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Why Gold-Backed Currencies Help Prevent Wars

Lecture by Ferdinand Lips, Zürich
(translated from German)

The context

I will start my talk with an allegation. You have gathered here for a specific reason. You have come because the gold standard was given up in 1914 at the beginning of World War I.

Looking at the program, I see that all of the topics with which we are going to deal are in some way related to that event. World history proves that there is a close relationship between monetary systems and war and peace. It is also evident that there is a close relationship between monetary systems and ethics and morals.

Unfortunately, it is not widely known that the 19th century was a period of prosperity and economic growth without inflation. It strikes us like a fairytale when we discover that in those days the most important currencies in the world were stable over a long period. The French franc, for example, remained solid for one hundred years. It was the era of the gold standard.

The Life Span of Currencies

French Franc	1814 – 1914	100 years
Dutch Guilder	1816 – 1914	98 years
Pound Sterling	1821 – 1914	93 years
Swiss Franc	1850 – 1936	86 years
Belgian Franc	1832 – 1914	82 years
Swedish Krona	1873 – 1931	58 years
German Mark	1875 – 1914	39 years
Italian Lira	1883 – 1914	31 years

(Source: *Pick's Currency Yearbook 1977 – 1979*)

How the gold standard worked

The basic rule of the gold standard was a fixed amount of gold for each money, i.e., each money was defined as a specific weight of gold. Paper currencies were redeemable into gold at any time. A nation's monetary reserves consisted of only gold. On an international level, importing and exporting gold was unrestricted. All balance of payments deficits were settled in gold. (Balance of payments: the sum of all transactions between the homeland and other countries.)

In this way, gold had a disciplining influence on a national economy. It limited public spending. It provided citizens with money that maintained, and even slightly increased, its purchasing power over time and was internationally recognized. If a balance of payments deficit developed, gold automatically transferred out of the country. As a consequence, prices began to decrease. Exports became competitive again and the balance of payments reversed. If a country had a balance of payments surplus, then gold entered the country and the economy is able to expand. Upward revaluations or devaluations were unthinkable. The system maintained its stability automatically. This is one reason why politicians do not like gold. Gold forces them to balance their budget.

The 19th century gold standard, the highest monetary achievement of the civilized world

The gold standard was neither conceived at a monetary conference, nor was it the brainchild of some genius. It was the result of centuries of experience. Great Britain was the architect. At the height of the gold standard at the beginning of the 20th century there were about fifty nations, all of them leading industrial nations, which participated in the gold standard. It was one big clearance community, and it worked.

In his book *Währungen am Scheideweg (Managed Money at the Crossroads – The European Experience)*, Prof. Dr. M. Palyi wrote in 1960:

“For the first time since Rome’s prime did the civilized world succeed in creating a monetary unit. The commercial and financial integration of the world was achieved without the help of a military empire or a dreamy utopia. In theory and in reality, this monetary unit was accepted and recognized as the only rational currency system. Due to the automatic mechanism and the discipline to which the monetary institutions were tied, fluctuations in the exchange rates were very limited if not altogether impossible. This was the incalculable advantage of a gold currency. Trade and industry were able to plan ahead. Especially the automatic mechanism and the “rules of decent behavior” in monetary affairs observed at the time, liberated the value of money from the impact of the governments’ whims. They substantially stabilized it on a worldwide basis. Despite all assurances by the monetary reformers, no reasonably equivalent replacement has been found in the meantime.”

Economist Ludwig von Mises wrote in his book *Human Action*:

“The gold standard was the world standard of the age of capitalism, increasing welfare, liberty, and democracy [...]. In the eyes of the free traders its main eminence was precisely the fact that it was an international standard as required by international trade and the transactions of the international money and capital market. It was the medium of exchange by means of which Western industrialism and Western capital had borne Western civilization into the remotest parts of the earth’s surface [...] and creating riches unheard of before. It

accompanied the triumphal unprecedented progress of Western liberalism ready to unite all nations into a community of free nations peacefully cooperating with one another. [...] The gold standard is certainly not a perfect or ideal standard. There is no such thing as perfection in human things. But nobody is in a position to tell us how something more satisfactory could be put in place of the gold standard.”

