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"GOLD STANDARD UNIVERSITY"

THE GOLDEN THORN IN THE FLESH

Part One of a Series of Two

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Soldiers throwing away ammunition before combat

The guessing game among gold market analysts is still on: will central banks resume gold dumping or won't they, as the price of gold takes another shot at \$700? In arguing the case pro and con, virtually all analysts miss one important point. Central bank sales of gold against the backdrop of deflation looming in the horizon is akin to soldiers throwing away ammunition just before combat. They should be doing the exact opposite. Soldiers should replenish their supply of ammunition. Central banks should reinforce their balance sheets by purchasing gold (as indeed several important ones, including those of China and Russia, are on record of doing). This is the only way to keep the powder dry. In a deflation it may be necessary to inject massive amounts of new credit into the system, but the only way to make the national currency more plentiful *without weakening it* (let alone destroying it) is through gold purchases. They are by far the most effective weapon of a central bank to combat deflation. Are we to assume that our central bankers are dummies who do not know this piece of elementary truth?

Dynamics of deflation

Gold reflects stability; both inflation and deflation reflect instability. It is a mistake to believe that currency values are only threatened during an inflationary spiral. Under the regime of irredeemable currency there is also a threat during a deflationary spiral, although it is more subtle. The deflationary scenario involves the impending danger of a domino-effect of insolvent firms falling, as they carry a crushing debt-burden which is further aggravated by falling interest rates and falling prices (or proxies of the latter: the loss of pricing power and market share). As Leon Fisher of Unknown News said in his piece *The Future Looks Very Bleak* (March 26, 2007): "The first indicators of economic collapse have already manifested themselves in the housing industry, and the Big Three automakers. Teetering on bankruptcy, they will be the first of the large economic dominoes to fall, and the rest will follow in short order. As a consequence, something on the scale of another Great Depression may be a possibility." When firms go under, when capital and jobs are wiped out on a large scale, then instability in the economy becomes pervasive. Trade war, heretofore waged clandestinely, becomes a declared war. Competitive currency devaluations are made into a legitimate weapon to capture export markets. This is the most destructive tool in the hands of a government second only to

starting a shooting war. In the present situation, it is coming with the inevitability of a Greek tragedy, drawing the protagonist to his doom.

Golden thorn in the flesh

In the meantime gold is still a thorn in the flesh of Western governments. They have not been able to live down the disgrace of their wholesale defaulting on their domestic and international gold obligations. The 'dog in the manger' syndrome still prevails: if the governments cannot control gold, then they are bent upon destroying it. This neurotic attitude must change. Western governments should make peace with gold, as Eastern governments already have. They should accept the fact of gold hoarding as they accept the tide and ebb of the oceans. If Western governments really wanted to promote the welfare of the electorate (as opposed to that of special interest groups), then they should enlist gold on the side of construction, not on the side of destruction. With gold's help they could set on a course of stabilization. Foreign exchange rates could be stabilized without any further delay, removing the threat of a trade war; as could the rate of interest, removing the threat of exploding debt burden to producers due to a falling rate structure. If Western governments did use gold constructively, then they could spare the electorate from much unnecessary economic suffering.

Don't fix the gold price

In implementing a stabilization program the inevitable bone of contention is how to fix the gold price. This is a non-starter. You cannot build consensus that way. No gold price is ever high enough to the debtors and to gold bugs, nor is it ever low enough to the creditors and to the chrysophobic. The need is for restoring the people's constitutional right to convert gold into the coin of the realm at the Mint. The government should open the Mint to the unlimited coinage of gold free of seigniorage charges.

The objection that gold coins from the Mint are already available is lame. These souvenir coins will never circulate unless seigniorage is reduced to zero. People will not part with their gold coins unless they are absolutely sure that they can get them back on exactly the same terms. Souvenir coins could not be used as the monetary standard or unit of value, unless the right to unlimited coinage is unconditionally guaranteed. A constitutional right of the citizens has been usurped by the government. No move towards restoring that right has been made. Nothing short of full restoration will do.

Note the hypocrisy of mainstream economists in suggesting that gold is passé. They say: "the right of the people to own and trade gold was restored 30 years ago and, see, gold still refuses to circulate". Lifting an executive ban subject to withdrawal is not the same as restoring the constitutional right of the people. Only after opening the Mint to the free coinage of gold can the eagle coin be promoted from a mere conversation piece to monetary standard and unit of value.

