

Monetary Pollution and the Gold Standard

Speech of Ferdinand Lips at the Arab Open University, Kingdom of Bahrein Branch, Bahrein May 6, 2004

Ladies and Gentlemen,

Today I am going to talk to you about the current monetary disorder. Sometimes I also call it monetary pollution. Our money has been polluted for almost a 100 hundred years and we are now paying the bill.

But I am also going to talk to you how this horrible situation could be remedied. I will give you also hope.

Let me start right away with one conclusion:

We are standing on the threshold of a historic event. We are witnessing world history in the making. We are living financial history as no generation before us has. --- We are on the verge of a historic flight out of paper into tangible assets. This financial flight will reverberate throughout the world. The flight has only just started.

It started in the year 2000. In that year the stock markets collapsed and gold started to rally. Today the stock markets, in particular the U.S. equity market, again sport bubble-like overvaluations. Central banks are printing paper money like there is no tomorrow. It's fiat paper money. Inflation, the great destroyer, is showing its ugly face again and bond markets are heading south. In some countries real estate markets resemble a bubble and a crash is looming in many parts of the world.

Why is all that happening?

It is because our money and in particular the world's so called reserve currency, the U.S. dollar is polluted. Up to the 15th of August 1971, there was never a period in history during which no currency was linked to gold. The world's history is full of examples of devaluations, coin clipping and bankruptcies. Yet it was always possible to switch to other currencies that were backed by gold. But if you disregard the Swiss franc, this was no longer possible since 1971.

All of the economic, monetary and financial catastrophes of the past 30 years can be traced back to this event.

Today money has no more gold backing. Today our money is created by the central banks and by the banking system. Our money is created out of thin air, out of nothing.

Today's system of paper money is still very young. It depends solely on the belief that the debts upon which it is based, will be repaid someday.

A single, one-off event, that could shake this belief and thus the foundation of the financial system, is a robust upsurge in the dollar price of gold.

Our non-system has made it possible that a mountain of debt could be created, the highest in the history of mankind. This enormous debt burden is the biggest threat to the future of our world economy.

Why did this debt come into existence? How was it possible?

It was possible because we have lost, or better, the world has carelessly given up the discipline of gold. We know that a rising price of gold is showing us, that there is something wrong with our money. Gold, the King of the metals is the best economic barometer. That is the entire reason why the price of gold is manipulated each day. The governments don't like it.

But we know from the history of the Gold Pool in the 1960s that gold cannot be manipulated endlessly.

At that time, the central banks tried to fix the price of gold at \$35.00 an ounce. On the 17th of March 1968 the Gold Pool collapsed and the entire pitiful experiment became the object of ridicule. The same thing is going to happen now, only worse. Gold is cheap because the governments of the world tamper with its price on a daily basis. The media talks it down or ignores it.

Analyst Doug Casey says: In 1971, at \$35, Gold was so cheap because it has been artificially depressed by government edict. Then the price was freed and it shot up to over \$800 in 1980. But today, at \$400 it is really only worth about \$75 in 1971 dollars. So it is down about 85%. Gold, the metal of Kings, is very, very undervalued. I expect this will change.

I expect the conditions of the present bull market in gold to be more dramatic than in the 1970s.

Why is this going to happen? I can name you 10 reasons:

1. A global currency war.

The world's reserve currency, the currency in which most of the world's financial transactions take place and in which the central banks have invested their reserves, is fundamentally weak. It must be propped up each day. Last year the Japanese bought Treasury paper for \$187 billion. This year in the first three months they already bought for \$147 billion. In the second week of January in two days no less than \$30 billion.

But the dollar now has cutthroat competition in the form of the Euro. The Russians are planning to sell their oil in euros.

The oil producing countries are the ones that suffer most. They are selling a much needed asset for worthless minidollars. It is a scandal of historic proportions. Future generations will talk about this and wonder.

The drama began when the gold standard was irresponsibly abandoned during the initial days of World War One. Since then the world has swung between inflation and deflation, between economic boom and bust. After the war there was the intention to reintroduce the gold standard. But it was never done. Instead the tragedy continued and in 1922 at the

Conference of Genoa the nations created the Gold Exchange Standard. This flawed construction is largely to blame for the Crash of 1929 and the Great Depression of the 1930s. The disaster continued with the Bretton Woods Agreement of 1944. At that time, the English-speaking nations dictated their program to the war torn countries. The Gold Dollar Standard was created.

Since the 15th of August 1971 when President Nixon severed the link to gold, and since 1973 when flexible exchange rates were introduced, chaos has prevailed in the global financial system. Forex markets have become a jungle.

Jacques Rueff, advisor to General de Gaulle described the reasons in his book "The Monetary Sin of the West" 1) quite accurately. He said: "Since the abandonment of the gold standard, i.e. the only system that ever worked, the world has been moving from one crisis to the next, from deflation to inflation, from economic boom to bust".

