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The Next Major Rise in Gold Has Begun!

By Patrick Heller
Liberty's Outlook

In my judgment, there are several pressures building up that will result in the price of gold rising above $1,000 to stay and probably reach at least $1,200 in the near future.

How soon? I think this will most likely happen between the last week in August and the end of September.

The groundwork for this price breakout has already been laid. Some smart buyers have already pushed up the price of gold. That means that the next major rise in the price of gold has already begun.

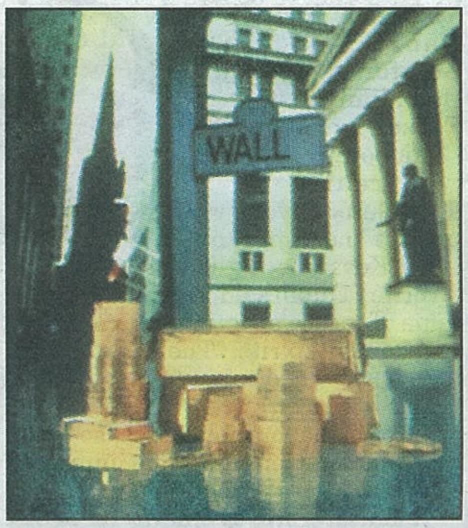
To make near term specific forecasts is treacherous. It is much safer to make vague long term prognoses.

Still, the accumulating signs mostly point to a higher gold price within two months. Let me share with you some of the factors supporting my prediction.

Factors Pushing Gold Prices Higher

Commercial Real Estate Mortgage Crunch: On July 7, Rep. Carolyn Maloney (D-NY), who is chair of the Joint Economic Committee, told the members of this committee that the $3.5 trillion of commercial real estate debt is a "time bomb" and a "looming crisis" as $700 billion of these mortgages must be refinanced by the end of 2009. She said this could spark a second wave of huge losses at large US banks.

Any further weakness anywhere in



the real estate market would add to doubts about the strength of the US dollar. If the forthcoming news is so terrible that politicians in Washington are using drastic terms such as by Rep. Maloney, you know things are much worse than the government is letting on.

"Panic" in Washington and London: Actually, I have heard multiple stories that politicians in the US and England are terrified at the prospect of so much horrible economic news coming soon. Among their reasons for alarm, beyond the issues I discuss here, are expected soaring default rates on credit card debt and rising default in prime quality residential real estate mortgages.

COMEX Now Allows Gold Contracts To Be Settled With Shares Of GLD Exchange Traded Fund: Adrian Douglas, a commodity analyst who also is a member of the board of directors of the Gold Anti-Trust Action Committee (GATA) published an analysis on July 11 revealing his discovery why COMEX gold market reports on trading activity and the movement of metals were not making sense.

In the past, COMEX contracts were settled by the delivery of the commodity. If that were not possible, then they were supposed to be settled for cash. However, the COMEX now says that a gold contract can now be settled by "substantially the economic equivalent" of gold. What has in fact happened is that shares of the GLD gold exchange traded fund have been used to fulfill commodity contracts.

In theory, these shares represent 1/10 oz of physical gold. However, there are many loopholes in the ETF contracts that allow the fund to effectively hold paper contracts rather than physical gold. As a result, there is doubt that the ETF could deliver gold to redeem outstanding shares.

Within eight months after GLD began operations in February 2005, the price of gold rose more than 50%. Like the opening of GLD, which made it much more convenient for investors to put money into the gold market, Douglas's analysis could be the one single event that sparks the next major rise in the price of gold.

By the way, COMEX silver contracts cannot yet be settled with shares of silver ETFs.

Investment Funds Dumping GLD, At Least Some Replacing With Physical Gold: The timing is so coincidental that there is a good likelihood that Douglas's analysis has resulted in multiple investment funds liquidating their positions in GLD.

On July 14, Greenlight Capital, a hedge fund that had been the largest investor in GLD, announced that it had liquidated its entire holding of 4.2 million shares of GLD (effectively about 420,000 ounces of gold worth almost $400 million) and replaced it with physical gold. The company declined to detail the nature of the physical gold it received, but it may have come directly from GLD to redeem the shares.

For a fund to take such an extreme step would almost certainly encourage other funds with GLD investments to closely scrutinize their holding. Since the Greenlight announcement, at least seven other funds have completely liquidated the GLD investment, though I have not been able to learn if they replaced the position with physical gold.

Federal Reserve Chair Bernanke Contradicts Himself About Inflation: When Bernanke was

Continued on page 18

The Next Major Rise in Gold Has Begun!

Continued from page 1

testifying to Congress on July 21, Rep. Ron Paul (R-TX), the sponsor of the "audit the Fed" legislation pending in Congress, asked some tough questions. In response to one, Bernanke said, "At some point as you know, we are going to have to start raising interest rates to avoid inflation." This contradicted Bernanke's claims that inflation is under control.

Inflation is the increase in the money supply. The outcome of inflation is normally an increase in prices, which many people confuse as representing inflation.

Just to make sure you grasp that concept, let me say it differently. Rising prices are not themselves inflation. Rater, they are the effect of inflation that has occurred.

