The Gold Standard

The journal of The Gold Standard Institute

The purpose of The Gold Standard Institute is to promote an unadulterated Gold Standard.

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Editorial

Belief and Logic

Galileo Galilee was the last of Florence's Renaissance Men. Amongst his inventions was the telescope. He convincingly (and bravely) demonstrated in his 17th century book 'The Dialogue' that, contrary to Church teachings, the heavens were heliocentric, not geocentric.

> *"I do not believe that the same god that endowed us with senses, reason and intellect has intended us to forgo their use."* Galileo

As Galileo had feared, instead of welcoming the articulation of this important and wonderful truth, Pope Urban VIII ordered a trial – in the original meaning of the word. Galileo was tortured until he publicly denied that which he knew to be true. The great genius was then confined to his house until he died, a broken man. Grand Duke Ferdinando II, Galileo's Medici sponsor, under threat of similar treatment, was forced to cease his patronage and forbidden to accord Galileo respect, even in death.

The first record of someone proposing heliocentrism was Aristarchus of Samos circa 260BC. He was largely ignored, as was Copernicus who reintroduced the idea in the 16th century.

The Church continued to enforce the geocentric theory formulated by Ptolemy and supported by Thomas Aquinas; the latter explained the movement of the heavenly bodies as being caused by angels.

The 18th century Enlightenment, known for its reason and individualism (the century of lights), began with great optimism around the turn of the century. The lights were extinguished by the French Revolution of 1789. People are passionate about beliefs. Reason and logic? Not so much.

In the 21st century, we discovered that, contrary to thousands of years of belief, our advanced societies owed their creation and continuance to individual freedom and the circulation of Gold, not to ruling pooh-bahs and their central planners.

The Earth revolves around the Sun, and societies revolve around Gold. Human societies are chrysocentric[1].

It is the failure to act upon this or, in most cases, to even understand it, that is edging humanity back to the primitive existence that was its lot for so many millennia.

When logic collides with belief, logic is still either ignored or put to trial, though these days it is usually trial by the media's red hot tongs. It would be prudent were we not take much longer to set aside today's tired old beliefs.

Philip Barton
President, Gold Standard Institute
Times of Gold

News

SNBCHF: Real vs Nominal Interest Rates

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BBC: A bit of discretion might have been wiser.

Tail Wags Dog

In my last articles we dug into the technicalities of Mengerian 'Marginalism'. We looked at the marginal productivity of labor, and the marginal productivity of capital; both topics important to an understanding of economics. Having gone 'rightward' into more details, we now turn 'leftward', to a larger picture overview of economics.

Indeed, we need to view the larger world situation beyond conventional 'economics', as economics has become inbred, tightly focused on finances, money, monetary policy, fiscal policy; the financial sector has become the proverbial tail that wags the dog.

In an honest, prosperous world finance supports the real economy, the physical economy; after all, one cannot eat Gold as we have surely heard often enough... and of course, neither can we eat paper promises. We need real

[1] From Latin chryso, from Greek khrusos – Gold

products from a real industrial/agricultural base to provide the essentials of life, and the luxuries that take life beyond survival.

As we saw in the last couple of articles, 'gambling', or what is today called speculation, has mostly replaced the real, physical economy; Wall Street has replaced Main Street... at least in the Western world. All the 'dirty, polluting' smokestack industries... except perhaps the military... have been sent over to China and India.

In the meantime, the Western world led... or more accurately coerced... by Washington has focused on money supply, on derivatives, forex futures, interest rates futures, stock markets, stock options, bond markets, NIRP, ZIRP; focused on the financial tail.

Now one truism for success in anything is to simply 'do more of what works and less of what doesn't'. This truism is of course too simple to be accepted by the 'intelligentsia'. As Mr. Bernanke so famously put it, if you don't hold a doctorate... or at least a masters... in economics, we won't even talk to you.

Really! We need a post grad degree to understand that doing more of what works and less of that which doesn't work is the way to go? Bah. In fact, the so called 'intelligentsia' have not enough real intelligence to understand this truism... and that the bottom line is, do what works and avoid what does not work.

For a real world example, let's compare China to the West... the Chinese economy has achieved marvels; in a few decades, China has gone from desperate famine, to being the No. 1 economy in the world (measured by purchase power parity) and certainly No. 2 by any (Dollar equivalent) measure.

