

The Best Gold Interview of 2010

Dear Reader,

We have something a little different but very special for you today. Jeff Clark, senior editor of our Casey's Gold & Resource Report, recently sat down with an industry insider to talk about the gold and silver supply. The insight gleaned is something every investor should know – even if you're not currently positioned in precious metals.

Here's the interview in its entirety.

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Jeff Clark, Casey's Gold & Resource Report

Much of what passes for “insider” information these days is often conspiracy-edged or largely conjecture. True inside information is actually hard to come by. So what follows is the refreshingly candid and uncut version of my talk with a first-hand participant in the murky and little-understood world of gold bullion, mints, and bullion dealers.

Customarily, when considering a company for a potential recommendation, I hold a series of discussions with management. It was during one of these vetting procedures that I spoke with Andy Schectman of Miles Franklin – and heard some disturbing reports about supply that every investor should know. Andy is a bullion seller, so you're welcome to take his comments with a grain of salt. On the other hand, what he sees week after week and what he hears from his high-level industry contacts might just make you pull back on that salt shaker and re-inventory the number of ounces you own...

Jeff Clark: Andy, tell us about the kinds of contacts you have in the industry and where you get your information.

Andy: I'm associated with two of the six primary mint distributors in the United States. There are only six primary precious metal distributors here because the qualifications are very difficult to meet. Aside from having \$100 million in annual sales, you have to extend a \$50 million line of credit to the U.S. Mint, and very few companies can do that. So in working with these companies, I'm privy to information that many others aren't.

Jeff: So, what have you been hearing from them about supply for physical gold and silver?

Andy: I think in order to properly characterize what's happening in the industry, it's important to start from a big-picture perspective, which is that by and large the masses in

this country are not involved in precious metals. In my experience, the move we've seen in gold over the last decade has primarily been from international investment – sovereign wealth funds in the Orient, petrodollars in the Middle East, India buying from the IMF, Russia and Japan accumulating, etc.

Most U.S. investors have lived through nothing but prosperity and good times, where they perhaps didn't think they needed to own gold – but I think the rest of the world isn't as optimistic about the future. So when you talk about supply, it's important to acknowledge that most people in this country don't own any gold and silver. To me, that's what should really alarm people.

Jeff: Tell us how you would characterize supply right now.

Andy: Fragile. Availability of product changes almost weekly.

But it's worse than that. When the market plunged 1,000 points in one day last month, two German banks bought about 35,000 or 40,000 one-ounce coins and cleaned out the Royal Canadian Mint overnight. Think about that: two banks cleaned out one of the world's preeminent mints in one day.

Then you have the Austrian Mint recently announcing they were running into supply issues. And the U.S. Mint has been the model of inefficiency for the last several years. They have been either reluctant or unable to meet demand when it comes to Gold Buffalos, Platinum Eagles, and fractional Gold Eagles. They issue dribs and drabs of them, but certainly not enough to meet demand.

Jeff: And they frequently run out.

Andy: They frequently run out, they frequently have delivery delays, and it's a situation where very quickly we could see major disruption in the supply chain.

Jeff: We saw supply constraint in 2008, where dealers were running out of product. Do you think we're headed there again?

Andy: I do. In 2008, when gold dropped from \$1,000 to \$700 very quickly, all product worldwide disappeared. Within weeks the U.S. Mint was shut down. The Canadian, Austrian, and Australian Mints were all eight to 12 weeks back-ordered or shut down. The Australian Mint stopped taking any new orders in July or August for the rest of the year. The Rand Mint, for the first time ever, sold out of all its product. One wealthy Swiss businessman flew his own 747 there and cleaned them out.

So product was impossible to get, but not just from the primary mints; even the refiners that made 100-ounce silver bars couldn't get them. No one could get anything, and it was a very scary time if you owned a gold company. There were many days I sat at my desk wondering how I was going to get product tomorrow, and there were times we couldn't take orders whatsoever. And that comes from a company that's done over \$100 million in sales, is a member of the certified exchange, and that has contacts that run very deep in the industry – and I couldn't get anything.

A friend of mine who owns a very prominent gold and silver company in Colorado has a store front, and back then he told me, "I want to put a sign on my window that says, 'All we do is buy, we don't sell,' because one person will come in there and clean me out and there's nothing to be had."

So what I think is ahead comes from that experience. If you factor in that very, very few people in this country have even held a gold coin – let alone own any gold, or understand the reasons to own it, or will even accept the arguments for owning it – I think the primary distinguishing characteristic of this market will be that people won't be able to get product when they want it. The rising price in and of itself will not be the main hurdle. For the most part, people will overcome price, because they'll want to own it. The real issue will be getting product in a timely fashion, and that will become difficult for the average American.

Jeff: What about supply from those selling coins and bars who bought at lower levels? Doesn't that increase the available supply?

Andy: This is what I believe is a distinguishing feature of this market: there is a total absence of a secondary market. There isn't one. Period. In years past, we used to do a lot of business with people wanting to sell. Today, virtually no one is selling their coins back to us. In fact, for every 100 transactions we have, maybe one is a seller – the other 99 are buyers. Our largest supplier, who provides over 60% of all bullion to the U.S. market, told me earlier this month they have days without one single buy back. And this is from the largest supplier in the U.S.

