Liberty's Outlook

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15th Consecutive Annual Silver Shortage!

Gold Hits Highest Prices In Almost 18 Years!

Page 3: Patriot Act Section 352—More Privacy Lost!

Annual Silver Surpluses/ Shortages 1971-2004 in Millions of Ounces

1971	**-34.6**	1981	114.3	**1991**	**-68.1**	**2001**	**-82.9**
1972	**-94.6**	1982	80.5	**1992**	**-75.7**	**2002**	**-87.0**
1973	**-128.0**	1983	162.5	**1993**	**-184.0**	**2003**	**-55.0**
1974	**-51.0**	1984	85.7	**1994**	**-200.6**	**2004**	**-55.0**
1975	**-4.1**	1985	88.2	**1995**	**-183.0**		
1976	**-17.8**	1986	8.4	**1996**	**-208.8**		
1977	**-49.1**	1987	40.7	**1997**	**-221.6**		
1978	**-57.1**	1988	24.3	**1998**	**-205.0**		
1979	25.9	1989	8.3	**1999**	**-161.4**	**Total**	
1980	207.2	**1990**	**-30.8**	**2000**	**-155.0**	**1971-2004**	**-1,563.6**

Source: CPM Group's Silver Survey 2005 and other cited data

Precious metals and rare coin activity have been at near frenzied levels for the past two months, with gold hitting its highest price in nearly 18 years!

Silver has jumped as much as 11% from its end of August lows. The U.S. government has issued regulations that take effect in three months further eroding financial privacy.

With so much going on, however, I think we will be even busier in the months to come. So, this month I will review the latest information on the long-term supply and demand fundamentals for the silver market.

Silver's Track Record

In 2004, the average price of silver for the year was $6.70, a 36.7% increase over the average 2003 price of $4.90.

Despite this surge in price, industrial and coinage demand for silver in 2004 increased 1.1% over 2003!

For almost the entire period from 1993 to late 2003, silver ranged from $4.00 to $5.50. Since late 2003, silver prices have been rising overall. A large number of new investors have entered the silver market over that time, many who have no previous experience in precious metals markets.

Once again in 2004, for the fifteenth consecutive year, the silver market had a huge supply shortage.

Total supplies from mine production, recycling, and government sales were 750.0 million ounces, falling 55.0 million ounces (6.8%) short of covering industrial and coinage demand of 805.0 million ounces.

For 2005, despite ever higher silver prices, a shortage of another 43 million ounces is projected!

Since the beginning of 1990, almost 2 billion ounces of silver inventories have been consumed to cover supply shortages. At the end of 2004, less than 1 billion ounces of inventories remain.

As I have said before, the 1970s string of shortages did not end until the price of silver soared above $50.00 in early 1980.

The shortages of the past 15 years dwarf those of the 1970s.

On the basis of this information, one would anticipate that the price of silver could explode upward.

I actually expected much higher silver prices long ago. Instead, the price has largely been stagnant. The silver price did climb to $8.20 in the spring of 2004 and topped $8.00 again later in the year.

This year, silver demand has been strong any time the price dipped below $7.00. Could silver be building a solid base for a major boom ?

Perhaps.

Analysts have been mystified as to why the price of silver did not soar years ago. But the fundamental supply and demand information is indisputable.

Inside this issue:

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I believe that the silver market is destined for huge price increases within the next four years, perhaps even within the next year.

To give you the background on my thinking, let's review the four major factors affecting silver prices: supply, demand, inventories, and investor psychology.

Supply: The four major sources of silver supply are primary silver mines, as a by-product or co-product of gold, lead, copper, zinc, and other mines, recycling, and government sales. In 2004, silver supplies rose 1.2% from 2003 to an all-time record 750.0 million ounces:

Source	*Millions Oz*	*%*
Mines	518.3	69.1%
Recycling	216.7	28.9%
Government sales	15.0	2.0%
Total	750.0	100.0%

Source: CPM Group

Note: Above totals include next exports over imports of 5 million ounces from "transitional economies" such as countries that were formerly part of the USSR, China, and North Korea.

Mines: Primary silver mines only account for 20-30% of newly mined silver. The balance comes as a byproduct or co-product of other mining operations.

