop their lower-grade resources, or search for new deposits.

Now they're paying the price. The cheap, easy-to-mine gold is gone, and the leftovers are low-grade and expensive to work. So mining companies are desperately looking for new reserves—but it takes years to find, confirm, and develop new deposits.

Last year, worldwide gold production had the largest decline in 39 years. We're headed for

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another steep decline this year, and probably for several years into the future.

Q: So supply is a very bullish factor. But what about demand?

This is the really exciting part. Just as supply is sagging, demand is exploding all over the globe—not only from investors, but also *governments*. This is something we’ve really never seen before, and the implications are just staggering.

According to the World Gold Council, gold jewelry demand is up 12 percent year-on-year by weight, and 20 percent when measured by dollar-value. Investment demand shot up by 56 percent in the third quarter. The total gold demand is up 7 percent by weight, and 18 percent in dollar terms.

That makes seven consecutive quarters of growth in demand by weight. Even more amazing, we’ve now seen ten consecutive quarters of double-digit growth by dollar volume.

The demand is coming from everywhere. For example, India and China together have one-third of the world’s population, and these people have historically loved gold. I’ve told my readers how demand in those countries has skyrocketed. In the first half of 2005, Indian demand shot up 55 percent in 12 months. And it’s up 14 percent in China, the world’s largest and fastest growing economy.

Buyers are snapping up the metal in the Middle East too. Dubai just opened its Gold and Commodities Exchange, a brand-new international gold futures market. Plus, the high price of oil has generated billions in petro-profits, and a lot of that money is going into gold.

According to the *Financial Review*, a lot of Middle East investors are growing afraid of U.S. stock and bond investments: they don’t like the Patriot Act limitations on foreign banking activity, they’re worried about the U.S. government freezing their accounts, and they don’t want to appear pro-American to radical neighbors at home. Gold is an excellent alternative.

But as if all that wasn’t enough, this month we saw something completely unprecedented: announcements from several major governments that they will be selling some of their currency reserves (which are mostly dollars), and buying gold!

For decades, world governments and central banks have been united in their war against gold. They’ve been selling it, or threatening to sell it, since the 1960s. But now they’re buying instead!

For example, on November 15, a Russian official announced Russia will double its percentage of gold reserves, from 5 percent to 10 percent. Not only that, the government made a point of emphasizing its plans. On November 24, Alexei Ulyukayev (the First Deputy Chairman of the Central Bank), said Russia will buy gold “on all markets on which it is available.” Then Vladimir Putin, the Russian President, said, “I think that the Central Bank should pay more attention to precious metals… Let’s not be too restrained here.”

Russia is talking about buying another 646 tonnes of gold. That’s double the annual gold output of all of South Africa!

And Russia isn’t the only one. Argentina and South Africa also announced their intentions to add to their reserves. And then we saw something even more momentous…

Kenneth Rogoff, the former chief economist at the International Monetary Fund, said that Asian central banks should sell their dollars and diversify into gold. Why? He said there’s a greater chance of “serious global recession and a higher probability of a nuclear attack on a U.S. city in the next seven years.”

This recommendation was breathtaking. First of all, the IMF has been anti-gold since the dollar came off the gold standard in the 1970s. What’s a former IMF official doing recommending gold? (And notice his comment about a possible attack—I’ve been warning my readers about this.)

Asian interest in gold was confirmed by an article in China’s *People’s Daily*. It said, “Central banks of Asian countries, including China, are

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Latest prices as GEA goes to press—December 7, 2005

Comex spot contract: silver $8.90, gold $519.00
Nymex spot platinum: $998.00, palladium $279.00
Nymex Light Sweet Crude Oil $60.60

