HAWK Talon

HAWK 100

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Accounting for Midas.

Monetarists advocate controlling economic variation by changing money supply. Keynsians advocate government intervention to stimulate demand or to stabilize prices. Both theories profligate without a tenable reserve to back money. Monetarists and Keynesians claim not enough gold exists to return to a gold standard. Let's explore their claim.

A troy ounce is 31.1035 grams and a metric "tonne" is 1000 kilograms, so one tonne is 32,150.746 troy ounces. Gold recently traded at $1,891.90 per troy ounce or $60,825,996 per tonne.

Estimating total global gold—mined since ancient Egypt and Mesopotamia through today—is difficult. Yet, data from the World Gold Council and GFMS Ltd, suggests total global gold supply is about 178,500 tonnes or 5.8 billion troy ounces worth $10.9 trillion. The US gold reserves are just 8,134 tonnes worth $500 billion.

Estimating global monetary base is even more difficult. The US monetary base is $9.3 trillion (M2—currency, bank deposits, savings accounts and money funds). The European Central Bank says it has €8.4 trillion ($12.2 trillion). EU members hold 10,203 tonnes worth $621 billion.

Global gold covers barely 50% of two of the world's 193 currencies, and each is backed by less than 5% gold reserves. A new gold standard would require monetary destruction or Midas's resurrection.

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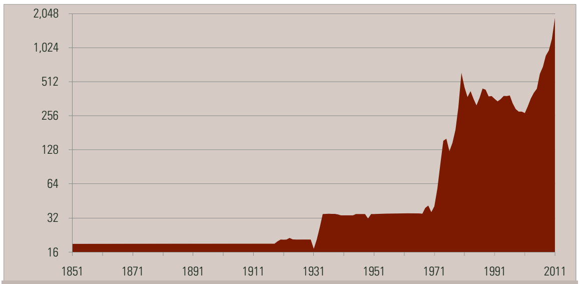
Act Four, Substandard and Poorer.



Annual average price of gold in US dollars. Logarithmic scale shows price doubling nearly six times since 1971. Source: World Gold Council.

Today, we witness the specter of a super-committee hurriedly assembled to tackle insurmountable debts that accumulated from domestic programs of Presidents Bush and Obama and wars in Afghanistan and Iraq. Forty years ago, August 1971, President Nixon secretly assembled another super-committee of sort to tackle insurmountable debts that accumulated from the 1960s Great Society and the war in Vietnam. That super-committee's decision to abandon the gold standard under the Bretton Woods system set the stage for a five-act, modern tragedy.

Emblematic of Nixon's shrouded administration, the play opens behind closed curtains. When the curtains withdraw ...

Act One, Stagflation. Abandoning the gold standard converts the US dollar into fiat money. *Investopedia* calls fiat money that which has no intrinsic value and is not backed by reserves. It tends toward a worthless state as inflation erodes any worth and the issuing government simply prints more faith-based paper. On cue, stagflation—high unemployment coupled with high rates of inflation—takes the stage to sing a 1970s psychedelic chord. Gold doubles four times. Consumer prices inflate 8.5% on average per year, and unemployment rises to 10.8% by 1982.

Act Two, Gold Falls. The play continues through the 80s and 90s with fiscal reforms enacted by Reagan which accrue benefits during Bush 41 and Clinton. Reagan's tax cuts and deregulations enable economic expansion and a strong dollar emerges. A vibrant domestic economy reinforces dollar strength and position as the world's reserve currency, While the audience falls in love with investments in newer technologies that harness the personal computer and internet, gold falls from center stage. Other commodities, energy, and real estate are all booed off stage and critically dismissed as too representative of the "old economy."

The audience rushes to intermission with Y2K-compliant computers and stocks crumble 49% between 2000 and 2002.

Act Three, Tragic Flaw. Curtains open on the dawn of the 21st century with a tragically heartless attack September 11, 2001. The nation falters and reverses course. Playing as heroes, Presidents Bush and Obama arrive sequentially with "compassionate conservatism" and "hope and change." They enact enormously expansive programs, authorize government to intervene for favored firms deemed "too big to fail," and devalue the dollar for political advantage. Tragically, they assume the world has unconstrained tolerance for their fiscal folly.

Act Four, Substandard and Poorer. A debased dollar destroys wealth as it buys fewer commodities, transfers into less foreign currency in global trade, and weakens US positioning. To illustrate, Fiat owns Chrysler, despite Europe's troubles, and S&P lowers its US Treasury rating to AA+ acknowledging unscrupulous politics and unsustainable policy.

Act Five, Hero Returns. Classical economists—like Wayne Jett, founder of Classical Capital LLC and author of *The Fruits of Graft*—call for the return of the gold standard saying the nation has already paid a "horrendous" price without it. Monetarists and Keynsians counter that the world's gold supply is insufficient to support the current monetary base. We explore the implications of their counter argument at left. Given those implications, Hawk100 sees no stronger argument in favor of gold, and supports gold's return as the constitutional standard "Tender in Payment of Debts" public and private. At a minimum, central banks should hold firm reserves to back every currency unit.

By Richard Clemens, CFA, *President*