For instance, the world's largest silver mine is the BHP Cannington *lead-zinc* mine is Australia, which produced 41.3 million ounces of silver in 2004. The second largest silver mine, the KGHM Polska Miedz *copper* mine in Poland produced 39 million ounces of silver in 2004.

Around the world, mine production rose 5% over the year before, and will likely rise another 3% in 2005. Technological improvements make it easier to discover new silver reserves and to economically extract lower purity ores.

Higher silver prices have a delayed effect on the expansion of silver mines. A new mine project takes about three years to begin production. When the price of silver reached $50.00 in early 1980, it took until 1983 for mine production to increase 10% from 1979 levels.

Recycled silver: Recycled silver supplies in 2004 were down a small amount from 2003.

The largest component of recycled silver, about 202 million ounces in 2004, comes from spent photographic papers, films and solutions, x-rays, old batteries, and industrial waste. As the use of silver in photography declines, the amount of photographic silver that is recycled also declines. This pretty much offsets any increased recycling from other sources brought on by higher prices.

The government of India is still trying to eliminate its ban on exporting silver. Should that occur this year, look for total recycled supplies to rise in 2005, perhaps as much as 5%.

Government sales: Government sales are minor mainly because governments have only small silver inventories.

China was a net exporter of silver in 2005, but at levels that were down about 75% from the year before. Domestic demand in China is growing enough that it may stop exports in 2005.

On the other side, India's central bank began to sell its silver holdings this year, so total silver supply from government sales will likely be unchanged in 2005.

Summary: Silver supplies should be higher in 2005 than in 2004, setting a new supply record in the process. .

Demand: Because of its relatively low price, silver may not deserve to be called a "precious metal." In fact, it is highly sought for industrial applications because of its *low* price.

As I said earlier, industrial and coinage demand rose in 2004 despite sharply higher prices. The low prices over the past decade have stimulated research into new uses for silver. Demand has also grown because the world population is growing as is the world's per capita wealth.

Use Category	*Millions Oz*	*%*
Jewelry/silverware	242.5	30.1%
Photography	239.4	29.7%
Electronics/batteries	106.8	13.3%
Coinage	10.5	1.3%
Other	205.8	25.6%
Total	805.0	100.0%

Source: CPM Group

Jewelry and silverware: Jewelry and silverware 2004 consumption dropped 7.6% from 2003, in response to the 36.7% higher prices. This is the most price-sensitive form of silver demand, yet you can see that total demand, in dollar terms, actually rose more than 25% in 2004!

Despite higher prices in 2004 and again in 2005, this sector may see an increase in demand for 2005 compared to 2004.

Photography: Despite the surge in the use of digital photography over the past few years, photographic silver usage has dropped barely 10% from its 1999 peak. The total photographic market is expanding, with x-rays leading the way.

Still, photographic silver demand is expected to slide further as the years go by. It could fall by as much as 8% in 2005 compared to 2004 levels.

Electronics and batteries: Silver is used in connectors, conductors, switches, contacts, relays, fuses, batteries, and lots of other applications. Demand was at its second highest level ever in 2004, topped only in 2000.

For 2005, silver usage may rise another 5% in this category.

Coinage: Silver used for coinage in 2004 rose 5% from 2003. The U.S. Silver Eagle Dollar is the largest component of this demand.

As more investors and collectors purchase physical silver, demand in 2005 should show another increase.

Other uses: Silver has a wide range of uses, from catalysts, mirrors, brazing alloys, water purification systems, solders, paints, medications, and so forth.

As more research is conducted on possible uses for silver, demand for silver for other uses is growing faster than any other segment—having doubled in the past 15 years! Demand soared more than 21% in 2004! Expect another 8% increase in demand in 2005.

Summary: The strength of silver demand for new industrial applications will continue to push total silver demand higher in coming years, more than offsetting the decline in photographic usage.

Because silver is such a small component of many fabricated products, rising silver prices have minimal effect on demand. From 1976 to 1980, for instance, the average annual silver price rose 263% (adjusted for inflation). Despite this soaring price, total silver demand only dropped 29%! The price of silver could triple or quadruple from current levels with only a modest effect on demand in this sector.