Silver coins		Dealer will buy at this price	Dealer will sell at this price
100 1 oz. silver American Eagles		$925	$1,100
100 1 oz. common rounds		$890	$1,100
$1,000 face value US pre-1965 coin bag (circulated)		$5,750	$6,950
$1,000 face value US circulated silver dollar bag (VG or better)		$9,000	$10,000
US Morgan silver dollars	PCGS MS64	$45	$65
	PCGS MS65	$110	$140
	PCGS MS66	$280	$375
Platinum coins			
U.S. Platinum Eagle:	1 oz.	$1,000	$1,275
	1/2 oz.	$500	$695
	1/4 oz.	$275	$450
	1/10 oz.	$110	$175
Gold coins			
Australian Kangaroo		$519	$595
British sovereign (Kings)		$110	$160
(Elizabeths)		$110	$160
Canadian Maple Leaf		$519	$550
Credit Suisse 1 oz. gold bar		$519	$550
Mexican 50 peso Centenario		$575	$675
South African Krugerrand		$519	$550
US Gold Eagle:	1 oz.	$525	$585
	1/2 oz.	$275	$375
	1/4 oz.	$125	$200
	1/10 oz.	$65	$95
US $20 double eagle:			
Liberty	Raw MS60	$550	$675
	NGC MS63	$775	$950
	NGC MS64	$1,200	$1,950
	NGC MS65	$4,150	$5,950
Saint Gaudens	Raw MS60	$575	$700
	NGC MS63	$625	$795
	NGC MS64	$700	$875
	NGC MS65	$1,250	$1,495

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

expected to further increase their gold reserves… Russia, Argentina, and South Africa have decided this month to increase their gold reserves, which reverses the selling trend by world central banks… It is only a question of time for Asian central banks to follow and buy gold: they hold $2.6 trillion U.S. dollars in foreign exchange reserves, and are able to change more of them into gold as a hedge against US dollar falls.

"The U.S. dollar will inevitably slip further. Some budget deficits of the seven major industrial countries are at a record level, and central banks are "printing banknotes" to devalue their currencies."

The article also pointed out that Asian investors are the world's largest gold consumers, but Asian central banks hold little gold. China's official reserves are only 1.1 percent gold, Japan has only 1.3 percent, and India 3.6 percent. Now compare this to the Eurosystem's 50 percent gold reserves, or America's 63.8 percent! Even a small move into gold by China, Japan, or India will create a huge demand spike.

Q: Why all the sudden interest from central banks? Why the sudden change from gold bears to gold bulls?

There are a couple of reasons for this. Foremost is that their primary reserve is the U.S. dollar, and the greenback is about to be inflated into toilet paper. (I'll explain more about this in a moment.) So foreign central banks are understandably concerned about keeping their savings in a depreciating currency.

As Tito Mboweni, South Africa's central bank governor, said, "Gold is no one's liability and it allows prudent diversification in the bank's total reserves." Translation: he wants to dump his dollars and buy gold because he's afraid of what Uncle Sam will do to his dollars.

Mr. Mboweni was being polite. Others have been more open. Last year, there was a speech by Oleg Mozhaiskov, deputy chairman of the Bank of Russia. He blasted "the blatant lack of discipline of United States fiscal policy" and "the irresponsibility of the U.S. government."

He also said, "The world has come to a paradoxical situation in which the creditor countries are more concerned with the fate of the dollar than the U.S. authorities themselves are...The number of people who have held assets in dollars and now wish to diversify them partly into gold—the traditional shelter from inflation and political adversity—is steadily growing."

So more and more, foreigners are unwilling to hold dollars as reserves. But there's another reason too.

For many years, central banks actively worked to suppress the price of gold. As currencies (especially the U.S. dollar) depreciate, the price of gold goes up. This makes central banks look really bad, especially the Federal Reserve, since the Fed's job is to maintain the stability of the dollar. So the Fed has pressured central banks around the world to suppress the price of gold.

This was done by loaning gold to "bullion banks," which sold the gold into the market. These sales depressed the price of gold. This is basically price-fixing, and its legality was highly questionable, but a few years ago Greenspan admitted this was being done.

But those loans have to be paid back eventually. And the bullion banks don't have the gold anymore—they sold it, remember? So they have to buy back gold on the market in order to repay the loans.

But prices have soared since then, making it much more expensive to buy the gold back. And rumors are swirling that some of the bullion banks are in serious trouble. For example, European financial powerhouse Deutsche Bank has been a huge global player in gold derivatives. But according to reports, the Bank has been trying to unilaterally change the terms of its derivatives contracts from "per ounce" to "per tenth ounce"—not just new contracts, but also existing ones! They have to be really desperate to pull a stunt like this.

If the bullion banks default on their loans, then the central banks don't get their gold back. But here's the problem: many of these loans were done "off the books." The central banks still list this gold as an asset. Officially, the metal is still sitting in their vaults. (Actually, in some cases it *is* still sitting there, but it's been sold to other owners.) If one or more bullion banks default, the world is going to learn there's a lot less gold in the vaults than the governments are claiming.

