Liberty's Outlook

Volume 13 Issue 9 Liberty Coin Service's Monthly Review of Precious Metals and Numismatics September 5, 2007

Global Liquidity Crisis Grows Despite Massive Government Subsidies!

P. 4: Tight Physical Silver Supplies Push Up Premiums!

In August, record levels of government subsidies to the financial sector were unable to stop, or even slow down, the growing global liquidity crisis.

The European Central Bank (ECB) injected $125 billion into the financial system on August 9, followed by another $136 billion soon thereafter.

The U.S. Federal Reserve Bank tried to reassure banks and brokers with its own injection of $24 billion. A 1/2% reduction in the overnight bank borrowing rate on August 17, plus an expansion of financial instruments that would be accepted for collateral for these emergency loans, enabled the Fed to push another $200 billion into the money supply.

Despite growing domestic economic troubles, Japan's central bank cancelled an expected interest rate hike to try to help out.

Even with these record amounts of subsidies, which total more than were released after the World Trade Center and Pentagon attacks on September 11, 2001, investors are running scared.

In a speech in New York yesterday, Robert Mundell, who won the 1999 Nobel Prize for Economics and who is considered the intellectual father of the Euro currency, said, "It was mind-boggling—that amount of money being pushed into the system. (The Euro) went down a little bit, but it was surprising that such a huge amount of monetary shock would not create a bigger effect."

Mundell also worried that, "The movement up in the Euro toward $1.40 is devastating for the European economy. It creates the potential for deflation . . . It's a hangover for the stock market."

The huge size of the August subsidies by the ECB and Federal Reserve had the side effect of temporarily clobbering the prices of gold and silver. At one point, the price of gold was down almost 4% from its August 8 closing price. Silver fell almost 15% by August 16 during intraday trading.

Since mid-August, gold has roared back to close even higher than it was on August 8.

In fact, the closing gold spot price of $672.75 on August 31 was the 3rd highest month-end gold close ever! Only the $681.50 close at the end of January 1980 and the $680.50 close at the end of April 2006 were higher. End of the month closing prices have added significance because these are the prices that financial and investment institutions must use in valuing their assets for reporting purposes.

Silver has recovered part of its price drop, but it is suffering partly from widespread investor worries that a global recession could lead to lower manufacturing demand for a wide range of commodities.

The financial turmoil started with tens of billions of dollars of losses in the past few months from the U.S. sub-prime mortgage market. Many investors are so worried about the safety of the capital they have loaned, that they are refusing to renew loans that mature.

For example, in early August, U.S. corporations owed about $2.2 *trillion* in short-term commercial paper debt, typically for 90 days. Borrowers have been unwilling to roll over these notes that have recently matured to such an extent that, in the past three weeks, the volume of outstanding commercial paper has shrunk by $244 billion, or about 11% of all such debt! This unwillingness of investors to continue holding this debt is even more surprising in that this is one of the forms of collateral that the Federal Reserve announced they will now accept against emergency loans.

What this means is that corporations count-

2007 Year To Date Results

Through September 4, 2007

Precious Metals	
Platinum	+11.9%
Gold	+7.5%
Palladium	-0.3%
Silver	-4.4%
Numismatics	
MS-63 $20.00 St Gaudens	+7.1%
MS-63 $20.00 Liberty	+0.0%
MS-65 Morgan Dollar	-10.0%
US Dollar vs Foreign Currencies	
Switzerland Franc	-0.6%
Japan Yen	-2.3%
Great Britain Pound	-2.8%
Euro	-3.0%
China Yuan	-3.3%
India Rupee	-7.5%
Brazil Real	-8.8%
Canada Dollar	-10.0%
U.S. Dollar Index 80.88	-3.4%
US and World Stock Market Indices	
Frankfurt Xetra DAX	+17.1%
NASDAQ	+8.9%
Dow Jones Ind Average	+7.9%
S&P 500	+5.0%
London FT 100	+2.5%
Russell 2000	+1.7%
Tokyo Nikkei 225	-4.7%
Intrinsic Metal Value Of U.S. Coins	
Lincoln Cent 1959-1982	2.25¢
Lincoln Cent 1982-date	0.78¢
Jefferson Nickel-non-silver	6.47¢
Roosevelt Dime 1965-date	2.94¢
Wash Quarter 1965-date	7.34¢
Kenn Half Doll 1971-date	14.67¢

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ing on being able to rollover this $244 billion in debt have suddenly had to liquidate assets or find other sources of financing.