The determination of the exchange rate between the paper dollar and the gold dollar ought to be left to the market which would then force the Federal Reserve banks to post

buying and selling prices for the gold dollar. The spread between these prices would show the quality of Federal Reserve credit for everyone to see. The wider the spread, the lower the quality.

This would mean a fair and open competition between the gold dollar and the paper dollar. Let the people decide which one they prefer, or what they want the Federal Reserve banks to do before they accept their paper as equivalent of gold. Let the unconstitutional privileges of the U.S. Treasury and the Federal Reserve to issue obligations without having the means and the willingness to meet them be abolished for once and all. Let no one have privileges without countervailing obligations.

Everlasting fair weather delivered by order of the government

The reason that the regime of irredeemable currency could survive so long (35 years, to be precise, longer than any previous experiment) is found in the uncritical embracing of the servile ideology of our age and the mindless faith in, or foolish longing for, government omnipotence. People cherish the myth of everlasting fair weather, and they fully expect their government and its central bank to deliver it. Awakening will be rude.

One may well deplore the hoarding of marketable commodities under the regime of irredeemable currency as wasteful, anti-social, and dangerous as it may ignite and stoke the fires of the inflation-deflation cycle. But for the marginal bondholder hoarding is a last resort. He has been disenfranchised, abused, and the credit system has been rigged to his prejudice. He is left out in the cold. He will not take it lying down. Disenfranchised as though he is, he won't be pauperized if he can help it. In every historical episode when hoarding was criminalized (sometimes punishable by death, e.g., in the various episodes of debasing the coinage of the Roman Empire; John Law's system, and under the regime of the assignats of the French Revolution) the people could ultimately prevail in forcing a return to sanity - or else the Empire collapsed.

Indictment of the regime of irredeemable currency

These remarks spell a most devastating indictment of the regime of irredeemable currency. This regime is totally insensitive to the rights, the needs, and the wishes of the savers in spite of the fact that they are the very providers of the wherewithal of economic progress. It blots out danger signals sent out by the markets. It denies the power of disposal over one's savings to anyone outside of a small elite. The natural outcome of this insensitivity is the paucity of savings in socially usable or desirable forms that could be available for economic development. Spontaneous savings, such as there are, take the form of inventory-padding, leads at the input and lags at the output level, e.g., artificially slowing output at the well-head, the farm-gate, or at the mill of the mine, and other forms of hoarding, are motivated by sheltering savings from plunder. Thus savings are generally unavailable for economic development and capital accumulation, except as part of stock-market speculation. To that extent the regime of irredeemable currency is guilty of turning savers into speculators, and accumulators of capital into gamblers. It is the most wasteful and uneconomic system of managing natural and human resources since the

primitive food-gathering economies. To this injury to human cooperation must be added the insult to human intelligence. On the top of all that, the regime has inflicted and will continue to inflict great sufferings on innocent bystanders. The inflationary-deflationary cycle hits people indiscriminately.

Next to guns, irredeemable currency was the main tool of coercion of the totalitarian governments in the 20th century: soviet bolshevism and nazi socialism, before their downfall. It was utterly disgraceful and deplorable that Western democracies were willing, not to say eager, to stoop so low as to embrace such a tainted instrument with gusto. By now politicians are firmly wedded to the regime of irredeemable currency - in callous disregard of the constitutional issues involved such as the sanctity of contracts, the right of the individual to property and due processes of law and, last but not least, the ideal of limited government. As Gold Standard University has set out to show, no less callous is the disregard for sound economic principles.

Is it not time that the political leaders of Western countries finally admit that the regime of irredeemable currency was not the outcome of natural progressive forces, as formerly trumpeted, but the result of a calculated series of confidence tricks played on a gullible people? Is it not time to say publicly that the experiment was an abysmal failure, and to call it off? Is it not time to allow free discussion of the demerits of such a dubious, debasing, and derogatory tool, and of the eternal merits of a constitutional monetary system?

Gold Standard University

The Inaugural Session of Gold Standard University took place at the Martineum Academy in Szombathely, Hungary, in February, 2007. Session Two is scheduled for August 15 - 29, 2007, which will include a blue-ribbon panel discussion on the gold and silver basis as a most sensitive theoretical tool of market analysis which is being developed by a team of researchers at Gold Standard University, under the title: *The Last Contango - the First Sign of Disintegration of the International Monetary System*. For further information please contact: GSUL@t-online.hu .

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