Inventories: Deriving inventory levels is difficult, because only a small percentage of total inventories are registered and reported on commodities exchanges.

However, it is unmistakable that inventories have declined sharply since the beginning of 1990—almost 2 billion ounces!

At the end of 2004, here are mid-range estimated inventories potentially available for industrial and coinage uses:

Category	*Millions Oz*
Comex	107.8
Tocom	0.4
U.S. and Japanese manufacturers	22.5
Bullion in private U.S. holdings	30.0
Bullion in Berkshire Hathaway	129.7
Bullion in private European, Asian, and Latin American holdings	20.6
Silver coins (primarily U.S. 90%)	508.0
Government holdings	122.7
Total	941.7

Source: CPM Group

Note: The above inventory figures exclude holdings which are consumed domestically in China, North Korea, and nations formerly part of the USSR.

The major source of inventories consumed in 2004 to cover shortages came from the Comex, and private holdings in the U.S., Europe, Asia, and Latin America. As a group, these inventories dropped 27% from year earlier levels! That leaves barely 150 million ounces.

These are the major sources of silver available to cover continuing shortages.

The other forms of silver inventories are not that available to cover supply shortages. Manufacturing inventories are still

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down one-third from 2000 levels, for instance. The amount of coin silver is actually increasing as more Silver Eagle Dollars are struck. The remaining silver inventories are in forms that were not liquidated when silver hit $50.00 back in early 1980.

Summary: This inventory tabulation is a mid-point of the range from the lowest to highest in categories where exact figures are not knows. It excludes many forms of fabricated decorative silver objects that, for all practical purposes, would not be sold simply because of a dramatic rise in the price of silver. It includes all silver coins struck worldwide since 1800 less any than have been melted in the past few decades.

With most silver coins now selling to investors at a premium to silver value, there is little likelihood that they would soon be sold for melting down and refining at current prices.

If you look at only the inventories that are readily available to cover shortages, there is only enough to last a few more years!

Because silver is no longer a reserve asset (at today's price, all government holdings combined are worth less than $1 billion) governments have little incentive to manipulate the price. As a result, the price of silver is free to respond to market signals much more than gold.

Investor psychology: With the fundamental supply, demand, and inventory figures for silver showing a near– and long-term shortage of silver, why hasn't the price already soared? Will it ever do so?

Above and beyond the data, there are several factors that affect investor psychology.

Of course, investors' choices are affected by all the economic, political (and weather!) events. In times of greater uncertainty, there is a definite trend in favor of owning tangible assets.

The surge in silver to $50.00 in 1980 prompted a lot of people to invest in the metal. However, silver supplies gradually increased while industrial demand slowly fell over the following years. This surplus lasted through 1989, gradually forcing down prices.

Even though the fundamentals had changed since the beginning of 1990, there are still a lot of former silver investors that are scared that there is still a glut of silver on the market that will knock prices down in the future. That has limited investor demand over much of the past 15 years.

But the times are changing.

When the stock and bond markets dropped in 2000 and stayed relatively weak for the next couple of years, many investors expanded their investment horizons to other assets, including silver.

Silver's attractive fundamentals brought in substantial new investment demand. LCS sold record quantities of silver in the first half of 2003, for instance.

At the same time, the psychology of existing silver investors changed. For much of the 1990s, any temporary jump in the price of silver would lead to a flood of liquidation. There is still some increase in liquidation as prices rise today, but at much lower levels.

These two trends are much like we saw in the late 1970s before silver prices exploded.

In the boom back them, investors didn't really start selling their silver until the price passed $20.00. In fact, most didn't sell until after it passed its $50.00 peak.

How High For Silver?

In the past 34 years, silver demand has exceeded new supplies by 5%. In 2005 dollars, the average silver price over this time was about $17.00. Since that price was not high enough to establish a long-term equilibrium, I think the price deserves to be higher.

Silver supplies cannot rise quickly if the price of silver shoots upward. Therefore, I expect any run to rise well beyond $17.00 before settling back.

Last year I anticipated that the price of silver would reach $10.00 by the end of 2005. Although there are still 12 weeks left, that doesn't look so likely now. Since prices are still rising over time, that just tells me that I was premature in the forecast, not flat out wrong. Maybe it will hit that level in early 2006.

