

THE ANTI-GOLD GOSPEL ACCORDING TO KALETSKY

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Anatole Kaletsky is the author of the most recent Anti-Gold Gospel (www.gavekal.com, January 21, 2008.) He is an establishment journalist, Associate Editor (formerly Economics Editor) of *The Times*. He says that he instinctively dislikes gold because “historically gold has been a terrible investment and, even in the short term, gold has failed as a store of value”. I am satisfied to leave this statement to stand on its own, and wish Kaletsky good luck in seeking a better store of value in fiat currencies.

It is patently disingenuous and unfair to compare the gold price to stock indexes. It would be fairer to compare stashed-away gold to passbook savings. A portfolio of equities takes managing. It may be beyond the reach of most wage-earners and pensioners while their savings is the main target of the pilferers who run the nation’s banks and monetary system. Who said pilferers were after wealth invested in the stock market?

I strongly object to the idea that “gold is an investment”. Gold is better described as a non-investment, more precisely a place where you park your savings when you cannot find satisfactory investment outlets either because interest rates are too low, or because the risk of holding equities is too high, e.g., after a bull run of the stock market driven by printing-press money. Gold is not an investment any more than a fire-insurance policy is. Governments have a sacred duty to protect the value of funds of the weak, who cannot fend for themselves in the investment arena. Without protection their funds would melt away like butter left in the blazing sun. Governments have failed miserably in discharging this sacred duty. The Biblical curse is upon them for “tormenting widows and orphans”.

Kaletsky, like everyone before him preaching the Anti-Gold Gospel, studiously avoids the question why the Treasury and the Federal Reserve should have the privilege of issuing obligations that they have neither the means nor the intention to honor. If anyone else tried to run a business on that basis, he would land in jail like Charles Ponzi did in the 1920’s.

Kaletsky also dodges the fact that gold is the only balancing item in the asset column that has no countervailing liability in the balance sheet of someone else. It is this feature that makes gold impervious to defaults, devaluations, and deliberate debasement of the currency. For this reason gold is universally sought after as a safe haven, especially when the seas get rough. There is simply no substitute for gold in this regard.

Gold is the indispensable regulator of debt in society. Kaletsky apparently believes that government bureaucrats should determine how much debt society is able safely to carry, and they should regulate the level of debt accordingly. Well, we have just tried this and found that whenever irredeemable promises are to be liquidated by issuing more irredeemable

promises, debt proliferates beyond any limit. The derivatives monster and its bastard offspring, “bond insurance,” is the beacon luring the boat of the national economy to its doom on the reefs. Clearly, debt existing in the world today will never be liquidated through the normal processes of debt-retirement, that is, without detours into deflationary or inflationary territory (i.e., through default or depreciation). It is lunacy to think that the debt-pyramid can continue to grow indefinitely without causing a major catastrophe further down the line. All debt will be liquidated in the same way as subprime mortgages: through default — or else, it will be inflated away.

By the way, did it ever occur to Kaletsky that there is absolutely no need for bond insurance under a gold standard? The reason is that interest rates and, hence, bond prices are confined to such a narrow range that bond speculation becomes unprofitable. Under a gold standard capital and talent are freed to pursue socially desirable goals.

Kaletsky’s argument that there is not enough gold in the world to serve as a means of exchange in our sophisticated global economy is the old war-horse of the Anti-Gold Gospel. All the output of the gold mines for the past half-century, plus all the monetary gold disgorged by the central banks in a futile effort to contain the gold price, has been gobbled up by gold hoarding. This is an unmistakable sign that people do not trust the integrity of government promises, nor do they buy the academic claptrap about gold being a barren asset and a barbarous relic. Obituaries of gold money have been premature. The golden corpse still stirs. People who sought refuge in gold have been amply rewarded for their foresight. More rewards are on the way. Others who did not avail themselves of the opportunity will have occasion to regret it. They are to be victimized by the welfare-warfare state and its unconstitutional power-grab in issuing irredeemable dollars. These dollars could not have been issued under a system of government of limited and enumerated powers. All present dollars have been issued unconstitutionally. They are the *corpus delicti*: proof of usurpation of unlimited power.

If constitutional money were re-established, then gold would come out of hiding and make itself available as a means of exchange. There is plenty of gold in existence to support a gold standard, provided that confidence in promises is re-established. There is no rigid rule limiting the amount of sound credit that can be safely built upon a given gold base, especially in this age of instantaneous and free communication. However, multiple credit construction and borrowing short to lend long as a banking technique must be renounced.

The last word whether gold is destined once again to become the pivot of the international monetary system, or whether it is hopelessly antediluvian and incompatible with economic progress, will not be pronounced by detractors of gold and devotees of fast-depreciating fiat money. Their time is up. Their schemes and nostrums have been tried. Now it is the turn of their victims to have their day in court to pass judgment on the fiat money experiment. “He laughs who laughs last”. The annals of monetary history do not know one single instance in which irredeemable currency survived the test of times. Either the currency was returned to its gold anchor in good time and its value stabilized, or it plunged to worthlessness within a generation. We are skirting these limits right now. The present experiment with the irredeemable dollar has been going on for just about a generation. You will not have to wait decades to witness the failure of this experiment.