We've seen defaults on a small scale before. One of the more notable was when Portugal lent 17 tonnes of gold to Drexel Burnham Lambert in 1989, which went bankrupt a few days later. Portugal lost all that gold.

But this is on a much larger scale. For example, Russia has about 500 tonnes of gold in its reserves. It's categorized as monetary gold (coins in the vault), allocated gold (gold bars stored in the vault), and term deposits (deposited with banks to earn interest). The "term deposits" is what we're talking about: gold lent out to bullion banks, who sold it into the market.

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Russia's term deposits are worth \$6 billion. Do the math, and that's about 373 metric tons of gold. But 373 divided by 500 means Russia has lent out about 75 percent of its gold. No wonder they want to beef up their gold reserves now—three-fourths of what they had is gone!

And that's just one government, among many involved in this scheme. We're talking about major amounts of gold, involving almost all the Western governments, and a massive cover-up that's starting to unravel. If the reports are right, we're going to see the mother of all stampedes into gold.

Q: This all sounds like huge support for a continuing bull market in gold. Are there any signs of broader interest in gold as an investment?

Yes, signs are everywhere. Last month, a Swiss banker at the annual London Bullion Market Association conference said, "I am getting calls from people I haven't spoken to in 15 years, asking me about gold."

In fact, all commodities are in a rip-roaring bull market, not just gold. The Goldman Sachs Commodity Index is up 292 percent since 1999.

And this might just be the first stage of a long, wild ride. Reuters just reported that pension funds in the United Kingdom are now considering investing in commodities. They're currently invested about 60/40 in equities/bonds, but they're thinking about switching 3-5 percent of their funds into commodities. These funds manage about 800 billion pounds—that's about \$1.38 *trillion* dollars. And if the British funds are thinking about it, it's a safe bet there are some American funds considering it too.

If these funds move even a tiny percentage of their capital into gold, we'll see a series of limit-up days on the market. People don't realize how small the gold market is, compared to the other markets.

New Recommendations and Portfolio Update

Since last issue, we've mostly modified our hedges as the markets have shifted.

Remember, this is only a summary of what we've already done. By the time you read this, the prices (and probably, the entire opportunities) will have changed. If you're not getting the recommendations immediately as I issue them, log into www.goldandenergyadvisor.com and make sure we have your current email address.

As we anticipated last month, the fall (and then rebound) of the energy market gave us the change to play some hedges. Here are the recommendations I've made since the last issue:

- Our Pioneer (PXD) options expired and were exercised. We made 6.6 percent in about two months.
- ConocoPhillips (COP). We bought back the December 65 calls (COPLM), and sold the January 65 calls (COPAM). Our credit was $130 for each contract, and we made $210 on the buy back.
- Cimarex (XEC). We bought and closed our December 40 calls (XECLH), and sold the January 50 calls (XECAH). Our credit was $90 per contract, and we made $135 on the buy back.
- Apache (APA). Our November 65 calls (APAKM) were expiring: we bought them back, and sold new December 65 calls (APALM). Our net credit per contract was $190, while the buy back was essentially a wash.
- Talisman (TLM). We bought and closed our December 50 calls (TLMLJ), and simultaneously sold new January 50 calls (TLMAJ). Our credit was $140 for each contract, and we made $40 on the buy back.
- We sold part of our XLE hedge (XBTXX) position when energy rallied. We took a loss on these, but these were only meant to protect our profits in our other energy stocks.
- We reviewed our natural gas stocks: Newfield Exploration (NFX), Bill Barrett (BBG), and Burlington Resources (BR). For subscribers who didn't get in when we first recommended them, I recommended getting aboard at these price points: NFX at $42, BBG at $34.25, and BR at $66.

You could buy *every single ounce* of gold mined last year with just 23 percent of IBM's market capitalization—that's less than one-fourth of the stock of just one company.

Trillions of dollars slosh around the world's markets every single day. If even a tiny fraction of those dollars are diverted into gold, we'll see a mania that most of us can't even imagine.

Q: Even though gold just reached a 25-year high? It can go that much higher?

Gold's historical high was reached back in 1980, when it hit $850 an ounce. Adjusting for inflation, that's equal to $2054.85 today. Gold is still cheap from that perspective!

Q: Especially when you look at the alternatives. Dollar-based assets seem ready to go into the toilet.

Yes, that's true. Our national debt just exceeded $8 trillion for the first time ever. That's $27,392 for every man, woman, and child in this country—including you and me, and each member of our families.

