FAREWELL ADDRESS

Gold Standard University Live: *R.I.P.*

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The Inaugural Session of GSUL took place in February, 2007, at the Martineum Academy in Hungary. Subsequent sessions, including one in Dallas, Texas, showed a healthy increase in attendance, on average by fifty percent. Still, I am now forced to announce that Session Four in Hungary in July, and Session Five in Canberra, Australia in November will be the last. GSUL will fold tent as its sponsor, Sprott Asset Management, Inc., has withdrawn its financial support. Mr. Eric Sprott said in his letter that "we weren't attracting enough interest to justify that ongoing expenditure".

To give you an idea of the odds I am facing let me quote from the article in Wikipedia (June 9, 2008) captioned under my name: "It should be noted that mainstream economic theorists criticize gold standard-oriented monetary economists and monetary reformers such as Professor Fekete as 'fringe' or 'amateur' economists, not worthy of serious study. Professor Fekete has never held a teaching position in the economics department of any prominent university".

A deep, searing corruption

Pre-1936 theorists of the gold standard are likewise dismissed by the mainstream as "not worthy of serious study". I am proud that I have tried to continue that tradition in the footsteps of giants like Adam Smith, Carl Menger, Böhm-Bawerk, Ludwig von Mises, Frank Fetter, Benjamin Anderson, among others. Monetary scientist Walter E. Spahr, who served as Chairman of the Department of Economics at New York University from 1927 to 1956, wrote in *The Commercial and Financial Chronicle* on March 20, 1947: "A deep, searing corruption has afflicted monetary science. It may require many years of painful effort to overcome this disease if, indeed, it can be combated successfully. The well-being of our nation has been undermined by this affliction… When gold payments were suspended in 1933 and we embarked upon a sea of managed currency, a very large number of professors and organizations [list appended] urged a prompt return to a gold standard. The question arises what has become of those voices. Were they in error then? Did those 710 economists know so little about monetary principles in 1933 that they could not, a short time later, defend their earlier position? *Or were they simply corrupted by a political movement which they found it inexpedient to oppose?* There appears to be no valid defense that can be offered for men who pretend to be scientists but who adjust their so-called principles in accordance with changing political tides. A very great number of those who pass themselves off as monetary economists either have not understood the lessons of the past or have been willing to junk them, in the interest of expediency, for such personal gains as they may have supposed they might realize…"

Perpetuation of an immoral and dysfunctional monetary regime

One representative of the mainstream, Professor Jeff Frieden of Harvard, says that "the topic of the gold standard has received massive attention from scholars since the 1980's — from Barry Eichengreen to Ben Bernanke with hundreds in between — and a serious analysis of its implications requires a serious engagement with the existing scholarly literature."

I have studied most of that literature and I have not been able to find one iota connecting our crisis-ridden monetary system to the forcible removal of gold from it. Rather, the gold standard is portrayed as an anachronistic monetary regime, the removal of which was due to popular demand. Moral considerations, sanctity of contracts, the honor of the government, the opprobrium of declaring bankruptcy fraudulently, the question of tormenting widows and orphans did not enter into it. Nor did long term economic considerations such as the ticking time-bomb of capital destruction. The question is never raised how well the gold standard succeeded as the protector of savings, as the instrument of capital accumulation and, above all, as the stabilizer of the interest rate structure. A façade that the mainstream has provided a reasonably complete and balanced view of the gold standard, past and future, is maintained but is outright mendacious. The existing literature is in fact a stumbling block in the way of impartial inquiry. It is dedicated to the maintenance of the *status-quo*, the perpetuation of an immoral and dysfunctional monetary regime: that of irredeemable currency. This has led me to found Gold Standard University Live, that is free to challenge the Keynesian and Friedmanite orthodoxy.

Let me mention just two broad areas of inquiry which have been overlooked by others, but which we have planned to tackle:

(1) *Gold and the theory of interest.* The latter cannot be understood without the former. We have to incorporate the theory of hoarding into the theory of interest. We have to study the problem of capital destruction in the wake of gyrating interest rates, the main consequence of ousting gold from the monetary system.