Jeff: Why do you think no one's selling?

Andy: People are afraid. They're afraid of what's happening geopolitically, economically, fiscally, and want to hold on to their gold. As they should, because this is exactly the kind of circumstance gold is for.

So I would argue that as gold and silver creep higher, there will be more and more buying and less and less selling. And less selling means less product for buyers.

When you look at the fact that there is no secondary market, and then you throw into the mix that the mints are already running into production problems, and then add the troubles in Europe, which could easily spread, I think it's easy to see how demand could outstrip supply. I assure you, there's an awful lot of gold acquisition going on in other countries – the Swiss and Germans, for example, see the handwriting on the wall. They were buying everything up when the European crisis broke. It was bedlam for awhile.

And if all of a sudden people here wake up and feel they really need to own gold but can't get it, we'll be right back where we were in 2008.

But to your point, yes, nobody is selling anything right now and almost anything you buy will be dated 2010. That's because there are no backdated coins to be had virtually anywhere. Maybe 20 here or 50 there, but nothing on a meaningful basis.

Jeff: It sounds like regardless of what's going on in America, global supply could be in jeopardy if this trend continues.

Andy: Absolutely, especially with the fact that there is no secondary market. Really, the people who enter the game late are going to be at the mercy of the mints. And if the mints run out of supply, or just stopped selling for whatever reason, it's "game over" for those who want to accumulate. Right now there's as good a supply as I've seen in a couple years, and that's at a time when we've already witnessed the Royal Canadian Mint running out of gold for a week or so, the Austrian Mint also running out of product, and the U.S. Mint rationing Silver Eagles for a short time.

Jeff: And you're calling this a good supply market?

Andy: Yes. It's as good as we've seen in a couple years.

Jeff: That's scary.

Andy: I don't think you're exaggerating by saying that. And the message is, "Buy now while it's still available." I know it may sound like I'm trying to sensationalize it, but I'm really not. Based on what I know, it's my opinion that if 5% of this country put 5% of their money into gold, there would be nothing left tomorrow morning. Supply is that small compared to the tremendous amount of money that's out there.

Here's another example. I had a meeting with a money management company here in Minneapolis that manages some of the oldest money in the entire country, literally billions of dollars. And when I spoke with them, I discovered the principals of the firm had never held a gold coin. They asked me questions that were as rudimentary as what I would get from a complete novice. By the end of the conversation, they said they would

start with a \$5 million order. I later learned this was a small order for just one of their clients. It was just dipping a toe in the water for these people.

Well, it won't take too many of these kinds of people waking up to gold to drain the supply chain. Most of the wealth in this country is driven through money managers, and at some point these people will tell their managers, "I don't care what the price or premium is, get me gold." When they come knocking in large numbers like that, the supply chain will dry up overnight. I know this to be true. If we see an event that drives money managers to buy physical gold, the supply will be gone.

Jeff: Some of that money is already going into the ETFs.

Andy: Yes, but not when you consider the total capital that's available. And keep in mind that the prospectus for GLD and SLV state that, more or less, you can't take possession of the metal. So, do you "own" gold if you have shares in GLD or SLV, or any ETF, for that matter? If you can't put the coin or bar in the palm of your hand, the answer is no.

Jeff: Are you seeing any difference between gold and silver? Is one more difficult to come by than the other?

Andy: We've seen a lot of demand for silver, probably more so than gold, and the U.S. Mint has already rationed Silver Eagles once this year. Junk silver bags are becoming much harder to get. And I think the higher gold goes, the faster silver will disappear. At some point the American public will realize they should have some gold and silver, and we could see a situation where the gold price could get out of reach for some investors. Those people will turn to silver and, as a result, it will probably be tougher to get than gold.

Jeff: If supply gets scarce, do you expect premiums to shoot up?

Andy: Absolutely. In 2008 the premiums were astronomical. Silver Eagles were \$5.50 to \$6 over spot. Gold Eagles were \$100 to \$150 over spot. The premiums went parabolic. That could easily happen again.

Jeff: And that was due to constrained supply.

Andy: Yes. When the price fell off the table, everything disappeared quickly. That's counterintuitive, I know, because logic would dictate that as the price of something falls, demand is waning. But as the price fell, I think it became more attractive to large interests around the world, and everything got gobbled up fast.

Looking ahead, I can tell you that the only way you'll see premiums stay where they are is if the mints are able to keep up with demand, and based on what I see I would argue there is no way they can. They can't even keep up now. On top of that, as I stated, people aren't going to sell their gold this time unless they absolutely have to, so there won't be any supply coming from sales.

Jeff: So your message to someone who owns little or no physical metal now is what?

Andy: Acquire as many gold and silver ounces as you can. In the end it's not about price paid, it's about number of ounces. View the supply issue as critically as you would the price, because I believe that more than anything else, the lack of available supply will mark this industry.

Jeff: Excellent advice, Andy. Thanks for your input.