The dollar is hemorrhaging on two counts: one is the trade deficit, and the other is the budget deficit. Both the political will and the economic know-how are missing to stop the bleeding. The U.S. is borrowing \$800 billion annually from foreigners to fund its consumption of foreign-produced goods and commodities. The federal government is running an annual budget deficit of almost \$600 billion. At one point foreigners will refuse to finance the burgeoning twin deficit, forcing the Federal Reserve to monetize all the additional debt.

The danger is real that the value of the dollar, both international and domestic, will collapse at that point.

Kaletsky says that the gold standard is totally anachronistic in our age of rapidly advancing technology and growing populations. He might as well say that good faith behind promises have been rendered obsolete by technological progress, and the more people there are the more the government is justified to cheat them out of their savings through currency debasement. Kaletsky is entitled to his belief that people will meekly continue in their assigned role of being victimized by spendthrift governments. However, the New Year 2008 brought with it signs aplenty that the open season of governments' preying upon savers and producers of real goods and real services is coming to an end. People wake up and realize that they are surrendering real goods and real services in exchange for irredeemable promises.

The consequences of this awakening will be most painful. The responsibility for the coming credit collapse in the wake of the unconstitutional paper dollar rests with the U.S. Treasury, and its partner-in-crime (partner-in-check-kiting if you will) the Federal Reserve. It may serve as a useful reminder to recall that the French, some seventy years before their bloody revolution, experimented with irredeemable currency under the management of the Scottish adventurer, John Law of Lariston. When Law's system unraveled people wanted to lynch him. He had to leave Paris in a hurry. Under the cover of night. In a disguise. Disguised as a woman.

The finance capital of the world, denominated as it is in dollars, is in danger of being wiped out. There is only one way to take out insurance against this contingency: buying gold. As I have explained above, the reason can be found in the balance-sheet concept of gold. The only financial asset that will survive any consolidation of balance sheets, any default, any devaluation, any depreciation is gold.

Gold holdings are the most negatively-correlated asset class to traditional financial assets. Portfolio-diversification can be achieved by balancing financial assets such as bonds, equities, and currencies by holding gold. The best timing to set up a gold hedge is when cyclical trends change, as they do right now. The Dow/gold ratio is presently indicating a change. It has turned from increasing to declining mode, which is a red-alarm signal warning wealth-holders that it is time to hedge financial assets and even to go overweight in gold.

The rising gold price and its implications have been largely ignored by the financial press and the investing public so far. The proposition that gold is still a monetary metal and still has a monetary role to play is ridiculed, while some central banks around the globe (e.g., that of Russia, China, India, Argentina, Brazil, to mention but the most important ones) are quietly remonetizing gold as they diversify out of dollars and build gold reserves from scratch. They keep this activity under cover as much as possible since it is not their intention to upset the golden apple-cart.

It is not too late to set up gold hedges as portfolio insurance. Private and institutional investors (including pension funds and insurance companies) have investments to protect worth some \$180 trillion. Not more than \$600 billion worth of gold bullion is presently earmarked as hedges for portfolio insurance. (Note that gold-mining shares are not eligible for this purpose.*) In other words, only about one-third of one percent of all the investments is protected by gold hedges while more than 99 percent is unprotected. Even this is a gross overestimate because most of the hedged portfolios are heavily overweight in gold, leaving that much less gold for the unprotected and thinly protected ones. Be that as it may, if global investors decided to allocate even a modest three percent of their assets to purchase portfolio insurance, the consequence would be that \$6 trillion paper assets would be chasing gold bullion worth \$0.6 trillion, or one-tenth, at the present price of gold. This means ten bidders for every ounce of gold available. Portfolio insurance is still cheap, but the cost may quickly go up ten-fold or more, once the stampede starts.

Kaletsky would serve his readership better if he advised caution at this juncture. It is still too early to dismiss the possibility that the *Titanic* of the world economy, having collided with the derivatives iceberg tearing a subprime hole in the hull, may go down. Golden life-savers may yet come handy.

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* Gold mining shares are not eligible as portfolio insurance since they have an ambiguous correlation to traditional financial assets. While from time to time they may be negatively correlated, and there is no question of their ability to benefit from promising trading opportunities, long-term wealth preservation demands fully allocated, segregated, and insured gold bullion. The counterparty risk involved in owning gold mining shares is not zero. Worse still, the full extent of this risk is unknown. To complicate matters further, many a government (such as that of Ecuador) keeps a jaundiced eye on its gold mining industry and is trying to determine the most opportune moment to expropriate foreign shareholders. Gold bullion is not dependent on anyone's promise, representation, or ability to perform (nor, if properly stored, is it dependent on the propensity of the government to expropriate), in a word: gold bullion is not someone else's liability. Therefore it is the only agent that can provide the necessary protection against both contingencies: systemic collapse and slow monetary debasement, while incurring the lowest possible level of risk.

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