Financial worries are even more dire in the London markets. Significant quantities of short-term debt were borrowed at the London Interbank Offering Rate (LIBOR) in order to re-loan an higher rates. Because of the liquidity squeeze, the LIBOR three-month rate has risen to 1.05% above the Bank of England base rate. In effect, borrowers who want to roll over maturing debt would now have to borrow it at a higher cost that may exceed what they have charged to re-loan it!

As Patrick Perrett-Green director of European derivatives and bond trading at Citigroup (one of the world's largest banks), said today **"The reality is that the central banks don't know how to deal with the current situation within the confines of their existing rulebooks. . . . In short, things are a mess and unless central banks start to properly recognize the dangers, the situation could reach critical."**

Top officials at one of the world's largest banks just do not speak so bluntly unless the problems are so bad that they cannot be hidden anymore. This one quote, all by itself, scares me enough to want to get out of all paper assets! And that doesn't even take into account that there is so much other hard data supporting such a shift.

Perret-Green urged the Bank of England to make an urgent cut to its base interest rate. He may get his wish. Tomorrow, the governing board of the Bank of England holds its monthly meeting. A possible interest rate cut is certain to be the most important issue on the agenda.

This past weekend, the Federal Reserve Bank of Kansas City hosted its annual retreat for central bankers at Jackson Hole, Wyoming. Apparently, as one speaker followed another, the mood got progressively gloomier.

There, Axel Weber, president of the German central bank and a member of the European Central Bank council said, "What we are seeing is basically what we see underlying all banking crises." He thinks that the world is undergoing a classic banking crisis, except that it is taking place outside of the traditional banking sector.

Many hedge funds have been forced to reduce their holdings recently simply because they have not been able to borrow as much money for new investments. One area where they have cut back is in purchases of U.S. Treasury debt. One exchange that trades Treasury debt among hedge funds has seen their volume fall by 80%.

On the other side, the investors who are becoming more reluctant to roll over loans in the private sector are putting their funds into U.S. government debt instead.

Between the decrease in demand from one sector and rising demand in another, the overall U.S. Treasury debt market has become the most volatile it has in years. Treasury bills, which have the shortest maturities, are considered to be the safest of all debt. Because they are so liquid, the daily fluctuation in their interest rates are typically 1 basis point (0.01%).

Just after September 11, 2001, 90-day Treasury bill interest rates fluctuated by more than 10 basis points on five days. From January 2002 through July 2007, 90-day Treasury bill interest rates fluctuated by 10 basis points or more on only six days.

In the month of August, 90-day Treasury bill interest rates fluctuated by 10 basis points or more on 15 days!

Because of this higher volatility, brokerage firms are widening their buy/sell spreads and increasing their commission charges. In some instances, the charges for purchasing Treasury debt have increased more than 800%.

Another speaker in Jackson Hole was Marty Feldstein, a Harvard professor who was the chair of President Reagan's Council of Economic Advisors from 1982 to 1984. He urged the Federal Reserve Board to immediately drop the federal funds rate from 5.25% to 4.25%. He considers tackling the near paralysis in the credit markets as more important than fighting inflation.

If the Fed didn't do this, he warned, "The economy could suffer a very serious downturn. A sharp reduction in the interest rate, in addition to a vigorous lender-of-last-resort policy, would attenuate that very bad outcome."

Ethan Harris, the chief economist at brokerage Lehman Brothers, echoed Feldstein's sentiments, "There's a pretty strong consensus that this has got a lot more serious."

While all this was going on, Federal Reserve Chair Ben Bernanke said that the Fed would act as needed to provide financial stability. In a classic example of speaking out of both sides of his mouth at the same time, Bernanke then went on to say "It is not the responsibility of the Federal Reserve to protect lenders and investors from the consequences of their financial decisions."

More News You Might Have Missed

1) The World Gold Council reported that gold demand in India, the world's largest gold consuming nation, for the first six months of 2007 surged 70% ahead of 2006 levels! Even if demand drops in the second half of 2007, it is likely that annual demand will set an all-time record.

2) The Barclay's Bank silver exchange traded fund (ETF) has seen its outstanding holdings decline. Since each share of this ETF represents 10 ounces of silver, it is possible to redeem shares to take delivery of the physical metal. This ETF requires that redemptions take place in 50,000 share lots (500,000 ounces of silver). Barclay's recently reported a one-day drop of 3,000,000 ounces of silver (about 2% of the ETF's holdings), which means that 300,000 shares had been redeemed for physical silver.

