Liberty's Outlook

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Real Estate And EMP—Risks To Paper Asset Values! How Gold And Silver Can Protect You

The primary reason we advocate holding precious metals and even perhaps rare coins is as insurance against possible losses in the value of paper assets such as stocks and bonds.

As such, we recommend that part of your net worth, 5-25%, be held in "hard assets."

With insignificant returns from interest bearing accounts and instruments, and the dismaying performance of many stocks thus far this decade, many investors have turned to tangible assets as a way to improve the return of their holdings.

One market that has performed well over the past several years has been real estate, both residential and commercial. Lower interest rates have brought down the mortgage payments for potential homeowners, with the result that many renters have become homeowners. Rising demand has pushed up real estate prices dramatically.

This phenomenon has happened in the U.S. and in just about every developed nation over the past few years (the exceptions being Germany and Japan).

It is not an exaggeration to say that most of the increase in the Gross Domestic Product (GDP) in industrialized nations during this decade is attributable to higher real estate prices.

How high have real estate prices jumped?

One way is to look at relative real estate capital costs compared to the cost to rent the same property.

The *Economist* recently analyzed this purchase/rental ratio and said the U.S. one-family homes were selling in 2004 at 35% above the average ratio from 1975-2000!

Not only are houses in the U.S. becoming more expensive relative to income levels, but much of this market is investor driven. The 2004 statistics from the national Association of Realtors in the U.S. show that 36% of house sales were for investment and appreciation purposes (13% are second homes and 23% are strictly investment). In normal markets, investment demand accounts for less than 20% of housing purchases.

Not only are people jumping into real estate, they are also doing so on a more leveraged basis than in the past. This year, approximately 25% of home buyers in the U.S. (and 42% of first-time buyers!) are not making any down payment on their purchase.

Further, recent new options for home buyers are interest-only and negative amortization mortgages. The latter is one where the buyer's payment is less than would cover interest, so the principal balance rises over time rather than declines.

In 2002, 8% of new mortgages in California were of the interest-only and negative amortization variety. Thus far in 2005, about 60% of new California mortgages are of these types. Nationwide, these highly leveraged mortgages account for one-third of the mortgage market!

Long-term interest rates have actually fallen slightly in the past year as short-term rates have nearly doubled. But, about 50% of new mortgages in the U.S. are adjustable-rate mortgages, making them more sensitive to short-term interest rates than long-term.

On top of this, homeowners are becoming more aggressive at taking out equity lines of credit on the homes. In essence, they are borrowing against the appreciation in their property to finance current consumer demand.

When you look at all these factors, it becomes obvious that it would not take much of a shift in the market to halt or even reverse the increases in the real estate market.

Here's a simple example from right here in Lansing. General Motors, the area's largest employer, is building a new plant to which it is transferring many employees from other facilities in the city. Originally, the plan was that there would be no substantial gaps in employment.

Plans have changed. General Motors has delayed the opening of the new plant by at least a year and in May it permanently closed major parts of its existing local operations. Now, employees at best are facing a one year gap in employment (though

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company benefits cover most of the lost income) and fewer employees will be able to transfer to the new factory than originally expected.

Several businesses that depend on the patronage of auto workers have seen their volume decline. Some have even closed as a direct result of the shutting of the old factories.

When I recently talked with the owners of the largest real estate firm in this area, their carefully-worded comment on the real estate market was that prices were still holding but it was taking longer for homes to sell.

In other words, a lot of folks in this area are not feeling all that prosperous right now. They are being cautious and cutting back their spending until they feel more confident.

Any kind of stall in the real estate market would put a lot of leveraged buyers into financial difficulty. That would hurt consumer demand in general and real estate prices in particular.

Elsewhere strong real estate markets such as Great Britain, The Netherlands, and Australia, have already cooled off considerably, and even seen prices decline. It could happen here.

Two factors might hold off the decline of the U.S. real estate market. First, there are already a number of alarmists warning of the overheated real estate market. Normally, a market is not truly at its peak until "everyone" gets in on the frenzy.

Second, when the real estate market declines it doesn't drop as fast as can happen with stocks. Losses of 10-20% per year are possible, but there is little likelihood of a 50% drop.

