The Gold Standard

The journal of The Gold Standard Institute

Editor	Philip Barton
Regular contributors	Rudy Fritsch
	Sandeep Jaitly
	Louis Boulanger
Occasional contributors	Philip T
	Thomas Allen

The Gold Standard Institute

The purpose of the Institute is to promote an unadulterated Gold Standard

www.goldstandardinstitute.net

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Editorial

This Time

There are some significant factors that differentiate the current crisis from the 1929 model. One of them is that this time the credit expansion that caused the bust has been much larger. Another is that this time the Fed has refused to ease up on its monetary debasement which means that we will probably end up with a hyperinflation. Another is that this time it will be a worldwide collapse, and finally, and most importantly, this time the Fed will not be able to blame it on gold.

Since 1971, when Nixon defaulted on the gold obligations of the US, consciousness of the monetary virtues of gold has fallen to encompass only a minute percentage of the population of the western world. Whilst this has presented a wonderful opportunity to swap paper pseudo-money for real money at fire-sale prices, it is also a stark and sobering reminder of the hundreds of millions of people who have zero real money in their possession.

The traditional inability of politicians to be responsible for the results of their legislation means that the finger-pointing will become ever more frantic as the crisis worsens. Who will be the recipient of the blame? The answer is obvious and the process has already started.

The bankers will wear this one. Whilst many of them, along with some of the financiers and Wall Street types have made out like pigs, it needs to be remembered that they were not the cause of this crisis; they were merely weak characters responding to a bad incentive. The cause, the incentive, was irredeemable paper money. A dishonest money will always create dishonest incentives and lead to a dishonest system.

Putting bankers and such people in the stocks, enjoyable though it might be, is not the solution to the problem. At The Gold Standard Institute we remain firmly focused on the problem… irredeemable paper money.

The attempt by governments to blame the bankers is an attempt to reduce it to a problem of specific people and thus encourage the blame game. There will always be people of weak character: that cannot be avoided. What can be avoided is a monetary system that rewards such people and grants them wealth and high station. The problem is not specific people; the problem is the paper money system itself.

Another thing that is different from the 1929 model is that this time, because of the globalised nature of the collapse, the public will come to recognize that no government, irrespective of its brand name, can be trusted to honour its paper money commitments. It is more than just the system of irredeemable paper money that is collapsing.

News

Dailycaller.com reports on presidential candidates being pushed to declare their hand on the Gold Standard.

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The Nassau Guardian: Talk of a return to the gold standard has even reached Nassau.

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GATA: GATA Chairman Bill Murphy and secretary/treasurer met in Washington with U.S. Rep. Ron Paul, R-Texas, chairman of the House Subcommittee on Domestic Monetary Policy and Technology, and two of his staff members. GATA's work and the information produced by their recent successful freedom-of-information lawsuit against the Federal Reserve was reviewed and he was urged to press the Fed for accountability, particularly in regard to its manipulation of the gold market, its involvement with the U.S. gold reserve, and its secret gold swap arrangements, the latter admitted to GATA by Fed Governor Kevin M. Warsh.

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Wall Street Journal: Bid to use Gold as collateral for trading with clearing houses progresses.

MineWeb: Headed for a 'Gold Standard System' by 2014. 80 Years on from the Great Depression, Ian Gordon reckons financial cycles suggest we are due for another collapse, but this time even worse. Gold and gold stocks may provide protection.

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Chris Powell, GATA: Gold Reserves - Sell Them All

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Washington Post: Update on Utah making gold and silver coins legal currency.

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MineWeb: Zimbabwe to move to a gold standard! "There is a need for us to begin thinking seriously and urgently about introducing a gold-backed Zimbabwe currency that will not only be stable but internationally acceptable," Gono said in an interview with state media. "We need to rethink our gold-mining strategy, our gold-liberalisation and marketing strategies as a country. The world needs to and will most certainly move to a gold standard and Zimbabwe must lead the way."

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A gold article from the BBC in the UK. Now that really is news!

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YouTube: From RT America - Washington DC - Return of the Gold Standard?

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Personal Liberty.com: "South Carolina Lawmakers want to bring back the gold standard. Both the South Carolina Senate and House are reviewing the Sound Money Legislation, which would make gold and silver coins legal tender in the State."

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GATA: "The Federal Reserve System paid GATA $2,870 in attorney's fees and costs for illegally withholding a gold-related document GATA sought in its federal freedom-of-information request and

lawsuit against the Fed in U.S. District Court for the District of Columbia."

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Jim Grant, publisher of Grant's Interest Rate Observer, the long-running finance journal, told a conference in Edinburgh that returning to a gold standard would "restore the price mechanism to its proper place."