(2) *Gold and the theory of speculation.* To understand the causes of the Great Depression we must understand speculation. The theory of speculation covers such topics as arbitrage, futures trading, basis (especially gold and silver basis), contango, backwardation, short squeeze, corner. Speculation is virtually ignored by conventional economic theory. The hurly-burly on the floor of the exchanges apparently does not reach the ears of inhabitants of the ivory tower.

The economic consequences of Mr. Keynes

Once these two gaps are filled, it becomes clear that the gold standard is naturally ordained as the only system that can stabilize interest and foreign exchange rates. By contrast, the regime of irredeemable currency has been inflicted upon the people through fraud and chicanery. Its foundation is no firmer than the gullibility of people who are, for the time being, willing to exchange real goods and real services for irredeemable promises to pay. But as the prices of crude oil and various foodstuffs convincingly show, there are definite limits to gullibility.

The claim of Keynes parroted by most mainstream economists, that the Great Depression was due to the "contractionist tendencies of the gold standard", is untenable. Just the opposite is true. Here is what happened.

In 1933 the forcible removal of gold signaled to bond speculators that the one and only competition to government bonds has been knocked out. They were quick to realize that their chance to bid bond prices sky high has come. The result was continually falling interest rates causing widespread capital destruction, as well as falling prices. Producers were bankrupted *en masse*. Economists have never bothered to study the untoward consequences of the forcible removal of gold, even though common sense would suggest that it cannot be done with impunity.

A careful and impartial examination of the record shows that the scuttling of the gold standard, as advocated by Keynes, was the main cause of the Great Depression and, unless it is rehabilitated with all deliberate speed, a new depression may be waiting in the wings.

Janus-face of marketability

Gold and interest are intimately inter-related. The concept of *marketability* is due to Carl Menger. It was through the evolution of the most marketable good that gold has become money. Gold is most marketable *in the large,* that can also be expressed by saying that gold is more *salable* than any other commodity. Silver is most marketable *in the small,* that can also be expressed by saying that silver (along with gold) is more *hoardable* than any other commodity. The Janus-face of marketability can be observed if we contemplate that gold is the preferred agent when one has to transfer value over *space*. The preferred agent in transferring value over *time* is silver. We may clearly recognize the dual nature of money throughout history, starting with cattle money *versus* salt money. This duality has to do with the paramount fact that space and time are absolute categories of human thought.

A new theory of interest

As salability leads directly to the concept of *value*, so hoardability leads directly to the concept of *interest*. Interest arises out of the desideratum to optimize conversion of income into wealth and wealth into income. I have chosen the conversion problem as our point of departure in developing a new theory of interest. I have deliberately discarded the old-line theory based on the exchange of present for future goods that assumes, wrongly, that a present good is always valued more highly than an equivalent quantity and quality of future good. A more careful analysis shows this to be true only on condition that the delivery of factors is dove-tailed. Premature delivery of a factor could cause losses and, hence, may result in perverse valuation.

The solution to our optimization problem answers two of the greatest of human needs: planning for the education of one's offspring, and providing for one's old age. If the conversion of income into wealth is done through hoarding and the reverse conversion through dishoarding, also known as *direct conversion*, optimum is reached when choosing the most hoardable commodity as the agent of conversion. However, direct conversion can be further improved upon by passing to *indirect conversion* through the agency of exchange. Typically, a younger man gives up income in exchange for wealth belonging to an older. The former is anxious to go into business for himself for which the latter puts up the capital. In this view interest appears as the value of improvement in efficiency through the exchange over direct conversion. In particular, direct conversion means zero interest. Interest becomes positive if social arrangements admit indirect conversion.