3) I have several times reported about the huge silver shortage positions by four or fewer major traders in the Comex silver market. On the suspicion that Scotiabank, one of Canada's largest banks which has been an active participant in precious metals trading, may have been a holder of a large silver short position on the Comex, silver analyst Ted Butler started a writing campaign to ask Scotiabank about this.

Unlike the Commodities Futures Trading Commission (CFTC) and the Comex, which refused so far to answer Butler's inquiries about silver, Scotiabank did reply a few weeks ago.

However, the letter was not completely illuminating. The letter did not deny that Scotiabank was one of the major holders of silver short positions on the Comex. Instead, it said that the bank did buy long and sell short silver and that if the Scotiabank did have this huge short position on the Comex, that it was offset by hedges elsewhere.

It may be just a coincidence, but in the few weeks since Scotiabank released this letter, about 50 million ounces of these huge silver short positions were closed out.

It may have been simply opportune purchases at a temporary low silver price by any trader.

Or it is possible that Scotiabank may be one of these four or fewer traders with a huge short position in Comex silver, where top bank officials have become uncomfortable that a scandal might break over this minor bank activity that could tarnish the reputation of the entire bank. If this is so, and this is speculation, there would be a major incentive for Scotiabank to quickly close out their silver short positions on the Comex.

4) Even the highest quality corporate debt is facing potential problems. Today's *Wall Street* Journal reports on the risks to Citigroup of financial "conduits" and Structured Investment Vehicles (SIVs) that are assets not even reflected as part of the bank's assets.

These conduits and SIVs include some of the best quality commercial paper. They are set up as separate entities from the bank in order to allow the bank to show more attractive operating ratios.

In a letter to their investors last month, Citigroup revealed that it managed or was affiliated with a total of $177 billion of conduits and SIVs.

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There seems to be little risk of default by the creditors of such debt. Instead, the greatest risk may be that investors will close out their positions in these funds. If the debtors are forced to liquidate assets to repay maturing debt that isn't rolling over, the value of such companies could decline.

In order to keep them off Citigroup's books, these conduits and SIVs designate that outside investors suffer the first layer of losses, should they occur. If they suffer more than minimal losses, however, then Citigroup would be on the hook.

At this point, it is entirely speculative, but if a conduit or SIV were to fail, that would scarce investors away from other conduits and SIVs. Alternatively, if Citigroup were to rescue one from failure, that would indicate that all of these really belong on Citigroup's financial statements.

5) Here at LCS, demand for gold, silver, platinum, and rare coins has soared since mid-August. Part of the reason is no doubt from the temporary dip in prices. But we have also seen a surprising increase in the number of first-time customers who express unease at the world financial and currency markets.

6) In recent years, homeowners have been adding an average of $800 billion annually to their home equity lines of credit, much of which has been used to finance consumer purchases. In 2007, it looks like this increase will be about 2/3 lower than that figure, which means much less consumer spending (i.e. lower demand for goods and services) and lower employment.

What This Liquidity Crisis Means To You

As I have warned you for several months, the paper asset markets are quickly becoming more unstable and risky.

Since the European Central Bank and Federal Reserve Bank mobilized almost a half trillion dollars in August, with little to show for it, how much more can they do in September?

When markets become more uncertain, investors flee to safety. The sharp decline in loans to the private sector and increase in demand for U.S. Treasury debt is one example of this investor shift.

However, investors are also shifting an increasing amount of their net worth out of paper assets and into tangible assets such as gold and silver.

The U.S. dollar will probably do worse than the Euro, yen, and other currencies because the U.S. economy is already strained by the huge budget and trade deficits, cost of the Afghanistan and Iraq programs, and the weak housing market.

It seems clear to me that the paper asset liquidity crisis is going to clobber all currencies to some degree, because they are ultimately not backed by anything more than the promises of politicians.

So, I don't recommend jumping out of the dollar to any other particular currency, though there might be a case for doing so on a short-term basis.

A few months ago, I predicted that the U.S. dollar will fail sometime between 2009 and 2014. The financial turmoil now wracking the markets is exactly what would be happening if my forecast were to come to pass.

The bottom line is to own assets that are not someone else's liability. Historically, gold and silver have been the ultimate refuge of investors seeking safety. Although technology has advanced a long ways over the centuries, the reasons to own physical gold and silver are still applicable.