The US government has increased the money supply by such a huge percentage in the past two years, that inflation is rampant. The effects of it have been dampened as the private sector cut back on consumption.

If there is any recovery in private consumption, the effects of the existing high levels of inflation will severely knock down the value of the dollar. Beyond the short term, the only way the US government can prevent the effects of high inflation is to sharply reduce the money supply and the federal budget – probably on the order of at least 50%! I just don't see this happening.

It has been amazing to me to see so many people fooled into thinking that inflation is under control, even as it has been locked into the economy since the summer of 2007. Maybe Bernanke's "confession" will get some people to wake up.

China Explicitly States It Is *Buying Natural And Energy* Resources: On July 20, Chinese premier Wen Jiabao publicly stated that his government would use its foreign exchange reserves to support and accelerate overseas expansion and acquisitions by Chinese companies. He said, "We should hasten the implementation of our 'going out' strategy and combine the utilization of foreign exchange reserves with the 'going out' of our enterprises."

About then, Chen Yuan, the chairman of China Development Bank, said, "I think we should not go to America's Wall Street, but should look more to places with natural and energy resources."

I reported this in the June 3, 2009 issue of *Liberty's Outlook*. Now the general public has learned that the Chinese government is mobilizing its foreign exchange reserves, including US Treasury Debt, to buy commodities like gold and oil.

US Government's Massive Debt Increases: Recently, the US Treasury was trying to sell more than $200 billion of debt. To hide the fact that foreign buyers have become less willing to purchase such debt, the US government changed the way that it reports who is purchasing such debt.

In the past, "indirect purchases" were used as an indicator of foreign demand. As I now understand it, if the Federal Reserve buys US Treasury debt because there are no other buyers, these are also being reported as indirect purchases. The first debt sale in late July reported that 68% of it went to indirect purchases, which was an incredibly high percentage. I think this probably indicates that the sale basically failed and the Fed had to bail it out.

First, the fact that the US government has to issue additional debt is bad news for the economy in the long run. Second, if demand for US government debt is so poor that the Federal Reserve has to buy it, it is really just

an act of creating money out of thin air (and also higher inflation).

No matter what word games are used, the growing US government debt will push prices and interest rates higher in the future as the value of the dollar falls.

US Government Shenanigans To Hide Bad News From The Public: Rep. Ron Paul sponsored HR1207, legislation in the House of Representatives calling for the Government Accountability Office (GAO) to audit the Federal Reserve. This bill now has 279 co-sponsors, over 64% of the entire House. Sen. Bernie Sanders (I-VT) sponsored the companion bill S604, which has 20 co-sponsors. On July 8, Sen. Jim DeMint (R-SC) saw that several amendments were being added to an appropriations bill. Many of these amendments were authorizations for the GAO to perform audits. So DeMint offered his own amendment to add S604 to this bill.

When this was done, Sen. Ben Nelson (DNE) objected that this violated Rule 16, which prohibits legislative amendments to appropriations bills. The Senate president agreed and dropped this amendment.

DeMint persisted. He pointed out that the Senate regularly violates its own rules. He listed each other GAO audit amendment on this appropriations bill. While the Senate president agreed that each of these violated Senate rules, he left them attached to the appropriations bill.

It is obvious that the Democratic leadership in Congress and the White House do not want the public to know what an audit of the Federal Reserve would reveal. One likely revelation would be just how much gold the US government still has in custody and how much it actually owns.

Both Bernanke and Fed vice chair Donald Kohn testified before Congress that passage of this legislation would create dire consequences. In particular, they said that if the public knew what the Fed was doing, that it would result in higher consumer prices and interest rates and that the US government's credit rating would decline.

No member of Congress asked either gentleman why the Fed was taking actions that would hurt the US economy (but only if the public knew about it). To my mind, it is an example of the US government trying to hide the truth from the public.

This is not an isolated example. On July 20, President Obama and Treasury Secretary Geithner announced that they would delay the US 2009 budget review by one month. If this review would produce good news, you can bet that there would be no delay in releasing it. I think it is safe to assume that this step really is just another attempt to push back disclosing more bad news.

At the conclusion of the meeting with Chinese officials today, Geithner announced that Americans will have to learn to live within their means. Translation: the Chinese were unwilling to bend over further to bail out the US government.

Mysterious Gold Deposited Into COMEX: On July 23, the COMEX reported the addition of 215,085 ounces of gold deposited in dealer, or registered, inventories. This follows months when dealer inventories were virtually unchanged. It was also one of the largest single day deposits in COMEX history.

Such an event is rarely by chance. My best guess is that "someone" knows that there is going to be a near-term significant withdrawal of gold from the COMEX. Should it come to pass, you can almost guarantee a quick rise in gold prices.

Soaring US Bank Failures: From 2005 through 2007, only three US banks failed over all three years combined. In 2008 alone, there were 25 bank failures. So far in 2009, there have been 64 bank failures.

Sheila Bair, head of the Federal Deposit Insurance Corporation (FDIC) predicts that there will be another 500 bank failures. Since she has consistently understated how bad the banks were doing, I doubt that she has now overstated the problem.