John Connally, former U.S. Treasury Secretary, a man who later ended badly, said the following in this regard: "The dollar may be our currency but it is your problem." How stupid for a man in such a high position and how arrogant.

But the scandal is now the problem of everybody. Countries who have their reserves and savings in dollars are losing daily. But they depreciate their own currencies as well. They do not want them to be strong because they want to sell their products to the American consumer. So there is a constant currency devaluation war going on. Should countries with the biggest dollar reserves such as Japan, China and Taiwan decide to diversify into other assets or even more seriously, begin to sell their Dollars, panic will break out. Why don't they buy more gold?

2. The U.S. dollar is weak because the financial situation of the U.S.A. is alarming.

It is weak because there is no longer any discipline. The discipline of gold is missing. They are living beyond their means. The U.S. trade balance deficit is now more than \$500 billion and it is rising. The Americans need \$1 _ billion of foreign savings every day in order to survive financially. That is the tribute the world is paying to the USA each day. It is a scandal. The U.S. budget deficit exceeds \$500 billion and is growing. With their worthless confetti

dollars, the Americans are buying from the rest of the world whatever they want. And we are paying them the tribute.

Charles de Gaulle called it an “exorbitant privilege”. Jacques Rueff described the arrangements of Bretton Woods for the Americans as “the wondrous secret of deficit without tears. They could give without taking, lend without borrowing and buy without paying.”

Many feel that this situation, which is nothing but a fraud of historic proportions, cannot go on for much longer.

3. Dramatic money supply increase in the USA and the rest of the world.

When the global economy went into recession, the markets have been flooded with liquidity. Greenspan keeps pumping out money as if there were no tomorrow. Governor Bernanke of the Fed clearly stated last fall that the “wonderful” printing press would be put to work if a depression threatened.

“In the long run we are all dead,” said the great cynic Keynes. “Après nous le déluge (After us, the flood) said the French King Louis XIV. With this flood of paper money and credit, the foundation has been laid for the next upsurge in the prices of goods and services. Deflation is no longer the problem but inflation is now the problem and one day maybe hyperinflation.

4. Most stock markets are overvalued and therefore dangerous.

Former Fed chairman Paul Volcker, the man who helped to create the SDR's, once said the following: “The fate of the world economy is now totally dependent on the growth of the U.S. economy, which is dependent on the stock market, whose growth is dependent on about 50 companies, half of which have never reported any earnings.”

The flood of money has found its way into the stock markets. Therefore they are overvalued and dangerous. Corporate insiders, which means the people who are in the know, have lately been dumping their shares at unprecedented levels. The public is still hyper-bullish and will certainly be left holding the bag when the markets break. This will be very positive for gold. People around the world will want to buy gold.

5. Negative “real” interest rates are positive for gold.

The flood of money has resulted in extremely low interest rates. When the rate of inflation exceeds interest rates, fixed income investments become unattractive. Historically, such conditions have always been positive for gold.

6. A deficit between gold production and demand – gold production is declining.

Gold mine production amounts to 2,500 tons a year and is falling. The demand for gold comes to 4,000 tons. According to some estimates even 5,000 tons a year. This deficit has been made up by central bank selling and even more by central bank lending. But gold production is expected to decline by at least 30% in the next ten years. In view of the low gold price, exploration was no longer attractive and has fallen sharply.

The head of Newmont Mining, Pierre Lassonde said that even if the price of gold rises to \$1000 an ounce, it will take 4 to 7 years until a new gold mine can be put into service. Without higher gold prices there will be no new gold mines. Without new gold mines there is not enough gold.

7. Huge short positions, a dramatic crisis at the central banks.

The central banks wanted to earn some money with their gold reserves. They were talked into it by the politicians and the bankers. So they entered the business of gold lending. They lent it to the bullion banks. It is estimated that 10,000 to 16,000 tons have been loaned out. This gold is gone because the bullion banks sold it. It is now missing. However the central banks in their balance sheets still show swapped gold or gold that was loaned as if nothing had happened, as if it were still in their coffers. The IMF allows them to perpetrate this deception. It is deception because one third to one half of the official gold reserves is now missing. But remember gold still has value to the central banks. They are going to lose confidence in the \$ and other currencies. So they will again begin to look at their gold. Finally even the public is beginning to realize what is going on, that the gold has been lost.

I therefore make a forecast. Within 2 to 3 years the central banks will again become buyers of gold. When the world realizes this change, there will be a gold panic.

8. The gold market is very small.

There is too little gold. The stock market value of all listed gold mines is only about \$100 billion, or about a third of the value of General Electric or maybe a fourth of the value of Microsoft. In contrast, global financial assets (i.e. money, bonds and stocks) add up to around \$150,000 billion or \$150 trillion. If only a small part of this mountain of paper money wants some gold, the price of gold and gold shares will explode.