Those 'smoke stack' industries shipped to China must be doing something right. Maintaining double digit economic growth, moving 600 Million people from poverty to the middle class... the Chinese are indeed doing something right, and clearly are doing ever more of it. In the meantime in the West, the middle class is being destroyed; real wages are shrinking, and only the 0.01% benefits.

Forty million US residents are living in poverty, surviving on food stamps... and this number is growing daily. Infrastructure is falling apart; conservative estimates suggest that it would take ~1Trillion USD just to bring existing infrastructure up to par; never mind building new. In the meantime the military complex sucks up that very same 1 Trillion, yearly... and wastes it on war, aggression, regime change, on spreading mayhem. Just maybe, the West is doing something wrong... and should be doing less of it, not more.

So, what is China doing right, and what is the West doing wrong? Clearly, China is growing its real, physical economy... growing the dog, not the tail. Meanwhile, the West is focusing on the tail; the financial world... and allowing the real, physical economy to deteriorate. No savings, just borrowing and spending; while China has the one of the highest saving rates in the world... along with India, a country that is also starting to do more of what is right and less of what is wrong.

Now clearly if the world were on an unadulterated Gold standard, much of this problem would disappear. Zirp and Nirp would become impossible; speculation (gambling) in Forex and interest rates would disappear and would be replaced by emphasis on the physical economy... but to get to that point, much needs to change; especially people's perception must change.

The world must realize that we need to do what works, not do what does not work. After all, when the US was on a Gold standard... even an adulterated one... in the nineteenth century, the US economy grew at a world record pace; the pace that the Chinese economy is growing at now, the pace that the Indian economy is approaching.

Real world examples abound, if we but look and see; the US economy is 70% dependent on consumer spending; so what does the 'intelligentsia' do? Work to stimulate even more consumer spending! What utter insanity. Consumer spending is not the driver of an economy; capital spending is... spending on productive goods.

If you buy a car for personal use, on credit, that is consumer spending; the car payments come from other sources of income. If you buy the same car, but use it as a taxi, this is capital investment; the car will pay for itself, the debt incurred is self-liquidating. This is not consumer spending.

More specifically, we should also differentiate capital investment; a taxi will last for maybe five or six years; short term. A factory will last for decades; medium term. A highway, railway, dam etc. will, with some upkeep, last for a century; indeed, aqueducts built in Roman times (two thousand years ago) are still in service. This is long term investment indeed. The initial cost has been amortized a hundred times over.

Guess what; China, and lately India, are investing big time in infrastructure; dams, water reservoirs, bridges, railways... such real physical entities will serve for generations, never mind the next quarter results. Do more of what works, and less of what doesn't.

Now understand, the politics of all this are another issue; the Chinese one party government is doing right things, but by no means am I suggesting the west needs to copy Chinese government structures; indeed, India has a more 'westernized' political system... but is still starting to do right things.

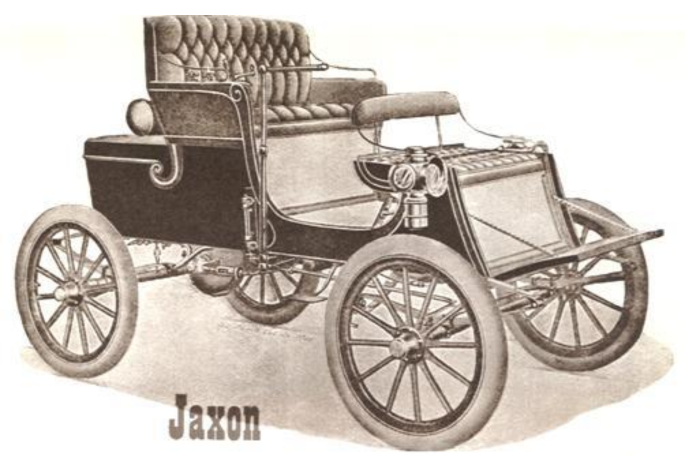
Mind you, the Chinese one party system is clearly stated; if Chinese policy is wrong, there is only one party to blame, the Chines Communist Party. In the USA, the one party (Demopublican) system is hidden behind a façade of 'democracy'; if a wrong policy is implemented by the Republicans, why simply blame them and vote for Democrats. Then when the Democrats continue with wrong policies, we can blame them and vote Republican... as if anything actually changed. So which system is more honest?