How Much Hard Assets Should You Hold?

I used to recommend that holding 5-10% of your net worth in hard assets such as gold, silver, and rare coins was a prudent conservative allocation as insurance against calamities that might wreak havoc with the value of your paper assets.

A few months ago, I raised my recommendation to 20% of your net worth.

Now I think even 25% of your net worth is reasonable.

It is relatively easy to compute your net worth. First, add up the total of your assets. Second, total up your liabilities, including any consumer debt that might have deferred payment terms. Third, subtract your liabilities from your assets to get your net worth.

Once you have your net worth, multiply that by the percentage you want to allocate to hard assets. Then compare this total against the value of your current hard asset holdings.

If you need to acquire additional gold, silver, or rare coins, please give us a call.

Which Hard Assets Should You Own?

It is one thing to decide conceptually that you should own some hard assets. The next questions are what kinds and how much of each should you own?

There is no one-size-fits-all answer to these questions. But here are my ideas.

The three main categories are gold bullion -priced items, silver bullion-priced items, and numismatic coins.

Some would want to include platinum and palladium. I do not recommend them as they are either markets where new supplies exceed demand or at least there are no long-term shortages as there are with gold or silver.

Summary Of Current LCS Recommendations For Precious Metals and Rare Coins

How much to allocate for each category of precious metals and rare coins?*

	Conservative	Moderate	Aggressive
Gold	45%	35%	25%
Silver	55%	55%	50%
Rare Coins	0%	10%	25%
TOTAL	100%	100%	100%

*Platinum and palladium both have volatile markets with long-term supply/demand fundamentals that are not as attractive as those for gold, silver or rare coins. While either or both might outperform gold, silver or rare coins in the short- to long-term, to be conservative we have omitted them from our allocation.

Gold bullion includes coins and ingots that trade on the basis of their intrinsic gold value. Silver bullion includes coins and ingots that trade on the basis of their intrinsic silver value.

Numismatic coins are those where you have to pay a significant collector premium above the metal value. In some instances, these coins might be available for close enough to metal value that they can be considered almost bullion (common U.S. $20.00 Double Eagles being a good example). Other coins have little or no precious metal content, so that the value is determined solely on collectible factors.

Gold is attractive because it is overwhelmingly a financial asset. Around the world for the past 6,000 years, gold is money. There are about 5 billion ounces of gold extant, about 80% held in private hands and the balance by governments, central banks, and official agencies. At current levels, that is about a $17 trillion potential market.

Gold is globally traded (although less so in the U.S. because it was largely illegal to own from 1933 to 1974) and highly liquid. Ordinarily, I would recommend that most of your hard assets be in gold.

However, I am more in favor of silver because 1) the fundament long-term supply shortage is more acute, 2) it is a smaller market than gold which gives it greater volatility on upside (and downside) than gold, and 3) ongoing research is finding ever more industrial applications that take advantage of its much lower cost and the fact that it can be used in small quantities for most purposes. In past booms, the price of silver has outperformed gold by far. I expect it to continue to do so. As a result, I favor silver bullion at about 55-67% of the amount you allocate between gold and silver.

Rare coins have greater potential appreciation for either gold or silver, but that also

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entails greater risk of loss. You have to be more careful to select the right coins, be careful about the quality, and buy them when they are more attractive values. Buy and sell spreads are wider than for bullion items. Because of the greater risk, conservative buyers may not find numismatic coins at all suitable. Even the most aggressive buyers should limit rare coins to 25% of their hard assets.

See the summary of recommendations at the top of the previous page.

Gold and Gold Coins

Gold settled today at $681.50, up $7.00 (1.0%) from four weeks ago.

Not only is the spot price of gold higher, but strong demand for physical gold has driven up premiums on many bullion-priced coins and ingots.

The low premium best buys continue to be the Austria **100 Corona** (3.1%), South Africa **Krugerrand** (3.2%), U.S. **American Arts Medallion** (3.2%), and Mexico **50 Peso** (3.2%). With higher premiums, they are now costing your $1-2 more above spot than they did last month

The British **Sovereign** (6.1%) has a lower premium for a smaller coin and may be the world's most widely traded gold coin.

Last month, I alerted you that supplies of **Common-Date U.S. Gold Double Eagles** were declining, and to expect higher prices. That has happened. We are also starting to see higher prices for the smaller gold coins.