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International Business Times: Could Ron Paul's Campaign Trigger a Return to the Gold Standard?

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Money Web.com: South Africa should think big and establish a gold-backed rand.

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Two items from Peter VC

NWT Mint: "It was well hidden in the Obama Social Health Care program: All purchases of gold and silver above $ 600 would have to be reported.... so the PTB would know who owns how much... not anymore."

New York Times: Gold Mania in the Yukon… a great story on the new gold rush.

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Newsroom America: Steve Forbes, the founder of one of the nation's premier economic magazines and onetime GOP presidential contender, says he believes the nation will return to the gold standard within five years because doing so would solve a number of economic, fiscal and monetary issues.

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Finally, a unique business opportunity to employ a monetary systems researcher, specialising in the role of gold, located in Austria.

He is a practising Lawyer and has a degree in Law at Padua University and a Masters in Austrian School of Economics at URJC Madrid. Speaks English, French, Spanish, Italian and reasonable German.

Expressions of interest to: pb@monetarymetals.org where they will be forwarded to the intended party.

False Belief #5: Deficits Don't Matter

There should be no further need for proof that ignorance rules the day than to observe the ongoing assertion from the top, or from those who should know better, that deficits don't matter. It boggles the mind to see how many people still seem to cling to such a destructive delusion. Unfortunately, the perpetrators of this false belief appear to be knowledgeable people. But are they?

For knowledge to manifest, reason must be operating. The very assertion that deficits don't matter does not in itself seem very reasonable. What is a deficit? Broadly, it can be defined as an excess of expenditure over revenue or the amount by which a sum of money falls short of the required or expected amount. In other words, a deficit represents a deficiency of some sort, an actual *imbalance* of payments. Unsettled deficits, if they persist, can only bring disorder.

Of course, common sense tells us that deficits do matter. Unfortunately, it has been taken for granted for far too long by men of the highest degree of education that they don't. As a result, human action has been misdirected long enough for bad habits to come in the way of progress. Disorderly fiscal and monetary policies have become the order of the day. Now, much unlearning must take place before the truth of the matter can again be recognised.

It is very convenient for politicians and money men to fabricate and maintain the illusion that deficits don't matter and that we can all continue to live beyond our means, without ever having to face the consequences. Deferring the inevitable is easy; dealing with it is an altogether different matter. One is irresponsible and selfish; the other is mindful of one's duty to reason and take responsibility for one's actions.

These days, all one seems to read about when it comes to sovereign governments is deficits: budget deficits, fiscal deficits, trade deficits, current account deficits, and so on. But which deficit exactly does not matter? Well, apparently, none of them matter.

Those who assert this are either the victims of a serious knowledge deficit or in breach of their duty of care. A consequence of this is the global financial and monetary disorder we find ourselves in today.

Globalisation or global free trade makes sense when prices are determined on the basis of sound money and any imbalances between nations are settled. But what we have today, thanks to unsound money since at least 1971 and unsettled trade deficits since then, is a percolating disequilibrium of gigantic proportions that can only end badly for all creditors.

Debtor nations must maintain the belief that deficits don't matter. Their ongoing 'deficit spending' depends on it. Believing such nonsense is tantamount to committing seppuku.

Louis Boulanger

Louis holds a B.Sc. from Laval University in Canada; is a Fellow of the Canadian Institute of Actuaries and the New Zealand Society of Actuaries; and is a Chartered Financial Analyst.

Prior to coming to New Zealand in 1986, Louis worked for nine years with a global consulting firm based in Montreal, Canada. In New Zealand, Louis worked for another global consulting firm for 18 years, including as Chief Executive of New Zealand operations for five years. In 2006, he launched his private practice.

Louis is also Founder & Director of LB Now Ltd, which provides independent investment advice to private and institutional clients, facilitates the purchase of bullion for private and institutional clients as an authorized dealer for BMG BullionBars and also helps firms comply with GIPS.

For more information of LB Now's services or to subscribed to Louis' e-letter 'Prosper!' see the contact details below.

louisboulanger now
Freethinking Investment Strategies

P.O. Box 25 676, St Heliers, Auckland 1740, New Zealand
Ph: +64 9 528 3586 Mob: +64 275 665 095
Email: louis@lbnow.co.nz www.lbnow.co.nz

From London

the gold market, quoted in United States Dollars has had a pretty lacklustre month. Silver has fared slightly worse. The gold/silver ratio was 37 at the time of the last journal. Subsequently, it reached a high of 45.69, before falling back to its current level of 40. Where is the likely trajectory of the ratio from here? What is the likely path of the metals against the United States Dollar? A feature which was very evident in 2006 – a gold price escalating in non-Dollar related currencies – is likely to resume soon. Many a commentator will soon be scratching their head as the Dollar advances with gold and silver in tow.