Summary: The real estate market in the U.S. today has many characteristics of an overheated bubble. That makes such investments highly risky. Rather than taking such risk, investors may want to add to their non-leveraged holdings of gold and silver.

The Risk Of Electromagnetic Pulse (EMP) Attack On U.S. Is Real

I don't want to be sensationalist. So let me quote the Abstract from the Volume 1: Executive Report given last summer to Congress by the Commission to Assess the Threat to the United States from Electromagnetic Pulse (EMP) Attack:

"Several potential adversaries have or can acquire the capability to attack the United States with a high-altitude nuclear weapon-generated electromagnetic pulse (EMP). A determined adversary can achieve an EMP attack capability with having a high level of sophistication.

"EMP is one of a small number of threats that can hold our society at risk of catastrophic consequences. EMP will cover the wide geographic region within line of sight to the nuclear weapon. It has the capability to produce significant damage to critical infrastructures and thus to the very fabric of US society, as well as to the ability of the United States and Western nations to project influence and military power.

"The common element that can produce such an impact from EMP is primarily electronics, so pervasive in all aspects of our society and military, coupled through critical infrastructures. Our vulnerability is increasing daily as our use and dependence on electronics continues to grow. The impact of EMP is asymmetric in relation to potential protagonists who are not as dependent on modern electronics.

"The current vulnerability of our critical infrastructure can both invite and reward attack if not corrected. Correction is feasible and well within the Nation's means and resources to accomplish.

Here's the translation into plain English. A nuclear bomb detonated above earth's atmosphere would create a split-second electromagnetic pulse, similar to an extremely high-energy radio wave.

For instance, a widely available Scud missile that costs about $100,000 could be launched from a ship offshore and detonated about 95 miles above the surface to affect about 1/4 of the continental U.S.

A more sophisticated ship-launched missile could be detonated about 300 miles above the Earth's surface and cover the entire continental U.S. and parts of Canada, Mexico, and the Caribbean.

For the U.S., EMP would the true weapon of mass destruction. Rather than killing a smaller number of people from a ground level explosion, it could literally endanger the lives of everyone in the continental U.S. when essential infrastructure collapses.

Another advantage to an EMP attack is that it can be done in such a way that the identity of the attacker is not instantly evident, thereby hampering efforts to respond.

EMP would literally melt the metallic components of electronic equipment. Unshielded electronic wiring in airplanes, automobiles, computers, communication lines, power generating systems, appliances, and the like would become inoperative.

Without electricity, refrigerators and water treatment plants would no longer work. Gasoline stations would no longer have power run the pumps. Hospitals, factories, and financial institutions would close.

In an instant, people would be deprived of transportation, communication, comfortable shelter, food, and water beyond what they had already on hand. The Commission expects it to take years to recover from such an attack, with some analysts saying that it would put U.S. technology back 100 years!

In some ways, the scenario of an EMP attack is worse than was feared for Y2K, when computers might have failed because of an inability to handle the date changes to January 1, 2000.

Unfortunately, the possibility of an EMP attack is not just theoretical. At least two nations and at least one terrorist group have the technology and equipment already in hand or could obtain it without difficulty.

North Korea has been selling missiles to other nations that have the capability of reaching and detonating where they could cover the entire

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continental U.S.

Iran has actually ship-launched and detonated its Shahab-3 missiles in what its government described as "successful" tests. International experts consider that the only purpose of these tests is for delivering an EMP attack. On May 31, Iran also announced that it was domestically manufacturing solid rocket fuel for these missiles. This is a much more stable fuel that can manufactured a long time before launch and then withstand the rigors of transportation by ship across oceans.

Terrorist groups such as Al-Qaeda already have the ships and certainly have the funding to acquire the missiles and nuclear warheads if they don't have them already. The nuclear warheads do not need to be the best available. One analyst thinks that the atomic bombs of the caliber of those dropped on Japan in World War II would be powerful enough to disrupt the U.S.

The Commission's findings made several recommendations about what could be done about this existing risk. For the civilians—besides trying to "harden" critical power grid and telecommunications infrastructure, it also urged deployment of a ballistic missile defense system. Such steps will take years and cost a lot. In the meantime, there are steps you can take to prepare yourself from the aftermath of an EMP attack.