As a result of this stronger demand, the demand for **Better-Date U.S. Gold Coins** is even stronger, if that can seems possible. Prices are up on several issues since the start of the year.

We have been aggressively seeking such coins, but can only find an odd piece here and there. For your benefit, we have decided to offer our entire inventory of **Better-Date U.S. $20.00 St Gaudens** now, before prices might go up further. See our enclosed offer for details.

The Month

Gold Range	34.00	5.0%
Net Change	+7.00	
Silver Range	1.57	12.0%
Net Change	-.94	
Gold/Silver Ratio	56.0	
Net change	+4.6	
Platinum Range	43.00	3.5%
Net Change	-8.00	
Platinum/Gold Ratio	1.86	

Date	Gold	Silver	Platinum
Aug 08	674.50	13.12	1,273.00
Aug 09	661.25	12.66	1,258.00
Aug 10	671.00	12.82	1,265.00
Aug 13	669.25	12.81	1,272.00
Aug 14	668.50	12.71	1,264.00
Aug 15	669.00	12.52	1,260.00
Aug 16	648.50	11.65	1,234.00
Aug 17	658.50	11.81	1,230.00
Aug 20	657.50	11.75	1,241.00
Aug 21	658.00	11.55	1,238.00
Aug 22	661.00	11.61	1,238.00
Aug 23	660.00	11.62	1,234.00
Aug 24	668.00	11.93	1,238.00
Aug 27	667.00	11.75	1,244.00
Aug 28	664.50	11.77	1,248.00
Aug 29	666.25	11.84	1,258.00
Aug 30	665.00	11.79	1,254.00
Aug 31	672.75	12.03	1,262.00
Sep 03	closed		
Sep 04	682.50	12.27	1,265.00
Sep 05	681.50	12.18	1,265.00

London Silver Market Premium To New York Silver Market = 3¢

Gold, silver and platinum quotes are working spots at 1:45 EST/EDT each day, quoted in U.S. dollars per troy ounce.

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Silver and Silver Coins

Silver finished today at $12.18 down a whopping 94 cents (7.2%) from last month.

As the price of silver slid into the $11s in mid-August, demand zoomed. Supplies vanished almost instantly.

As a result, premiums jumped on almost all forms of lower premium bullion-priced silver. Last month, you could buy bags of U.S. **90% Silver Coin** (1.5%) for five cents an ounce over spot. Even though premiums are not as high as two weeks ago, now that silver is back over $12.00, you still have to pay 18 cents an ounce above silver value for bags of 90% Coin.

Supplies of physical silver have gotten much tighter in the past few weeks. If you are looking to acquire a sizeable quantity of **100, 10, or1 Ounce Ingots** (4.9-5.7%), you just might have to wait two weeks or so for delivery.

Compounding problems with the silver market was the death in a car crash of the owner of a major Midwest bullion wholesaler in mid-August. A number of dealers have contacted LCS to encourage us to help fill the void. We are likely to do a little more wholesale trading as a result, but we simply do not have the physical space available to add staff for a major effort.

As with rare gold coins, supplies of many silver numismatic coins are drying up. Still, we were fortunate to make two modest interesting purchases: **Gem Mint State 1903 Morgan Dollars** and **Gem Mint State-65 Full Bell Line 1963-D Franklin Half Dollars**. The latter coin, while considered common in average Mint State condition, is surprisingly scarce in a well-struck high grade.

Contact LCS Promptly In Event Of Delivery Problems

LCS uses registered mail service at the post office to deliver almost all of our retail customer purchases. The track record is good, with about one package being lost every three years.

A few months ago, a registered package going to a customer was on a mail truck involved in a major accident. As a result of this accident, the package broke open and a handful of silver coins disappeared.

The purchaser took it upon himself to file the claim with the post office. We are not sure of all the details, but the claim was denied, whereupon he contacted LCS.

It is likely that if the customer had contacted us so that we could have filed the claim, it may have been paid.

The normal situation is that the post office pays LCS for a claim, whereupon we complete or replace the customer's order. LCS Office Manager Barb Robinson worked for the post office in years past and has more familiarity with how to submit the necessary paperwork to expedite a claim.

Although the odds are that it will never happen to you, please remember to contact us promptly if you receive a package that is not intact and may have suffered some losses or damage.

Please Be Patient Calling Us

With soaring activity over the past few weeks, we have had some difficulties answering all telephone calls. We are trying to handle the volume, but ask you to please be patient and give us one or two more rings before hanging up.

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