In any case, we need to start doing more of what works and less of what doesn't; we need to stop the tail wagging the dog... and soon. It is late in the game, and total economic meltdown is just around the corner... and such a meltdown is a big reason for wars to start. In today's nuclear age a major war would cause our extinction. Extinction is forever.

Rudy J. Fritsch

The Midas Conundrum

A review of Scott Sumner's treatise on gold's role in the Great Depression of the 1930s



This automobile is a 1903 Jaxon—a name more related to President Andrew Jackson than to me. When you examine a horseless carriage, its nature as an *integrated* system of mechanical, material, and chemical parts is easy to perceive. It's inspiring to learn that cars emerged in the course of one generation during the Golden Age of the industrial era.

Soon the War to End All Wars (1914-18) halted such civilized progress until the victors grudgingly converted *military* excess into an almost-as-deadly *economic* assault (1919-39) on the defeated nations. Car designs, of course, did not degrade in response. But the constriction of international trade changed the design trade-offs that determined how each side in the war could build their vehicles.

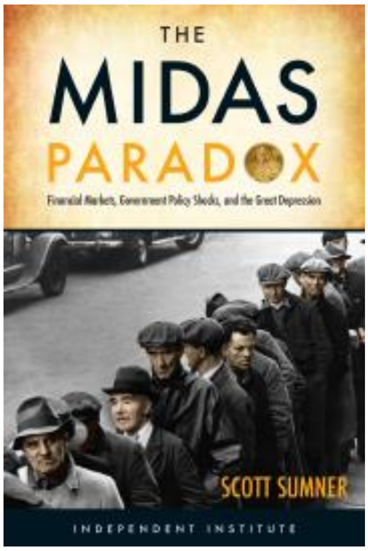
Unsafe At Any Speed

As an analogy, let's imagine a counterfactual fiction: *suppose* that Germany had been the primary manufacturer of spring steel needed for a car's suspension. In this parallel universe, the WWI Allies must make do without springs; they switch to tank treads and bigger balloon tires. In the punishing "peace" of the 1920s, German leaf springs might still be under-produced—subjected to arms controls and import quotas backed by patriotic bias of the victors. Perhaps the tidy automobile design of 1903 would morph into a meaner and rougher ride. Frenchmen might prefer jarring their bones with hardened wheels that survive poor road conditions while Americans risk a blow-out and subsequent crash asking rubber and air to do spring steel's job. Newspapers would debate inflation vs deflation and blame the rigid nature of wheels and uneven pavement. States would pass speed limits, impose load limits and over-tax their citizens to build over-designed roadways. Some cities build rail lines, centralizing and organizing to do without cars altogether. Self-defense advocates collect army-surplus tanks, but are prohibited from taking them to do their shopping by load limits on bridges and roadbeds, not to mention gun control laws. Perversely, spring-free design could be embraced without seditious questions yet with boundless unintended consequences.

Of course what's gone wrong is that this devolved auto has been handicapped by divisive politics. It's missing the subsystem which makes it flexible enough to ride on irregular roads at full speed. But instead of confronting engineering fact and overcoming their fear of German steel plants, everyone blames the *wheel* and forgets how cars worked just 15-20 years before. After all, who works on their own car these days?

That didn't happen. But something analogous did; it took just one Lost Generation to forget how the international gold standard had once worked.

Paradigm of the Paradox



So arose the dysfunctional world in which Scott Sumner's magnificent book "The Midas Paradox" has been set—one in which there is an international gold standard, but

> *"... there was no consensus as to what the rules of the game actually were. In a sense, the interwar gold standard was both too flexible and not flexible enough. A rigid adherence to a fixed gold reserve ratio would have greatly reduced central bank hoarding during the early 1930s. Alternatively, a much more flexible regime which completely disregarded the gold reserve ratio would have allowed central banks to more easily cooperate to economize on the demand for monetary gold during a deflationary crisis. Instead, there was enough flexibility to do a lot of damage, but not enough to easily repair that damage." [Kindle location 2960]*

The game's rules had *changed* in the trauma of the war years and through a post-traumatic resolve to not return to antebellum arrangements that had empowered the Axis. Sumner omits this larger context and accepts the prevailing taboos of his focus decade.