Even though you cannot buy silver as cheaply as you could three years ago, higher silver prices still look like almost a "sure thing" to me. Mega-billionaires Bill Gates and Warren Buffett have significant investments in silver.

For most people, I currently recommend that silver make up half of your precious metals holdings.

Patriot Act Section 352 Regulations Established

Under the guise of combating terrorism, the U.S. Treasury recently released regulations to implement Section 352 of the USA Patriot Act of 2001.

This section applies primarily to rare coin and precious metals dealers. The regulations pretty much have to do with coin dealers having an effective system to be on the alert for transactions that may potentially fund terrorism (and also, unstated, tax evaders).

Beginning January 1, 2006, coin dealers who transact more than a nominal amount with the public will be required to have on hand several documents to be able to prove to the Internal Revenue Service (IRS) at a moment's notice that they are complying with the requirements of Section 352. These documents are:

- A statement identifying the company's designated Section 352 compliance officer, even if there is only one individual working for the company.
- A written plan adequately detailing how the company will comply with Section 352 regulations.
- A certificate of training for all owners and staff of the dealership who may be in a position to have to prepare paperwork to comply with Section 352 regulations.
- A signed statement by someone who is not one of the people who may potentially have to prepare paperwork to comply with Section 352 regulations for the dealership. This statement must confirm that the signer has reviewed the dealership's satisfactory compliance with Section 352 regulations.

The penalties for failure to have the above paperwork are onerous, especially for small companies.. An IRS auditor can visit a dealership at any time and request to inspect these four documents. If any of the documents are not available, the fine is $1,000 per day (beginning January 1, 2006) until all such paperwork is available.

These requirements apply to coin dealers even though they may never have any transactions that call for reporting large cash transactions.

LCS has retained the services of the recently retired IRS official who helped write the Section 352 and other anti-money laundering regulations for the U.S. Treasury (and who also trained federal, state, and local government officials on such regulations). General Manager Pat Heller has already been certified for attending a training workshop on compliance. This firm will be ready by January 1, 2006 to pass scrutiny.

Unfortunately, information about Section 352 regulations is only slowly going around the industry. A high percentage of coin dealers who will be required to have this paperwork don't yet know of these requirements. Those who are getting the timeliest information tend to be members of the Industry Council for Tangible Assets (ICTA), the national coin and precious metals dealer trade association (Pat Heller serves on its board of directors).

There is rampant misinformation about how to comply with Section 352 regulations. Some dealers fear that they will have to obtain copies of drivers licenses from every retail person with whom they buy or sell anything, as banks and other financial institutions now have to do when opening new accounts. They will not.

However, coin dealers will have to con-

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tinue to comply with previous regulations on reporting the receipt of large amounts of cash (defined as cashiers' checks and money orders in amounts under $10,000, currency, and travelers checks) in one or more related transactions over the course of a 12-month period, even though such reports are rarely investigated.

Where members of the public will perhaps be subject to more invasion of their privacy will be the far greater requirements for dealers to file "suspicious transaction" reports. These are reports of actual or potential transactions with the public that are smaller in size than meet the $10,000 threshold for reporting the receipt of large amounts of cash. If a dealer prepares such a report, they are prohibited from disclosing to anyone the fact that such a report has been filed. These suspicious transaction reports are investigated thoroughly and immediately by the federal government.

Most mail-order customers and those who pay by credit card will not be affected by the tightening standards for reporting suspicious transactions. Where this will likely have the greatest effect is in face-to-face transactions of several thousand dollars that are paid in cash where the dealer does not know the customer. For their own protection, expect most dealers to start putting down retail customer names and addresses on sale and purchase transactions that are in the thousands of dollars.

Unfortunately, this loss of privacy will be the price of avoiding a possible investigation as a suspected terrorist (or tax evader). As it is, I expect the effect of the Section 352 regulations will be that a number of innocent people, in the act of trying to maximize their legal privacy, may risk being investigated as a possible crook.

Developments on this issue will be reported in future issues.