The era of the gold standard during the 19th century was the golden age of the white man. During this period, after Napoleon, there were only seven wars of any importance.

Post-Napoleonic Wars During the 19th Century

1855	Crimean War
1861 – 1865	American Civil War, abolition of slavery, Abraham Lincoln
1866	Prussian-Austrian War, Königsgrätz, North-German Union
1870 – 1871	German-French War
1877 – 1878	Russian-Turkish War, Congress of Berlin
1894 – 1895	War between Japan and China
1895 – 1898	Spanish-American War
1900	2 nd Anglo-Boer War in South Africa

And furthermore: There was no terrorism of the scope we know today.

Contention

My claim is that, had the gold standard been maintained, the warring nations would have had to observe the rules of the gold standard, and, therefore, World War I would have been over in a few months. Because of the automated mechanism and the prevalent “rules of decent behavior,” financing the war on credit in a Keynesian style would not have been possible. Parenthetically, except for Karl Marx, Swiss historian Jacob Burckhardt describes Keynes as one of the great destructive forces in world history.

Soon after the onset of World War I, the moment came when the world turned to monetary fraud. Political pressure to finance the war with money created out of nothing made a sane monetary structure futile and led to the ruin of currencies – and a war lasting four years. The world lay in ruins and a young, hopeful generation was lost somewhere on the battlefields.

The collapse of the international monetary system provokes the demise of the old world order

The result of World War I signified the fall of the Old World. Reading Stefan Zweig's book *Die Welt von Gestern (The World of Yesterday)*, you will be able to see what the world looked like then, and how cruel it is today. As we are in Austria today, we should remember what the Austro-Hungarian Empire represented and denoted how orderly the situation in Western, Central and Eastern Europe was in those days. One of the most senseless things to happen in world history was the breakup of the Austro-Hungarian Empire and everything that was connected to it.

Of course, there is no such thing as a perfect world, but cross the Hungarian border from the Burgenland and enter the next bigger city, Körmend, and then you will know what I am talking about. A few years of communist rule has laid the land in ruins. Financing the war is what mainly ruined Germany, then the most thriving country. The Reichsbank financed a large part of its war effort on a short-term basis, i.e., not with long-term War Loans like the British. This fact, in addition to the Versailles Treaty and unreasonable reparation payments, led to hyperinflation, destruction of the middle class and, finally, Hitler. It set the stage for World War II.

The monetary tragedy of the 20th century

The return to the gold standard after World War I was a *fait accompli*. But it lacked wisdom and power on the part of those in charge. In 1922, at the Conference of Genoa, the gold exchange standard was introduced. Please note that it was not the gold standard that was reestablished, it was the gold exchange standard that was launched. This meant that, apart from gold, national banks could also use dollars and pounds, i.e., the currencies of the triumphant nations, as reserves. Suddenly, dollars and pounds were equivalent to gold. That was inflationary, because dollars and pounds were now accounted for twice: first, in the country where they were issued; and, second, in the country that held them in reserve.

Furthermore, it should have been known that paper-ticket currencies were in no way immune to loss of purchasing power. Therefore, they could not be permanent and generally valid yardsticks. Gold always keeps its value—paper currencies do not. Today, it is generally accepted that increased credit formation was the reason for the uncontrolled speculation in the real estate and stock markets during the 1920s. Their collapse paved the way for the crisis of the 1930s. The same thing can be said for the present stock market crisis. It is also due to immense credit formation over the past twenty years and lack of monetary discipline provided by the gold standard.

Central banks, banks and the war

When the gold standard was abandoned, central banks were the last barrier to rampant money creation as long as they were able to maintain their independence. However, in the meantime we have learned from bitter experience just how ineffective these so-called keepers of stability were. An excellent example for this is the U.S. Federal Reserve in 1913. This fateful institution was founded even before the

war. Since, the dollar has plummeted to about five percent of its former value. Central bank independence was not what it was cut out to be. Central banks became compliant pawns of governments and their constituent banks. In today's non-system, it is precisely central banks that, in conjunction with banks, make financing of wars of adventure possible by means of unlimited credit formation. There are no brakes anymore.