He avoids discussing the collapse of multilateral trade and the restructuring of the Fed's reserve assets by confining his primary sources to news accounts beginning around 1927—after those parts of the damage had been done. His analytic sources feature the half-dozen orthodox studies of the Depression proper: Keynes, Friedman & Schwartz, Eichengreen, Teman, Bernanke, and others interested in diagnosing the policy errors *within* the then-prevailing system. These sources: the daily flow of financial news, the statistical summaries, and the modern macroeconomic interpretations offer considerable insight into how laws, policies, actions, shocks, and the gold market's reaction to them contributed to a deflationary contraction of the world economy. No source, as far as I know, questions the premise that the game being played was still free and fair. They all know, as even Alan

Greenspan just acknowledged, that this was not the "gold standard from before 1913". And yet all gold standards somehow look equally intractable to a central planner.

Sumner's book, though handicapped by these paradigmatic blinders, at least starts to ask how *the system itself* may have been wrong, if not actually misbegotten. "Midas Paradox" explains how the economic car-without-springs—the gold standard without gold bills as its clearing house—was wrecked and discarded by central bankers licensed to drive it. To a New Austrian School reader it is annoyingly mute on why springs (gold bills as circulation credits and banking reserves) would have been such a bad thing. If the reserve ratio is the key to the problem, surely the capital structure of the reserve is worth studying. Gold bills were Germany's primary form of commercial credit. The German economy was the one most dependent upon them and upon the London banks which cleared bills in the prewar years. Indeed, DeutscheBank was founded by the Kaiser to strategically reduce Germany's dependence on foreign clearing. Bills' exclusion from postwar banking may have been just an irrational overreaction by vindictive and ignorant diplomats.

> *"[I]nterest rates (real or nominal) are simply not a very good indicator of the stance of monetary policy. During the Great Contraction it was central bank gold hoarding that best illustrated the contractionary stance of monetary policy." [Kindle location 2850]*

That the gold reserve ratios of the Allied countries diverged disastrously in the early '30s (France required new currency to be 100% backed by gold at a time when other central banks were cautiously dishoarding) should have raised the question of how such reserves had been constituted in the early '00s. How could a century old international standard suddenly be so discoordinated? Adding bullion to reserves decreases gold in circulation, but adding discounted gold bills to reserves increases the gold in circulation. It puts it to work in the economy where real merchants are risking their livelihoods to engage in commerce. Bills are the legally sanctioned reserve asset, unlike the government bonds which fund not-for-profit public goods.

I don't think Sumner's omission is intentionally driving bills down the memory hole; prime commercial bills are still central to our $1T money markets. But gold bills are seldom even taught as ancient history. Usually "the Real Bills Doctrine" is flippantly debunked by bond speculators and never examined by economics students. Sumner may yet give the subject proper consideration, if he can ever drop his policy-centric obsession.

> *" '[I]n the United States at certain dates in 1932 there was a . . . crisis of liquidation, when scarcely anyone could be induced to part with holdings of money on any reasonable terms.' (Keynes 1936 [1964], pp. 207–08) Keynes developed much of the General Theory in 1932 and 1933, and thus, it would not be surprising if the failed 1932 OMPs (open market purchases) were on his mind when he lost confidence in the efficacy of monetary policy during depressions." [Kindle location 2689]*

Sincere Praise Nonetheless

Sumner has written the most honest and excruciatingly detailed, New Keynesian, tour of the Great Depression. For financial news junkies this book is a Reader's Digest of the contemporaneous press. For gold standard advocates, it may be the first major book to treat the gold market as key to the puzzle (the paradox of Sumner's title), rather than as a convenient whipping boy. Sumner uses modern, non-academic, prose throughout. I found his macroeconomic reasoning counterintuitive in many cases, but I suspect conventionally schooled economists will not miss a beat.

Most importantly, the book is sincere in its search for the truth. It subjects the contemporary and retrospective analyses to modern tests of plausibility and relevance. Sumner's study of the original material clearly spanned more than a decade of careful research. His stature as an authority on these subjects will be nearly unassailable except versus his own efforts to improve, at which I hope he will persevere.