The following point is important. The nexus between gold and interest is established by the fact that if indirect conversion is hampered through secular or canonical proscription (e.g., usury laws), the economizing individual is not helpless. He can still achieve his goals by falling back on direct conversion through hoarding/dishoarding gold. He will do that even in the absence of proscription. In case interest is artificially lowered by the banks or by the government, he will hoard gold in protest and dishoard it as the rate of interest is allowed to rise. Thus gold is the agent to validate time preference. This aspect is almost always ignored by authors, including Ludwig von Mises to whom gold hoarding was a *deus ex machina*. He failed to see that time preference would hardly amount to more than a pious wish if gold hoarding did not give it teeth. Moreover, this is true whether *on* a gold standard or *off*. When on, gold hoarding implies withdrawal of bank reserves whereby individuals directly force the banks to adjust the rate of interest to a level consonant with prevailing time preference. The main excellence of the gold standard is that it makes adjustment crisis-free. When off gold standard, hoarding makes the gold price soar, leading to monetary crises. Although the upshot is the same in either case, namely, higher interest rates, under the regime of irredeemable currency the adjustment is made in a crisis-prone environment. A swinging interest rate structure is generated that is most damaging to savers and producers.

Gold hoarding provides an escape route for the individual from the harsh consequences of predatory monetary and credit policies of banks as they plunge society into debt slavery. For those who fail to use the only prophylactic, gold, debt slavery is all but inevitable.

Interest and marginal utility

The monetary metals are characterized by their great stores above ground. The stock-to-flows ratio is a high multiple for gold. The suggestion has been made that the world's monetary silver has been consumed by industry and is gone. However, we can account for the disappearance of monetary silver through a more plausible hypothesis, namely, that most of it has gone into hiding. Silver is a monetary metal in the first place; it is an industrial metal only in the second, propaganda to the contrary notwithstanding. Industrial uses of silver are marginal applications, subject to squeeze by the investment demand.

The case is different for non-monetary commodities. Here the stock-to-flows ratio is a small fraction. The reason is declining marginal utility, in contrast with monetary metals having constant (near-constant) marginal utility. Mises dismisses constant marginal utility as contradictory since it implies infinite demand. He is plainly in the wrong. Mises missed the nexus between gold and interest. Demand for gold would be infinite only in the absence of interest which acts as obstruction to gold hoarding. By contrast, demand for non-monetary commodities is limited by declining marginal utility. Keynes made a colossal blunder when he talked about "wheat rate of interest", "coal rate of interest", etc. Interest can only exist in relation to a monetary commodity with constant marginal utility. The marginal utilities of wheat and coal decline very fast indeed.

Lysenkoism ─ American style

The reason why mainstream economics is silent on the connection between gold and interest is that it exposes the incredible mismanagement of the economy in the twentieth century, as well as the corruption of the monetary and credit system by the government and banks in the twenty-first. Universities no longer serve the cause of search for and dissemination of truth. Instead, they serve as the "intellectual body-guard" of Keynesianism and Friedman's monetarism. They provide refuge for a reactionary conspiracy that has succeeded in hijacking the world's monetary system and putting it on a collision course with the welfare of the world's population. Savers are pilfered and producers are plundered. Universities have betrayed people anxious to secure their economic survival in the face of untold dangers as indicated by the Babeldom of runaway debt and exploding derivatives markets. They are silent where they should be outspoken and critical. Apparently, they don't want to embarrass their paymasters.

History will not be kind to mainstream economists. Keynes, Friedman, and their followers will be lumped together with Soviet biologist Lysenko, stooge and sycophant of Stalin. Lysenko sent his fellow biologists to the Gulag, never to be heard from again, whenever they opposed his hare-brained theories on genetics. Lysenko betrayed science just as he betrayed humanity. No less than Stalin, he was a monster.

Theory of speculation

Speculation is man's main tool to deal with risks and future uncertainties. Mainstream economics fails to make a distinction between risks created by nature and risks created by man. The latter includes risks involved in foreign exchange and interest rate fluctuations. They are certainly not created by nature, witness the fact that such risks are non-existent under a gold standard. Clearly, they were created by governments while abandoning the gold standard, thereby destabilizing foreign exchange and interest rates.

It is untenable to assume that under the regime of irredeemable currency speculation can tame these fluctuations. Just the opposite is true. Futures markets make interest rates even less stable and more volatile. It is not possible to predict whether bond prices go to zero as they would under hyper-inflation, or whether they go sky high as they would under hyper-deflation. This problem is crucial and it can be approached only through understanding bond speculation, especially as it is helped by tail-winds provided by the central bank.