9. Gold is money and heading east, the Golden Dinar, India and China.

Dr. Mahatir Mohammad, former Prime Minister of Malaysia, I heard, was for many years a supporter of a gold currency, the gold dinar. In history the gold dinar was the currency when the Arab empire and culture spread from the Middle East to North Africa and Spain. The gold dinar is supposed to become an international currency. It would become a true competition of the paper dollar which is worth nothing. The oil producing countries are giving away their oil wealth for worthless paper. Worthless paper that can be printed out of thin air. He reasoned that one of these days the oil producing countries will run out of oil. Therefore they should be paid in gold now. Gold will remain while the dollar goes bust. China has liberalized its gold and silver markets and India is the biggest buyer of them all. Meanwhile the Western countries are selling.

10. The power of cycles or the law of nature.

In the bible there are the seven fat years and the seven lean years. There are cycles. There have always been cycles in human life. The Russian economist Kondratieff has found that such a cycle does last about a generation. One cycle has 4 phases and one can compare them to the seasons of the year. The autumn or harvest phase came to an end in the year 2000. We are now in the winter phase. This is the worst phase. Since each Kondratieff phase lasts about 15 years, we are now facing very difficult times ahead, the Kondratieff winter phase.

What is the best thing for investors to do during the winter phase. Richard Russell, when he was asked about the best investments during the winter, once said: The two best investments are two things that people do not have, cash and gold. Gold is money and has

always been the best money during the 5000 year history of mankind. One can use it to buy the necessities of life. Gold is diametrically opposed to paper.”*

1. Conclusion:

I believe we are looking at a gold bull market of historic proportions in the years to come. Corrections such as the one we are seeing now are not only normal, but also trivial. The price of gold in recent weeks has dropped because supposedly the U.S. economy is growing. The jobs market is said to be improving and according to Mr. Greenspan inflation is under control, interest rates will increase and that the “dollar” will strengthen. Nothing is further from the truth. Furthermore markets are terribly volatile because hedge funds have nearly \$1 trillion under management which they then leverage. With this ammunition they can cause large swings in the markets, and especially in the gold market.

You should use such weakness to buy bullion and mining shares. There is every reason to believe that the rise of gold mining shares will be wilder, more than the internets were in the late 1990’s.

2. Conclusion:

So far I have not talked about Silver.

I am even more bullish about silver than I am on gold. Silver has served as money for thousands of years. For thousands of years in history, the ratio between gold and silver was between 10 and 14 to one. One ounce of gold for 14 ounces of silver. Then something very dramatic happened: the Franco-Prussian War of 1870/71. With it came the end of the bimetallic system. (Under this system gold and silver served together as money.) The victorious Germans received so much gold from the French that they decided that from now on gold alone should serve as money. After all gold was also much easier to control than silver because silver is in every household. So silver no longer played an official monetary role in most countries. The result was that the natural order between the two metals, reflected by the historic ratio over thousands of years, was destroyed. The ratio began wild gyrations and from now on fluctuated between 100 and 15. In 1980, gold briefly went to

\$850. Silver reached over \$50. So the ratio was about 17. During the bear market of the precious metals of the 1980s and the 1990's the ratio went as high as 100. In the autumn of 2003 it was between 70 and 80. At the beginning of 2004 it came back to the 60s and is now around 56. The natural order however was not completely destroyed. Why? The ratio will undoubtedly go down to between 15 and 20. It always does.

What does this mean for the price of silver? The Dow theorist Richard Russell feels gold and the Dow will eventually meet at \$3000. In other words 1 to 1. If we are to reach \$3000 gold and the gold/silver ratio is then at 20, you can figure out yourself how high the price of silver can rise.

This is the one overriding reason why the outlook for silver is much more attractive than for gold.

Other reasons are:

All the gold that ever was produced is still here while most silver has been used and all cannot be recycled. Applications in industry of this wonderful metal are increasing daily. Also silver is always produced as a by-product of either gold, zinc or copper. It is therefore very difficult to increase the silver production rapidly.

There has been a deficit between supply and demand for many years. Government stocks are at an all time low. Furthermore silver is as manipulated as gold and there is a huge short position which may be very, very explosive.

So the outlook for silver and silver shares is much more spectacular. The total market capitalization of listed silver shares is only about \$15 billion and this is very, very little money. Nobody really follows the silver shares. Therefore, once the public gets involved, prices of silver will explode and the shares will go to the moon. For all these reasons I am not only looking for a gold bull market of historic proportions but also for a spectacular silver bull market in the years to come. And it will very, very wild. Silver is the restless metals as Prof. Jastram once said.