And that's the outrageous thing about all this—you and I *will* be the ones paying it all back.

People usually pay no attention to the debt, because the government owes it, not the people. But where will the government get the money to pay the debt back? From taxes. Where do taxes come from? The people!

So if you have a family of four, you already owe over $100,000. You're going to have to pay it sooner or later. And you owe more and more every single month!

It took our country 220 years to rack up a $5 trillion debt. Six years later, in 2002, we added another trillion. Then it took only two years for the next trillion, in early 2004. Now this past October, we breached the $8 trillion mark.

That's $8,000,000,000,000: a number too big to even understand. Think of it this way: it's a stack of $1,000 bills that's 543 miles high!

This time next year, it will be $9 trillion, if the current spending is any clue. Since the fiscal year began, we're racking up additional debt at an annual rate of $1.05 trillion—a staggering figure. You and each member of your family will owe an additional $3,547 per person by the end of the year—bringing you up to almost $31,000 apiece.

This insanity has to stop, but it's accelerating instead. Washington is throwing the wildest spending orgy ever seen in history.

We're headed for a catastrophe, but the

politicians are covering it all up. You might have heard about Laurence Kotlikoff, the economics chairman at Boston University. He's created a ground-breaking method to calculate long-term costs of current obligations. Based on his work, two economists were hired by the Bush Administration to calculate the long-term financial prospects of Social Security and Medicare.

Their report showed that as the Baby Boomers start to retire, we're facing a $44.2 trillion deficit. That's about $150,000 *per person* in this country. But rather than deal with the facts, the report was thrown away (and the man who commissioned the report, Treasury Secretary O'Neill, was fired).

Kotlikoff has pointed out that our current situation can't go on: our economy is going to implode, and there probably will be little warning. He said, "The country's absolutely broke…This administration and previous administrations have set us up for a major financial crisis on the order of what Argentina experienced a couple of years ago…If you look at financial crises, they occur seemingly overnight. More and more pieces of straw drop on the camel's back, and all of a sudden the camel collapses. Nobody knew exactly what day Argentina was going to go south or exactly what day Russia was going to default. The timing is up for grabs."

Leonard Burman, the co-director of the Tax Policy Center, was just quoted by the media on this. He said, "The long-term budget projections are just horrifying. I've got four children and it really disturbs me. I just think it's irresponsible what we're doing to them."

By the way, the Baby Boomer report was done a few years ago. The situation is actually far worse now, with our deficits skyrocketing since then. For example, President Bush signed a new Medicare drug coverage bill in 2003. Its price tag was a whopping $400 billion over 10 years. But even that number was too small: the true cost has now ballooned up to $720 billion. And that's just one spending bill out of countless thousands: it doesn't even include the "bridges to nowhere" and other nonsense that Congress has passed lately.

The only thing keeping us afloat is consumer spending, and that can't last forever. In just the last two months, Americans have spent $132.4 billion more than we earned. Most of that has been financed from the real estate bubble: Americans pulled $600 billion out of their homes last year. People are using their homes like giant ATM machines.

But interest rates are rising, and the real estate bubble is cooling off. The party will be over soon, and then the bills will come due.

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No wonder that the media are running articles like the one in *USA Today* that said, "A fiscal hurricane is on the horizon." The paper interviewed David Walker, head of the Government Accountability Office and Comptroller General of the United States. He said, "We face a demographic tsunami that will never recede."

The article said the U.S. is like Rome before the fall of the Empire. Walker said, "Our business model is broken." Douglas Holtz-Eakin, director of the non-partisan Congressional Budget Office, said he was "terrified" about the budget deficit in coming years.

The article didn't even mention the final nail in the coffin—Alan Greenspan is retiring as head of the Federal Reserve, leaving a terrible mess behind. But will his replacement be a fiscal conservative, somebody who'll clean this mess up? Nope—instead, we're getting "Helicopter Ben" Bernanke, the guy who said we can solve our economic problems by printing up lots of money and throwing it all out of a helicopter.

And to prepare for its new Chairman, the Fed just announced it will no longer report the M3 Money Supply figure. M3 is the broadest measure of money supply. Why do you suppose the Fed doesn't want to reveal this number anymore?

Because it shows the true hypocrisy of the Fed. Greenspan and his cohorts jawbone about "fighting inflation," at the same time they're flooding our economy with dollars! In 2003, money supply growth was 3.4 percent. In 2004, it was up 6.4 percent. In the first 10 months of 2005, up 6.42 percent—more than the entire previous year. Of course, money supply inflation leads to price inflation…the exact thing the Fed says it's "fighting."

