

A Plunge into a Monetary No Man's Land

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The question keeps swirling around regarding the Fed and just how much Treasury paper they can buy from the market under current rules. Our guess is about \$1.7 trillion. A good part of that may well be in notes, which will probably keep long dated rates low. On the other hand they may increase the current limit, and buy everything in sight.

That probably means the 10-year T-note could fall from its current level of 2.50% yield to 1.5% yield and mortgages, as we stated before could fall to 3.38% on the 30-year fixed rate loan. This kind of spirited buying would tend to crowd out other buyers forcing them into corporates, foreign bonds, commodities and gold and silver, as well as back into the stock market. This kind of policy means major monetization, higher inflation and perhaps eventually into hyperinflation. Needless to say, this is a very dangerous game.

A plunge into a monetary no man's land. The liquidity that will be set loose in the POMO market will be enormous and the avalanche will begin early next year and it will cause asset price inflation. These antics will also suppress the value of the dollar forcing a test of 71.18 and perhaps breaking that long-term support level.

Bank reserve liquidity will likely surge to \$3 trillion. Will the banks aggressively lend or will borrowers balk due to such unusual conditions? That also means the Fed balance sheet could reach \$4 trillion. Then the question arises, if this doesn't kick start a recovery can QE3 be kicked up to \$8 trillion? What will inflation be like under QE2? Will it be 14% or 34%? Will hyperinflation begin, or will that be left to the duration of QE3? We do not have all those answers, but we are entering very dangerous territory.

In reaction to this massive monetary onslaught the dollar will fall, the stock market will hold its own, the Treasury-Agency markets will remain relatively unchanged, commodities will rise and gold and silver will increase in value exponentially. All the funds created have to have someplace to go and it certainly won't be into real estate with its massive inventory overhang in spite of historically low interest rates. Once in place, whether it is QE2 or QE3, the time frame will be squeezed probably into a 3-year window, or less. The election may change the makeup of Congress and the Senate, but the Fed's direction is set. They have no other choice other than what they are doing to extend the time line of collapse. These policies won't work and all the elitists are aware of that. Within three years we should have a crunching deflationary collapse. Interest rates would rise and bonds fall, the stock market would collapse, commodities would hold their own or perhaps give up some gains and gold and silver being the only remaining real money would hold their own or move higher. We might add that the LBMA, Comex and GLD and SLV would have long before collapsed. Confidence in the system will have been crushed.

As far as Fed exit strategy is concerned there is none. There can be none.

Bonds, those instruments of guaranteed confiscation, are certainly not the place to be. Total return before inflation is dreadful. After real inflation it's horrible. Even the market has done better and commodities, gold and silver are up more than 20%.

The Fed has become the country's lifeline and we find that deeply disturbing inasmuch as it was the Fed that is responsible for the current position we are in. Our latest look shows the Fed now the second largest owner of US Treasuries. Last week they overtook Japan to place second behind China. Of course, this is madness, but if foreigners are unwilling to buy and the Fed has to buy to keep interest rates low, they have to be the buyers of last resort. This policy began in June unbeknownst to most and has precipitated the slide in the value of the dollar and has heightened the flight into gold, silver and commodities.

The question now is can the Fed do this indefinitely and how high will inflation go as a result of such a policy? Trillions of dollars of old debt is coming due with some \$150 billion in new debt monthly. Each month that debt grows exponentially far into the future. Capsulating the debt spiral we can come to no other conclusion than there is going to eventually be a default, which will be preceded by hyperinflation. That is when the public no longer has confidence in the currency and abandons it by using it as soon as it comes into their possession. This is where we are eventually headed. The timing is difficult because we do not know when the major nations will finally capitulate. The past week we heard comments from Brazil regarding the possibility of a meeting similar to the Plaza Accord meetings of 1985, in order to address the growing currency war and the failure of the US dollar. We predicted such an event this past May and thought that this could come about by the end of the year or early next year. We thought it could be overridden by QE2 that could have been underway in June and July. That did happen via the repo market and some bank lending, but not nearly enough to keep the system moving parallel.

The result has been stagnation, higher inflation and unemployment and the Fed forcibly being thrust into the treasury and Agency markets, as buyers of last resort. What is really distasteful about all this is that the Fed continues to lie about what they are really up to. That in part is why it is easy for the Fed to elevate the stock market in anticipation of the November election. The reaction to that has been a very powerful gold, silver and commodities markets.

The financial regulation, the Dodd-Frank bill, failed to stop some of the worst excesses in structured assets and derivatives; an area that is essentially unregulated. In order for banks and securities firms to pull in more profits they are being encouraged to commit financial fraud and not be subject to regulations.

Little or nothing was done about derivatives and that is where the trouble also lies, as well as in structured assets based upon corporate and Treasury debt. These are being sold to retail clients based on higher yields, which also involves subprime debt and auction rate securities. You would think these fools would have learned something after watching the terrible losses of the past few years. Obviously not, they are determined to lose their investments. That brings us back to our old adage, never, ever, ever chase a yield, it can

only end in losses. Worse yet, there are no real after markets in these securities. You are at the mercy of the seller. Another problem is that the regulators do not even know this is going on. That is understandable. If you file a formal complaint concerning naked short selling they are abusive and ignore you. This follows the arrogance of the Fed and the SEC to listen to warnings from the financial communities that subprime mortgages; ABS, MBS and CDOs were toxic bombs about to explode. They as well refused to look into the legalistics of the mortgages, the packaging of the bonds and the obvious phony rating systems proffered by S&P, Fitch and Moody's. Worse yet, they have for the past few years been guaranteeing the mortgages via Fannie Mae, Freddie Mac, Ginnie Mae and FHA that started the problems in the first place.