In his book *Jenseits von Angebot und Nachfrage (The Social Crisis of Our Time)* economist Wilhelm Röpke said: "One can venture the claim that governments very rarely had complete control over their currency without abusing it." In today's age of the welfare state, the probability of such an abuse is greater than ever before.

The tragic decisions of Bretton Woods in 1944

The world had not learned anything at all. At the close of World War II, it was decided to introduce the gold/dollar standard. A direct result was inflation in the 1970s. Again, notice the subtlety. After World War I, we went from the gold standard to the gold exchange standard with dollars and pounds. After World War II, we proceeded to the gold/dollar standard. The pound had lost its previous stature in the interim, and, next to gold, the dollar remained the only valid reserve currency and, then, only because the dollar was convertible by foreign central banks into gold on demand. It was a sign of the increasing economic power of the U.S.

The structure created in Bretton Woods gave Americans the appalling monopoly to settle their debt with paper-ticket-token money they had printed. Nobody could have resisted such temptation. When this structure collapsed on August 15, 1971, we moved to a system of floating exchange rates. That fully opened the floodgates for creation of money, credit, deficit spending and speculation.

Today's international order is a consequence

In a speech on August 7, 2002, President George W. Bush said the following: "There is no telling how many wars it will take to secure freedom in the homeland." With this comment Mr. Bush announced that there might not only be a war against Iraq, but many wars around the globe. He did not define when a war would be considered won or lost. This means that these wars may continue indefinitely. The consequences of these wars are very clear. Trade and investment activities will suffer great damage in such an environment of insecurity.

I will now take a closer look at the question of how the U.S. will be able to pay for these wars. In principle, the U.S. is bankrupt. It has been like that since August 15, 1971. That was the day America escalated its war against gold. Not unlike a banana republic, the U.S. defaulted on its sovereign obligation to redeem dollars for gold as agreed upon in the Bretton Woods system. Theoretically, the U.S. cannot be warring at all, i.e., under the strict discipline of the gold standard it would not be possible.

Because of the nation's deficit, there would not be any money left to spend on an unproductive and destructive war. The U.S.'s foreign debt is enormous. Until the

early 1980s, the U.S. was a creditor nation. Now it is a debtor nation, including a catastrophic balance of trade, which is running up an annual deficit of \$450 billion. And still the U.S. is conducting wars, which it is paying for with paper-ticket-token money, which basically is the equivalent of counterfeit. The Americans are creating this funny money themselves – and everybody has accepted it since 1971. Ever since then, and for the first time in history, the world has been living on a system of irredeemable paper-ticket-token money. So we may note that if the world were on a gold standard, the U.S. could not be conducting any wars. Why? Because then they would have to pay for them in gold. Gold, therefore, acts as a braking mechanism. Putting on the brakes has a disciplining effect.

Who, then, actually pays for these wars? The answer is simple. We all do, out of our savings and our promises of future payment, e.g., our pensions! It was no different for Kennedy's and Johnson's Vietnam War. We were all footing the bill by eventual world inflation leading to rapid devaluation of our currencies.

The 20th century

Contrary to the 19th century, the 20th century was a century of inflation, hyperinflation, trade and currency wars, waves of speculation, military conflicts, two world wars, hundreds if not thousands of local wars, hundreds of millions dead, annihilation of entire nations, mass migrations, economic ruin, and, finally, the decline of civilization.

Why are there wars? Without a doubt, economic reasons weigh in as the most ponderous in any string of motivations for international conflict that ultimately lead to war. They range from primeval struggles for hunting territories, pastures, salt mines and fertile valleys, to predatory attacks and conquests of the seafaring and trading nations, all the way to modern battles for living space, sales territories and, the most important motivation of all, access to natural resources. Internal political problems also play a major part. Often wars are started to divert attention from problems on the home front. In the Middle East, both aspects are involved: the control over oil resources and the distraction from the disastrous condition of the U.S. financial system. Saddam Hussein is only a pretext.