When banks fail, the FDIC bails out depositors to the limit of FDIC coverage. The FDIC has paid out so much in 2008 and so far in 2009, that it was almost certain to exhaust its assets by the end of September.

News that the FDIC is running out of assets would just about guarantee a major bank run, so I have no doubt that the US government (i.e. taxpayers) would supply whatever was needed to prevent that. However, just the news of the FDIC running out of funds could panic the public anyhow.

Inaccurate Bank Earnings Reports: In an effort to try to make the news appear better than it really is, banks are getting quite creative at reporting earnings.

Citigroup, for instance, had an operating loss of $2.4 billion for the quarter but managed to report a profit of $4.3 billion after including the one-time profit from the sale of its Smith Barney unit.

Bank of America reported profits of $2.42 billion, which included a $5+ billion one-time profit from the sale of most of its shares of China Construction Bank.

On the same day these earnings were reported, Bank of America CEO Ken Lewis said, "Difficult challenges lie ahead from continued weakness in the global economy, rising unemployment and deteriorating credit quality that will affect our performance for the rest of the year and into 2010." Despite the seeming good news from the banking industry (and most other large banks reported similar better-than-expected news), I think Lewis's comment gives a better picture of what is really happening.

HSBC Discontinues Precious Metals Storage: In July, HSBC, a bank with one of the largest depositories of precious metals in the US, notified its customers for whom it is providing custodial services that it is getting out of that business. The bank told its customers to quickly remove their holdings or to sell them.

There may be two factors involved with this abrupt change. Other specialists in precious metals storage have long suspected that HSBC's rates were too low to cover costs. If that were the only factor, the bank could simply have raised its rates.

However, it is entirely possible that this move was an attempt to force significant liquidation of physical precious metals by customers who don't want the hassle of taking possession or making alternative, more-expensive, storage arrangements. If this move is really an attempt to help suppress precious metals prices, it would be a sign of extreme desperation by the US government and its trading partners (including HSBC).

Goldman Sachs Reports Theft Of Market- Manipulating Software: In early July, Goldman Sachs reported the theft of one of the company's proprietary trading programs, allegedly taken by one of the employees who helped create it. In reporting the theft, Goldman Sachs said that usage of this program could make it possible for the user to manipulate markets unfairly.

Why would Goldman Sachs create such software unless there was some plan to use it? There is a lot more to this story than has been revealed. Whatever is the whole truth, I doubt it will be pretty.

European Central Bank Reports No Gold Sales For Past Two Weeks: Every week, the European Central Bank reports on gold activity by itself and by most European central banks. For almost the entire 10 years of the Central Bank Gold Agreement, the largest part of central bank gold sales came from these banks. In the last two July weekly reports, none of these banks reported selling any gold, perhaps the first time in the past decade when this happened. There are actually reports of several central banks actively building gold reserves, which would negate the declining official sales. If this drop in gold supplies continues, there will be larger shortages.

What Does This All Mean?

In July, *Liberty Coin Service* enjoyed serving a surprising number of new customers who often made larger than typical purchases.

When Adrian Douglas released his analysis in early July, the price of gold was barely over $900. It rose about 5% over the next two weeks, until the price was bombed in late July. *(Ed. Note: As we head to press Gold was treading around $965).*

At some point, I am convinced that the price of gold will take off. Actually, it really should have soared long ago to well over $2,000. The only reason it has not, in my thinking, is actions taken by the US government and its partners to hold down prices.

The tactics to hold down gold prices have become quite blatant in the past year, which is a sure sign that the manipulators are running out of "ammunition." Thus, it would take less of a spark to cause gold prices to soar.

When the time finally comes that gold makes a major move, it could do

Continued on page 22

Major Gold Rise

Continued from page 18

so quickly. Last September, the price of gold jumped almost $100 in a 24 hour period. It could do this again – and more.

A byproduct of this surge in gold prices will almost certainly be a disappearance of physical gold, and higher premiums for whatever may be available. I envision a lot of liquidation of "paper gold" that gets turned into demand for the real physical products. Late last year, we saw the almost complete disappearance of all forms of physical gold from the market. I predict the shortages will be worse this time around.

The soaring gold market will also bring along the silver market with it. Once the owners of the huge short positions in the gold and silver commodity markets are forced to cover or declare bankruptcy (probably both), prices could rise faster than we have ever seen.

Right now, it is still possible to obtain physical gold and silver on a relatively prompt basis. That could change.

With the dip in gold and silver prices, we enjoyed our highest sales day in many months. If this continues, we could see shortages developing soon.

If you are considering the purchase of physical gold or silver, I recommend doing so by August 20 at the latest. If my prediction does not come true by the end of September, I think it will still come to pass somewhat later. If you act now when you know you can get the product, you are safer.

Editor's Note: Patrick Heller is editor of *Liberty's Outlook*, published by Liberty Coin Service, 300 Frandor Ave., Lansing, MI 48912, 1 year, 12 issues, $129. Liberty Coin Service has been a dealer in rare coins and precious metals since 1971. www.libertycoinservice.com.

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