We now come to the second part of my speech. In the first part I explained the reasons why I am so bullish about gold and silver and so bearish about the stock and bond markets.

Now I want to tell you what could be done to get the world out of this mess.

Why do we have all those trade deficits?

Why do we have all those government deficits?

Why do we have inflation?

Why did we have deflations?

Why are currencies constantly losing value?

Why do we have recessions and why do we have depressions?

And last but not least: Why do we have wars?

Why:

The answer is --- because at the beginning of the First World War the world has given up the gold standard of the 19th century. The gold standard was given up in a few weekends. They nations wanted to finance the war. There is another important date and that is the year 1913. 1913 is a very important date because this is the year the Federal Reserve System was founded supposedly to keep money stable. We know that didn't happen because since the Federal Reserve System was founded the U.S. dollar has lost more than 95% of it value!

The world has given up Sound Money. With it the world has built up the welfare state it cannot finance. We have no more Law and Order. We have given up everything and we are running the risk of losing everything. The world is running the risk of losing its future if we do not go back to sound money, honest weights and measures. Dr. Mahatir Mohammad wants the Golden Dinar. The entire world has to go back on a Golden future. If we don't, the world will have no future.

So what is the Gold Standard really?

And what does it mean to the world, to you and to me? I will give you the answer and I will now cite from my book "Gold Wars". The book was published in 2002 by The Foundation for the Advancement of Monetary Education FAME, New York (www.FAME.org) 2)

I am citing:

“Those who are de facto in charge of the world’s monetary system, the large banks and the large investment banks, will not agree. In this respect, I have no doubt. They are reaping enormous benefits from fiat money. – In the U.S. more than \$600 billion in 2000 alone. – They will not easily relinquish those revenues. But the question remains: Do we want to repeat the catastrophic blunders of the last century or do we want to learn from history and avoid them? That is all. Mainstream thinking is not enough and never will be. All the great people of this world were independent thinkers.

There are plenty of quotations and wise words that could be mentioned here, but let us mention just two of them. Investment advisor Harry Schultz, publisher of The International Harry Schultz Letter, has written one of the best definitions of the gold standard:

Gold is the essential linchpin for our *individual* (not group or nation) freedom. Gold belongs to the monetary system as a *governing* factor. We belong back on the gold standard. I used to compromise and say a *quasi-gold* standard will probably do, a modified Bretton Woods version. And that may be what will evolve, but in my view we should fight for a pure gold-standard, the old-fashioned form, because it worked! And not just for fiscal reasons! It *forced* nations to limit their debt, spending and socialist schemes, which meant sound behavioural *habits* were formed around those limitations, and those *habits* rubbed off on everyone. People were more honest, moral, decent, kind, because the *system* was honest and moral.

Today we have cause and effect of the opposite standard: *no* limits on what governments can do, control, dictate; no limit on government debt, welfare or socialist schemes. There is no governor on the government. This habit rubbed off on the public, causing them to go into debt, lose respect for the system and morality. The effect brings more divorce, fraud, crime, illegitimate births, broken homes. When the money of any country loses its base/backing there is no standard for any behaviour. Money sets a standard that spreads into every area of human activity. No paper money *backing*, no morality. That is why gold coin money worked so well and why the U.S. moved into paper money very slowly, carefully keeping the paper-\$s backed by 100% gold. But slowly, like slicing a sausage, that backing was removed in stages, ‘til now there is none. The effect of this cause is all around us.

Violent films reflect violent society reflect no respect throughout society. Layer by layer, we are corrupted when money loses certainty. Today's stock market bubble is part of the scene as will be tomorrows mega-crash and mega-recession.

Big brother was made possible through the absence of automatic controls and loss of individual freedom via non-convertible currency. So, pass the word. Fight for gold. Not for profits, though they are helpful and help us fight for individual freedom, but for a future that returns to sanity in various standards. If we have a gold standard we get golden *human standard!* The two are intertwined. They are the ultimate cause and effect. God blesses.”

General Charles de Gaulle, President of France, gave France the greatest gift he could offer: He renewed the country's confidence. On the 4th of February 1965 he said: “The time has come to establish the international monetary system on an unquestionable basis that does not bear the stamp of any country in particular. On what basis? Truly, it is hard to imagine that it could be any standard other than gold. Yes, gold whose nature does not alter, which may be formed equally well into ingots, bars or coins; which has no nationality and which has, eternally and universally, been regarded as the unalterable currency par excellence.”

Thank you!

- 1) Rueff ,Jacques, “The Monetary Sin of the West”, New York: Mac Millan, 1972
- 2) Lips, Ferdinand, “Gold Wars – The Battle against Sound Money as Seen from A Swiss Perspective”, New York, FAME The Foundation for the Advancement of Monetary Education, 2001