These wars continue to contribute to the destruction of currencies' purchasing power. While a gold coin from the times of Alexander the Great or Julius Caesar still shines as it did then, it is the fate of the purchasing power of paper-ticket-token currencies to revert to their cost of production, and that is nil. The Germans can tell the U.S. a thing or two about that. A total loss after World War I, another total loss after World War II, and finally admission to the European currency system, the Euro. All that happened within less than one hundred years.

Gold-as-money is a precondition for freedom

Not only is there a correlation between gold currencies and war, but also between gold currencies and freedom. U.S. Federal Reserve Board of Governors Chairman

Alan Greenspan wrote a well-known essay “Gold and Economic Freedom” in 1966 attesting to this. He recently confirmed that he believes this essay is applicable today.

Once we remember that one of the first official acts transacted by Lenin, Mussolini and Hitler (and, by the way, also by Franklin D. Roosevelt) was to forbid possession of gold, we recognize the context. Even today the price of gold is manipulated and kept artificially low. Wall Street bankers and their helpers have been at it for quite some time. In the U.S. a suit was filed. I cannot say more about this at the moment, but it should serve as an impulse to reflect on the present situation. These manipulations are described in my recently published book *The Gold Wars: The Battle Against Sound Money As Seen From A Swiss Perspective*.

All we have today is paper-ticket-token money. It is equivalent to counterfeit money. It does not offer a citizen any security. He cannot save enough money. If he does save, most of it is lost. The situation is worst for recipients of wages and pensioners. In the end he is forced into the arms of the (welfare) government, and he effectively loses his freedom. Politicians will mostly resist the reinstallation of gold-as-money. Röpke was right when he wrote in his book *Internationale Ordnung - heute (International Order and Economic Integration)*: “Depoliticizing money was never as vital as in the era of modern democracy.”

Conclusion

Today, when “Humanity is at a Crossroad,” as the topic of the conference characterizes the worldwide political situation, we want to address academic faculties. We want to know what they can contribute to finding a way out of this and to prevent an unimaginable escalation of suffering. As a banker, I implore you to put the gold standard back on the agenda. The people understand it intuitively. The gold standard would be my guild’s aid to bridle the power frenzy of the mighty.

Paper-ticket-token or funny money is like a drug addiction. It takes more and more of the drug to satisfy the addiction. Collapse is the final result. There is no indication today that this experiment with the equivalent of counterfeit money will end any better than earlier, similar experiments. Due to the U.S.’s economic power, paper-ticket-token money has already lasted longer than one might expect. Allow me to conclude with a quotation from a speech given in Washington D.C. in 1948 by Congressman Howard Buffett from Nebraska, father of the most successful investor of all times, Warren Buffett. The address was entitled “Human Freedom Rests on Gold Redeemable Money”:

“Our finances will never be brought into order until Congress is compelled to do so. Making our money redeemable in gold will create this compulsion. [...] The paper money disease has been a pleasant habit thus far and will not be dropped voluntarily any more than a dope user will without a struggle give up narcotics. But in each case the end of the road is not a desirable prospect.[...] I can find no evidence to support a hope that our fiat paper money venture will fare better ultimately than such experiments in other lands. Because of our economic strength the paper money disease here may take many years

to run its course. [...] But we can be approaching the critical stage. When that day arrives our political leaders will probably find that foreign war and ruthless regimentation is the cunning alternative to domestic strife. That was the way out for the paper-money economy of Hitler and others. [...] I warn you that politicians of both parties will oppose the restoration of gold. [...] Also those elements here and abroad who are getting rich from the continued American inflation will oppose a return to sound money. [...] But, unless you are willing to surrender your children and your country to galloping inflation, war and slavery, then this cause demands your support. For if human liberty is to survive in America, we must win the battle to restore honest money. [...] There is no more important challenge facing U.S. than this issue – the restoration of your freedom to secure gold in exchange for the fruits of your labors.”

Ladies and Gentlemen, these are the subtle relationships between freedom, money, intellect, war, peace and gold. Thank you very much.

Ferdinand Lips is the author of *The Gold Wars: The Battle Against Sound Money As Seen From A Swiss Perspective*.

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