Why Sumner Matters

Scott Sumner hopes that the Fed will devote its open market operations to a market-guided program targeting a fixed growth rate of the nominal gross domestic product (NGDP). This approximates some of our New Austrian School economic goals—specifically that the supply of circulation credit should match the immediate needs of the core economy, no more or less. I've criticized his NGDPT proposal for its reliance on central banking, on unreliable, after-the-fact, government data sets, and for its assumption that countercyclical bond purchases/sales do, in fact, change the supply of credit to the core economy and alter its nominal pricing.

Nonetheless, Sumner receives good support and libertarian acclaim via Econlog and the Independent Institute. He cuts the profile of a young Alan Greenspan or Milton Friedman. Like them, if given policy-making power, he would use it vigorously instead of, ideally, trying to minimize coercion. Again and again his blogs and book bemoan the ways in which market realities make life inconvenient for those charged with directing policy.

> *"[P]olicymakers had no simple roadmap for stabilizing the economy in a world where financial markets were very sensitive to any suggestion of policies that might put the dollar under a cloud of suspicion." [Kindle location 2966]*

As if markets should just become disinterested in endogenous forces trying to sway them. They won't. They exist to extract profit from such forces to the maximum extent possible. The income inequalities of the present era are in large part driven, entirely unintentionally in most cases, by the force exerted by monetary policy. Bailouts and Quantitative Easing do not go to the 99%; they accrue to the 1%, who are able to game monetary policy.

Eventually, I think Sumner will have to renounce this idea that you can't fight City Hall, and accept that City Hall can't fight Mr. Market. Sumner still has a way to go on this. Even Greenspan rejects rule-based market intervention now. Sumner's NGDP plan, though rule-based, is trying to capture "the rule of the market". If he ever comes to view gold bills as the embodiment of that rule—combining data collection, credit verification, and the open market action itself—he will be sold, and far less monetary policy will be needed or tolerated.

We can wait for that unlikely outcome, or we can persevere, as Sumner has already, by marshaling data from the pre-1913 gold standard to better explain how it weathered exogenous shocks in its day. Jim Grant wrote about the 1921 recession without whipping the gold standard. Murray Rothbard explained the 1819 panic in Austrian school terms. These bracket the crucial Golden Age. Which contraction/expansion event, outside a central-banking economy, was best moderated by fluctuation of the discount rate in the bills market? Study that for a dozen years, write a treatise as well as Scott Sumner does, and the Gold Standard will have its new champion.

Greg Jaxon
Greg Jaxon is an American software engineer who has been studying New Austrian School economics for over a decade, in part by fact-checking Professor Antal Fekete's revisionist historical claims.

Land-Backed Currency

Some people recognize the absurdity of the current monetary system based on the concept of backing bank notes and the electronic equivalent with promissory notes that promise to pay with bank notes that promise to pay nothing. They have been taught that gold is the worst sort of money — even worse than the current monetary system. So, some suggest backing the currency with land. Unfortunately for them, land makes low quality money.

For any commodity, including land, to serve adequately as money, it needs to be portable (relatively high value per unit of weight), homogeneous or uniform, durable, divisible, recognizable, highly marketable (highly liquid, universally acceptable), and stable in value. Also, the commodity used for money should be fairly scarce, but not too scarce. Furthermore, it should have a high stock-to-flow ratio, that is, the quantity of the commodity readily available for use as money is high compared with the newly added supply.

Portability. Land scores extremely low in portability. How does one transport a square kilometer of land from Iceland to New Zealand? Presumably, the land could be dug up and transported by ship. Then, how deep does one dig? Moreover, the cost of transporting the land probably would far exceed the value of the land.

Homogeneity. Land scores extremely low in homogeneity. In valuing land, location is vitally important. Land in the City of London has much more value than an equal area of land in central Greenland.

Durability. Land scores high in durability, especially if its use is ignored.

Divisibility. Land scores high in divisibility. It can be subdivided to where a magnifying glass is needed to see it.

Recognizability. Land also scores high in recognizability. Everyone can recognize land.

Marketability. Land scores low in marketability. It cannot be transferred in seconds from one owner to another without a significant, often a great, loss in value. Moreover, days may be needed to transfer land ownership legally. Thus, land is not highly liquid. Also, land is not universally acceptable as payment for goods, services, and debt.