These results are not the result of stupidity, incompetence or arrogance. It was planned that way. This is your government and the privately owned Fed at work.

The net short position in the Commitment of Traders report of commercials hit a new high this past week, that is over 308,000 contracts, all of which we believe are in a losing position. The situation in the gold and silver shares is similar. In times past such a large net short position has been intimidating and often led to a breakdown in gold prices. Not this time. We saw a one-day correction and that we believe is it. Money and credit are expanding at a furious clip, economic policy is dreadful and we just saw ¾'s of the administrations financial complement abandon ship. The lone important survivor is Tim Geithner, who is incompetent and cannot properly file his income tax. The dollar remains under pressure versus other major currencies, and all currencies are lower versus gold. The euro is under terrible pressure as is the entire EU. All nations to various degrees are increasing money supply at a rate of plus 10%. As we have stated so often production of gold and silver have been declining for years with no new large projects in sight. We have strong gold and silver markets for the next almost five months. We now have China as a major buying factor in the market along with Russia and traditional India.

The last two option expirations were non-events and that may continue. It is everything that shouldn't be. Lo and behold, central banks have become gold buyers not sellers and the European control banks have sold virtually nothing for two years. We might ask the US where is Germany's gold. Zero interest rates have made it much less expensive for players to be long gold and silver. Inflation has been cranked up and should reach 14% by the end of 2011. Commodities are again going through the roof. Inflation, real inflation, is already at 7%, not the 1.6% the government feeds us. The dollar's reverse head and shoulders pattern is looking ominous. The government has lost control of their gold price suppression and they are losing control of the economy. Within the next two years it will be a disaster for the world economy.

One of the very important aspects as a result of the strength of gold is the geopolitical implications. We have Russia, China and the rest of the BRIC nations lined up on one side and the US, and Europe lined up on the other. Not only are they accumulating gold in a big way but they seem to be telling us that there is no US gold in Fort Knox, under the Fed in NYC or in West Point, and what gold is there belongs to other parties. We'll find out in time, but is that really good enough. As Ron Paul says let's finally audit the Fed. It has been 56 years since an audit has been done. As a result there are going to be economic, financial, and political ramifications from the stockpiling and price of gold, if in fact the US doesn't

have any or has very little left. Government and those who control it have lied for years, so what makes one think it will be any different this time. If these BRIC nations continue to accumulate gold and the West doesn't we are in for some ferocious problems, if we have little or no gold. The official holdings of these BRIC nations is declared at about 10% of what the US, UK and Europe has, but because of past experiences we believe it is closer to 15%.

No one really knows what western central bank gold holdings are, because they have been shrouded in secrecy, leased and held on the books as still existing and the lies about what they have are legend. The central bankers only think that they have a need to know. Even the Fed has used millions of taxpayer dollars buying off Congress, so that the gold hoard will not be audited. As a result for the past dozen years we have had an evolving financial, currency and free trade war on our hands. They all are part of the same problem and strategic planners do not know how to solve the dilemma. The options opened to the West are no longer there because they are broke and all have a financial Ponzi scheme going via their central banks. The opposing players know that. Each day that passes sees less US dollar denominated paper being purchased. This is why it has been important for Western central banks to control gold prices. They stupidly have allowed buyers, such as the BRIC nations, to buy gold for 30% of what it should be selling for. At the same time their suppression program has had very limited success over the past 15 years. Gold moved from \$252 to \$1,350 over that period. Over the last nine years it has risen almost 20% annually on a compound basis.

Russia has been a persistent gold buyer both of domestic production and in world markets. China has bought domestic production, but has not been aggressive as Russia in world markets, choosing a subtle market approach. We believe China will have to become much more progressive in the markets as their dollar holding rise, unless of course, there is a third world war. It is not difficult for China to use intermediaries to buy, as they have done in the past. China strongly markets both gold and silver to its citizens particularly in exchange for dollars. As a result of this Chinese approach, the overall BRIC approach and buying by the rest of the world, control of gold trading will soon be at an end. You might say how do we know this? It is a good question. Markets are not scientific they are an art form and we have been deeply involved in this gold and silver venue for over 50 years. As time passed you know what to look for and what to expect. That is how we project what should happen. The long study of finance, monetary policy and the desire for total world control have allowed us to back into what we believe will happen. For the past 21 years we have done that and have been right 98% of the time. Consequently we have an excellent opportunity of continuing to be correct.

The bankers, Wall Street and the City of London have lost and they know it. Talk radio and the Internet have exposed what they are up to worldwide and there is no way for them to stop it short of a revolution or WWIII. The time has passed for them to successfully pull off such a diversion and get away with or survive. They have craftily interconnected just about everything. Gold has again become the ultimate currency and anything to disrupt gold's position would now bring down the entire financial system worldwide. The bottom line is if you do not own gold and silver coins, bullion and shares you are a fool. Both metals are headed considerably higher and there is no changing that.

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