Besides having food, water, and medicines on hand, you will also need a means of payment. Credit cards and bank accounts will be worthless. There is a good possibility that even the U.S. dollar will fail without any government to support it.

For this reason, you need to have on hand some silver and gold for barter purposes. To have on hand does not mean owning it in a brokerage account or even having it in a safe deposit box. You need to have it where you can physically put your hands on it without having to depend on other businesses being open.

In such a scenario, I think U.S. 90% Silver Coins (especially dimes and quarters) and the 1 Oz Silver Rounds and Ingots will be some of the most widely traded forms of money. Alloyed (not pure) small gold coins such as the 1/10 and 1/4 Ounce American Eagles, 1/10 and 1/4 Ounce South Africa Krugerrands, British Sovereigns, French and Swiss 20 Francs, Netherlands 10 Guilders, Russian 5 and 10 Roubles, and Mexico 2, 2.5, 5, and 10 Pesos would probably be the most widely circulated gold coins. Pure gold is so soft that it cannot withstand the rigors of circulation, so I would avoid them if purchasing gold coins for possible spending. That leaves Canada Maple Leafs, Austria Philharmonics, Australia Kangaroos, China Pandas and the like off the shopping list.

Summary: I certainly hope that we never see an EMP attack anywhere, but the capability of an unsophisticated one-missile attack on the U.S. exists. Simply for insurance if this horrid event comes to pass, each person should have direct access to some silver and gold coins and ingots. If budgets permit, allocate at least $1,000 per household member toward this end. Any silver or gold you already own can count towards this purpose as long as you have direct access to it.

Here the ownership of gold and silver may not only protect you from the loss of value of your paper assets. They also might save your life.

Rare Coin Market Stays Mostly Solid

The rare coin market, for the most part, is staying strong and active. However, there are some areas where demand has stalled at current levels, and some prices have even dropped in the past couple of months.

It happens that the weaker areas are the very ones we had warned our customers to avoid—like Carson City Mint Morgan Dollars, 1895-O Morgan Dollars, and High Relief 1907 $20.00 St Gaudens.

Collectors are still chasing the better-date coins. For instance, in a recent week we received at least six calls asking us if had a low-grade circulated 1916-D Mercury Dime in stock. Demand for such coins is much larger than our ability to locate and stock them. That bodes well for continued increases across wide areas of the rare coin market. The difficult part is simply finding attractive coins at any kind of reasonable price.

Gold and Gold Coins

Gold finished today at 423.50, up $8.25 (2.0%) from five weeks ago. Gold was much more volatile in June than the relatively modest change would indicate.

For much of the month, gold surged from its recent relative low level, hitting a high on June 23 at $441.50. It still closed over $440 three days later before what I term the "Federal Open Market Committee (FOMC) swoon" took effect.

On June 30, right before the long Independence Day weekend, the Fed increased short-term interest rates another 0.25%, its ninth such increase in the past thirteen months.

(Let me digress for a moment. When trying to manipulate a market, you can get maximum effect by carefully timing announcements. Normally the FOMC meets and makes their interest rate hike announcements on a Tuesday. The impact of any major announcement can be magnified if it comes on the Thursday just before a three-day weekend, when traders are looking diverting their attention from business. Whoever, scheduled this FOMC meeting for June 30 was a genius if the purpose was to have maximum impact at driving down precious metals prices.)

After the announcement of the interest rate hike, gold dropped 3% over the weekend. But it did not go all the way back to the levels at the beginning of June—which I consider significant.

Just as we have seen consistently with the other interest rate hikes, I think right now is a bonus buying op-

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portunity for gold. If the market behaves as before, gold (and silver) will recover within a week and approach levels we saw in mid-June.

The low-premium best buys in gold are still the Austria **100 Corona** (3.5%), South Africa **Krugerrand** (3.7%), and U.S. **American Arts Medallion** (3.7%). Among smaller coins, I like the **British** Sovereign (7.6%).

Several **common-Date U.S. Gold Coins** in MS-63 and MS-64 grades are down 5-10% in the past month, as I anticipated. I believe the bargain buying opportunity is almost over, so don't delay adding some lovely $2.50, $5.00, and $10.00 Liberties and $5.00 and $10.00 Indians to your holdings.