The Month

Gold Range	$27.25	6.1%
Net Change	+21.25	
Silver Range	.54	7.7%
Net Change	+.37	
Gold/Silver Ratio	62.8	
Net change	-0.3	
Platinum Range	25.00	2.8%
Net Change	+7.00	
Platinum/Gold Ratio	2.03	

Date	Gold	Silver	Platinum
Sep 07	444.75	7.05	905.00
Sep 08	446.50	6.96	909.00
Sep 09	449.00	7.00	911.00
Sep 12	449.50	7.00	910.00
Sep 13	446.00	6.95	908.00
Sep 14	449.75	6.99	911.00
Sep 15	455.25	7.02	915.00
Sep 16	459.25	7.22	919.00
Sep 19	466.50	7.34	928.00
Sep 20	466.00	7.32	928.00
Sep 21	468.75	7.36	930.00
Sep 22	466.50	7.35	925.00
Sep 23	463.50	7.27	922.00
Sep 26	465.75	7.31	912.00
Sep 27	462.50	7.27	914.00
Sep 28	469.50	7.34	919.00
Sep 29	472.00	7.49	925.00
Sep 30	469.00	7.45	925.00
Oct 03	466.00	7.40	919.00
Oct 04	466.00	7.37	910.00
Oct 05	466.00	7.42	912.00

London Silver Market Premium To New York Silver Market = 4¢

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

Gold and Gold Coins

Gold closed today at $466.00, up $21.25 (4.8%) from last month.

Last month I said that it looked like gold was poised to break up above $450. The following week, it did just that! Then kept going.

When gold settled at $472.00 on September 29, that was its highest close since January 25, 1988!

As gold rose, both buyers and sellers we active. For the past week, activity on both sides has slowed down.

The forms of gold where you get the most product for the least money continue to be the Austria **100 Corona** (3.4%), South Africa **Krugerrand** (3.6%), and U.S. **American Arts Medallion** (3.6%). They all have at least a $5 per ounce price advantage over coins like the U.S. **American Eagle** (5.4%) and Canada **Maple Leaf** (4.8%). Among smaller coins, the **British** Sovereign (7.6%) is a low-cost choice.

Rising gold prices led to a surge of demand for **Common-Date U.S. Gold Coins.** The MS-63 8-coin U.S. Gold Type set is up nearly 16% in the last four weeks, while the MS-64 set is up almost that much!

Normally, when U.S. Gold Coins jump in price like that , you see profit-taking. This time, I think it will be different. At the huge Long Beach Exposition in California three weeks ago, no wholesaler had any Common-Date $10.00 Indians at the show in any Mint State grade! MS-63 $10.00 Indians are up 26% since the last newsletter. With supplies so tight (LCS has sold more U.S. Gold Coins to retail customers in the past month than we have in any month over the last fifteen years!), I expect prices to continue rising..

Better-Date U.S. Gold Coins that sell close to the price of the common issues can be an even more attractive value—if you can find them! Before prices took off, we managed to acquire a sizeable group of **Choice Mint State-63 $5.00 Liberties** that we are offering at well below current retail prices for a short time. Some are common-dates and some are these attractive better-date issues. Get them while you can. See our flyer.

Silver and Silver Coins

Silver finished today at $7.42, a rise of 37 cents (5.2%) from four weeks ago.

Little silver has been liquidated over the past two months, much less than physical demand. Because of this, premiums have held near their recent higher levels.

At the same time, the premium of the London market silver price over the New York Comex silver price bumped up a tad—not enough to send a warning signal, but still enough to keep an eye on it.

With all for favorable factors going for it, there is every possibility that silver will reach $8.00 by year end, even if it doesn't make it all the way to $10.00.

The best buy remains the U.S. **90% Silver Coin** (3.3%). It has the lowest cost per ounce of silver content, the greatest divisibility, and is also the most liquid. The **100, 10, and 1 Oz Ingots** (5.7-6.6%) cost more but have an advantage of occupying slightly less space.

Now that it is virtually certain that the series of U.S. Presidents Dollar coins will happen, probably starting in 2007, dealers are stocking up in anticipation of higher demand for the older **Common Mint State Morgan and Peace Silver Dollars**. Expect to see significant price increases over the next few months. LCS was fortunate to acquire some of the nicest coins from a 1923 Peace Dollar bag. See our offering of **Choice Mint State-63 and Gem Mint State-65 1923 Peace Dollars.**

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