But instead of fixing the problem or stopping the hypocrisy, the Fed has decided to just cover it all up. So in a few months, there'll be no more M3 numbers. Apparently the Fed doesn't want anybody to see what Helicopter Ben is going to do.

The government already under-reports inflation—the CPI and other statistics are heavily "massaged" to cover up the truth. But now we're apparently gearing up for some serious money-printing…and serious inflation, maybe even to banana-republic levels.

No wonder investors are stampeding into gold!

Q: James, what gold investments do you like right now? Assuming gold rises to $1,000 as you predict, where does an investor get the greatest appreciation?

I'm going to be very choosy about gold stocks at the current $514-$516 level. I may be making specific buy recommendations sometime during January or early February.

Right now, even though I'm crazy about gold and its chances to jump to over $1,000, I'm also bullish on certain energy stocks. My *Gold & Energy Advisor* Portfolio currently includes three natural gas stocks: Newfield Exploration (NFX), Burlington Resources (BR), and Bill Barrett Corp (BBG). (I just sent an Update to my readers about these stocks, with recommended entry points for people who didn't get in when I first recommended them.) If we get a cold winter—and it's starting to look very frigid in the north—we'll see a 10 percent, 20 percent, even 25 percent jump in these equities in 30 to 90 days.

I'll use the profits I generate from these gas plays to load up on a select group of gold stocks. I'm expecting a pullback to under $500 early next year, and that's when I'll buy. That's my plan.

Q: But what can our subscribers buy now if they believe like you that gold is heading to $1,000 an ounce?

I hope my subscribers are profiting on my gas and oil recommendations. While they wait for the gold, silver and even platinum stocks I intend to recommend, they would best be served by doing what I've been doing since 1999….buying really rare and high quality U.S. gold coins.

I always buy coins certified by one of the two top independent grading services (PCGS and NGC). In fact, I discuss them in my book, *The New Bull Market In Gold,* along with my reasons to invest in these gold coins and what gold coins to buy. I cover the dynamics of the rare coins market and explain it's a very liquid market.

Just a few years ago I was buying Gem Uncirculated MS65 $2.50 Indian Gold coins struck from 1908 through 1926 for less than $2,000 each, graded and certified by PCGS or NGC. Today, these same coins sell for $7,000 each. In two instances I bought $2.50 Indians for $2,000 that now trade wholesale for $11,000-$13,000!

Last year, I bought an MS66 1878 $3 gold coin for $14,000 that you couldn't replace today for $26,000. And the rare coin market is only starting to get hot! More and more gold bugs are going to be created and made into believers as gold rises in the next few years. A $3 Gold in MS66 condition could soar to $75,000, even $100,000.

Higher gold prices are like fuel to a fire!

Universal Gold and Bullion is run by a close friend of mine—Mike Fulgenz. He's received every possible industry accolade. I recommend talking to him and his staff about U.S. gold coins: (800) 459–2646.

They'll load you up on books that Mike has written that will help you understand just how important (and easy) it is to buy QUALITY and RARITY. Once you understand how it works, and that you should only buy NGC and PCGS graded coins—you're set to make some serious money as gold rises to $1,000.

I've personally been buying and accumulating Indian $10 U.S. gold coins from 1907-1930S. (The Gem 1933 is a great coin, but it's expensive. I avoid the 1932—it's too common, especially in MS66 or better condition.) Stick with the rest of the series in MS64-MS68 condition and you should score big.

I also love rare dated gold with low populations, i.e. VERY, VERY, RARE. A good example of a rarity is an 1850 $2.50 Gold Liberty in Gem Uncirculated MS67 condition. Besides being rare overall, there are only 3 of these coins graded in this condition.

It would sell for $45,000 now but I think it could jump to $225,000 if gold hits $1,000. Don't be afraid of buying U.S. Proof gold or rare dated $20 Liberty gold coins either. In this bullish gold market, good coins will jump 300 percent to 1000 percent while gold only doubles.

Last year I was recommending 1925 and 1926 $20 Saint Gaudens in Gem Uncirculated condition and selling them for $2500. They're now selling for over $3,000—up 20 percent already, and as I explained in my book, I think they'll hit $11,000.

Q: James, thanks for a great interview.

It's my pleasure.