Stability. Land scores low in stability of value. In 1991, the aggregate value of all the land in Japan was almost four times that of the United States. By 2005, land in Japan had lost half its value while land in the United States had more than tripled in value.

Scarcity. Land scores extremely low in scarcity. Next to salt water, it is earth's most abundant commodity. It is the most abundant commodity if the land beneath the oceans is counted.

Stock to Flow: Land has an excellent stock-to-flow ratio. The amount of new land being formed is insignificant compared to existing land. Also, land being destroyed is insignificant.

Land scores high in durability, divisibility, recognizability, and stock to flow. However, it scores low in portability, homogeneity, marketability, stability, and scarcity. The negative attributes of land as money far outweigh its positive attributes. They make land an extremely poor quality money. (On the other hand, gold scores very high in all the aforementioned attributes that high quality money should have. Thus, gold makes an exceptionally high quality money.)

In spite of being a poor quality money, land has been used to back currencies that were redeemable in land. An example of a land-backed currency is the assignat.

Soon after the revolutionists came to power in France, they established a land-backed paper currency called the assignat. Land that the revolutionary government had confiscated from the Catholic Church, the Crown, and Royalist refugees backed the assignat. Buying land from the government redeemed the assignats, i.e., the government convert assignats into land. When the assignat became legal tender in 1790, it traded at par with specie. By 1796, its value had dropped to zero. Even the death penalty and the Reign of Terror could not maintain its value. In 1796, the government replaced assignats with mandates, another land-backed currency that could be converted into land. Mandates circulated only a few months before they, along with assignats, lost their legal-tender status and became worthless.

In conclusion, unlike gold, which is high quality money, land is low quality money. Any monetary system based on land or backed by land results in low quality money.

Thomas Allen
http://tcallenco.blogspot.com.au/

Gold Fixed-Income Investments

The following is a blatant plug for a business that I am invested in both philosophically and monetarily. Its aim is to get Gold circulating again. No, not in day-to-day purchases, but, and more importantly, in the area of saving and investing. – Philip Barton

Introducing the gold fixed-income investment

Gold fixed-income had existed for centuries, but this asset class is now all but forgotten. Monetary Metals Treasury™ makes what was once old new again.

There is a universal desire to live on interest, not spending the principal. Fixed income meets this need, with its steady payments. Unfortunately, the Federal Reserve has imposed a zero interest rate policy. Savers, fund managers, and retirees have a problem.

The Monetary Metals Treasury™ offers the solution. Investors who want to earn gold for the use of their gold are matched with businesses that use gold productively. This innovative gold fixed-income product is designed to reduce risk for the investor. It is tax-efficient, and compliant with applicable regulations.

Monetary Metals Closes First Gold Fixed-Income Deal at 5%

FREEDOMFEST LAS VEGAS, Nev., July 15, 2016—At FreedomFest, Monetary Metals announces that it has closed its first gold fixed-income deal, to finance the gold working inventory of Valaurum. The initial amount of gold meets Valaurum's current needs, with room for expansion driven by its growth. The interest rate is 5 percent of the gold, paid in gold.

Both gold investors and businesses benefit from Monetary Metals' innovative financing structure. It reduces risk to investors, while also reducing complexity and cost to businesses.

Monetary Metals provides physical gold to Valaurum, to meet its needs in making the Aurum® gold currency unit. Valaurum's proprietary manufacturing process requires a fixed quantity of gold. Monetary Metals provides this gold, while retaining ownership.

Conventional precious metal financing is not only costly, when it's available at all, but complex. Gold's high value and volatile price means that companies which borrow cash to buy gold are risking big losses. Borrowers typically use complex hedging strategies, which adds extra moving parts, people, and costs. The Monetary Metals solution does not transfer price risk to the company

"Monetary Metals offered Valaurum an unusually affordable and simple product for financing gold for our manufacturing process. By helping us expand production and lower our costs, Monetary Metals has advanced our mission of putting gold into the hands of everyone who wants it," said Dr. Adam Trexler, President of Valaurum.

"We are excited to help Valaurum with its gold financing needs. Our innovative business model matches businesses who need gold, with investors who are willing to provide it. We can now offer a yield on gold, paid in gold," said Keith Weiner, Monetary Metals' CEO.