The following facts are either not widely known or not well-understood. Open market operations of the Federal Reserve (Fed) were introduced in the 1920's in violation of the Federal Reserve Act of 1913. They were legalized retroactively in the 1930's. There was hardly any public discussion of the wisdom of the move or the stakes involved. Pre-1936 economics was categorical in its condemnation of the monetization of government debt. Introducing the catchy name "open market operations" has made it possible to monetize government debt through the back door.

Economists failed to predict the disastrous consequences of this *ex post facto* legislation. Bond speculators were given a risk-free opportunity to profit. In pre-empting the Fed they would buy the bonds beforehand, dumping them after the Fed has completed the purchase of its quota. Risk-free speculation imparted a bias to the market favoring rising bond prices or, what is the same to say, falling interest rates.

It speaks volumes about the degradation of economics in the wake of the Keynesian revolution that an illegal trick could be elevated to the holiest of gestures whereby high-powered money is created, and nobody points to the downside of the prestidigitation.

Revisionist theory of the Great Depression

Most importantly, economists have also failed to identify falling interest rates as the main cause of the Great Depression. They have concentrated on falling prices, not realizing that in doing so they are confusing cause and effect. The true chain of causation is as follows.

Persistently falling interest rates result in the erosion (ultimately, destruction) of capital deployed by the producing sector. In effect, bond speculators siphon off money stealthily from the capital accounts of the producers. The latter are unaware of being victimized by this vampirism of the financial sector. But they are, whether they recognize it or not. Profits of the bond speculators do not come out of nowhere. They are the flipside of the opportunity loss suffered by the producers who have to continue financing their capital at the higher rate. Unable to escape from the clutches of debt, the producers are squeezed. They scramble to sell more of their product at fire-sale prices in the hope to be able to service debt contracted at the higher rate. In this way a downward spiral of prices is created.

The prevailing optical illusion suggests that money is scarce. Everybody cries out for the Fed to create more money. The Fed complies and enters the open market to purchase more bonds. In doing so it provides bond speculators with another opportunity to make risk-free profits. Interest rates fall further and producers are squeezed more. A vicious circle is activated. At the end of the spiral producers go bankrupt in droves.

According to my revisionist theory the Great Depression, far from being caused by overproduction as suggested by Keynes, was caused by wholesale destruction of capital. The ultimate cause was risk-free profits granted to bond speculators through the Fed's open market operations.

This is a most serious challenge with which the prevailing orthodoxy is confronted. The weakness of its position is shown by the unwillingness to take it up and have an open debate. It is with regret that Gold Standard University Live has to suspend its operation and let Keynesian orthodoxy win by default.

Witch-hunt in Washington

High energy and food prices have given occasion for a witch hunt in Washington. Politicians are trying to push the blame on speculators, calling for legislation to limit long positions in the futures markets. These laws, if enacted, would be counter-productive. All this goes to show that economics is a complete ignoramus when it comes to speculation.

Speculating in crude oil and in grains is *not* risk-free. Profits are the incentive for speculators to lend liquidity to the markets and to temper price swings. Indeed, speculation stimulates production or retrenchment according as the threat is scarcity or overproduction.

It is a blunder to regulate speculators out of the commodity markets. The result is predictable: illiquidity, more volatility, more scarcity. Consumers would end up paying even more for energy and food.

So much for commodity speculation. Bond speculation is another matter. As explained, bond trading does not address risks that exist in nature. It addresses risks created artificially by the government. Worse still, instead of promoting stability, it destabilizes the interest rate structure further. Worst of all, bond speculation is made risk-free by the open market operations of the Fed. The cap on bond prices has been removed, and continually falling interest rates may push the world into another Great Depression, possibly worse than the last one in the 1930's.

Farewell message

These are just some of the questions GSUL has set out to investigate in depth. Mainstream economics avoids these topics like the devil avoids holy water. Other schools such as the Austrian, for example, appear to be more interested in cultism and in regurgitating old tenets than in new research of new problems to which mainstream economics turns a blind eye.

It is with regret that GSUL gives up its plans to discuss these burning issues in public just at a time when the need for such debate appears to be the greatest.

I take this opportunity to thank everybody, participants as well as sponsors, for their support of our cause. I wish everybody a prosperous journey through what promises to be truly hard times.

June 26, 2008.