Better-Date U.S. Gold Coins are still in strong demand and almost impossible to find.

After somewhat lengthy negotiations, we managed to acquire a modest group of the **2004 Canada 25th Anniversary 1 Oz Maple Leaf Commemorative.**. This is the lowest mintage bullion-related 1 ounce gold coin ever struck in North America, which we can offer at a price that clobbers the competition. See our offer.

Silver and Silver Coins

Silver ended up today at $6.93, down a relatively large 57 cents (7.6%) from last month.

On June 6, silver came within one cent of its highest price in almost six months, which apparently triggered some profit-taking.

A week later, after the sell-off had run its course, the silver price started to climb once more. This rally was short lived. Then the silver price fell in conjunction with the FOMC interest rate hike.

For years, I have used two indicators to identify times when the price of silver may explode. The first is if the retail price on U.S. **90% Silver Coin** (3.5%) is higher than 2%. When it trades retail above that level, refiners cannot profitably melt down the coins to recycle the silver, leading to a drop in physical supplies.

The second indicator is if the price of silver in the London market is more than 6-8 cents higher than the New York market. The world's largest silver market is the London Bullion Market Exchange, which requires its bars to be refined to .9999 purity. The bars on the New York Comex are only .999 fine. To be deliverable in London, New York bars would have to be refined once more, then physically transported across the Atlantic Ocean, a process that would cost 6-8 cents per ounce.

The London premium over New York has mostly been 1-3 cents for the past year. It recently jumped to 8 cents. If this premium can hold for a week (it may just be a temporary burp caused by the FOMC announcement and the 3-day holiday weekend in the U.S.), that would mean that both indicators are turning positive at the same time, which has not happened in years.

While I am not forecasting a quick surge in silver prices, because the London premium might be a false alarm, it could happen. Don't wait to build your position.

Our most recommended form is the 90% Coin. It has the lowest premium, best liquidity, and maximum divisibility.

The market for **Common-Date Morgan and Peace Silver Dollars** has held steady, even with the shakedown of some of the scarce dates that ran up too far too fast. I consider this to be one more indicator of the continuing bull market in rare coins.

If you ever wanted to own a coin that played a significant role in changing world history, you have a chance. This month we offer affordable specimens of the **Treasure Silver "Pieces of Eight"** from the Maravillas shipwreck. The loss of this one ship changed history in two ways. See our flyer for details.

The Month

Gold Range	$26.25	6.3%
Net Change	+8.25	
Silver Range	.68	9.1%
Net Change	-.57	
Gold/Silver Ratio		61.1
Net change		+5.7
Platinum Range	44.00	5.1%
Net Change	-10.00	
Platinum/Gold Ratio		2.02

Date	Gold	Silver	Platinum
Jun 01	415.25	7.50	864.00
Jun 02	422.75	7.53	870.00
Jun 03	423.75	7.49	869.00
Jun 06	426.50	7.52	875.00
Jun 07	424.50	7.43	875.00
Jun 08	424.50	7.44	874.00
Jun 09	423.75	7.25	868.00
Jun 10	427.00	7.27	866.00
Jun 13	429.00	7.25	868.00
Jun 14	427.00	7.26	869.00
Jun 15	429.00	7.32	876.00
Jun 16	436.00	7.36	885.00
Jun 17	438.00	7.33	891.00
Jun 20	438.00	7.21	894.00
Jun 21	438.75	7.28	877.00
Jun 22	438.00	7.26	885.00
Jun 23	441.50	7.27	883.00
Jun 24	440.50	7.27	887.00
Jun 27	440.25	7.24	884.00
Jun 28	436.25	7.10	877.00
Jun 29	437.00	7.07	881.00
Jun 30	435.75	7.03	876.00
Jul 01	427.75	6.86	865.00
Jul 04	closed		
Jul 05	422.75	6.84	850.00
Jul 06	423.50	6.93	854.00

London Silver Market Premium To New York Silver Market = 8¢

Gold, silver and platinum quotes are working spots at 2:45 EST/EDT each day, quoted in U.S. dollars per troy ounce.

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