The recent correction in the whole commodity complex has reminded the market of how fickle the bid on commodities can be. Don't forget that commodities apart from gold and silver have quickly declining marginal utilities. Should there be a small disturbance in the demand for a substance whose marginal utility falls quickly, the price of the substance can fall more sharply than a substance of slowly declining marginal utility. Gold and silver should not be placed in the same bucket as soft commodities – or other commodities generally – just because their price movements are similar. This is a result of the grossly overextended credit system rather than anything else.

Sandeep Jaitly

The 'Gold Basis Service' is a monthly subscription newsletter that describes movements in the gold and silver bases. The service offers forewarning of potential exchange default - as well as of significant changes likely in the gold price and gold-silver ratio from movements in the bases. Along with the monthly gold basis service is the quarterly 'Course of the Exchange' economic commentary. This commentary relates to general observations from a Mengerian perspective on the current market place for global equities; government paper and other goods.

The cost of the subscription is US$490 per annum. Full details can be found at Bullionbasis.com.

When is 'Crunch Time'? (Part 1)

The most often asked questions in all the talks I have given and attended is, 'when'? Once the audience understands that the world economy is on the road to destruction, the one thing they want to know more than anything else is 'when do we get there'?

Will the collapse come next month, next year, or next decade? Unfortunately, this question is impossible to answer. It's like the proverbial 'straw that broke the camel's back'; as straws are piled on, no one can predict ahead of time which straw will cause the rupture; the very next straw, perhaps a few hundred more... or perhaps another bale.

We know that Crunch Time approaches, and we can deduce that the only way to avoid a rupture is to stop piling on the straws. Today, the 'straws' of increasing debt are being piled on at an ever increasing rate, a guaranteed way to cause a rupture... but when will the break happen?

There is no way to know; a consequence of the non-linearity of real-world economics, a non-linearity that is rarely addressed, except by 'rogue' economists like Professor Fekete. No projection of linear trends can possibly predict the exact time of non-linear events.

In reality the only way to discover the timing of such unpredictable events is to 'run the experiment'... and find out. In other words, keep piling on the debt, and see when the 'camel's back breaks'... not a very smart way to run the world economy, is it?

The only guide to non-linear events is to be found in history. If we see several camels get their backs broken, then we can develop some idea of a camel's ability to carry debt... er, straw...... and can guess when THIS camel will collapse.

Unfortunately, or perhaps fortunately, there has only been one Great Depression, so our sample base is too small to make statistically sound projections. Nevertheless there were many 'depressions' before the Great Depression, and we must study them if we are to learn any lesson from history.

Looking back at the nineteenth century, there were 'panics'; short lived, sudden dips in the economy. Today, the mainstream calls this series of dips the 'business cycle'; but is this name truthful, or is the reality something else?

From a strictly logical viewpoint, what could cause a general dip in all businesses? What correlation is there between the business of the apple grower, the tailor, and the plumber? What common factor could affect the majority of all disparate businesses in the economy?

The only factors common to all business are money, credit, and profit. No matter what the business produces, whether a consumer product, a producer product, or a service, all business is concerned with and affected by these financial factors. Clearly, 'business cycle' is not a very informative or descriptive name for the cyclical pattern of 'boom and bust'.

Under the Gold standard practiced in the nineteenth century, the quantity of money was fixed; the supply of Gold (money) only grew as fast as it could be mined. This fact is one of the key reasons why Gold is the very best money possible; it's enormous stock to flows ratio. Mine supply adds no more than about 2-2½% to the existent stock every year. In view of this, sudden changes in the money supply could not be the root cause of the boom-bust cycle.

We are then left with only one variable that effects all business; credit. Unlike money (Gold) credit is variable and can increase or decrease, independent of money supply. So, we have the phenomenon known as 'cheap money' or 'easy money'... but in fact, this refers not to money itself, but to credit... that is, borrowed money. The so called 'business cycle' is better called the credit/debt cycle.

Ever since the creation of the Bank of England, the natural availability of credit has been interfered with; under an unadulterated Gold standard, credit is NOT created or controlled by central banks, or indeed by any banks. The availability of credit under the unadulterated Gold standard is strictly regulated by the voluntary participants of the market.

No one is coerced or fraudulently led to lend or borrow; interest and discount rates are not set by a central banker, or by a politician, but explicitly by the

collective action of market participants. There is no such thing as 'easy money': there is only money that is lent at a rate suitable, or at least acceptable to both the lender and borrower. If the rate is not acceptable for either lender or borrower, the loan is not made. This is the very definition of a free market.

Bankers are motivated by the desire to maximize their own profits, which they can increase by lending out more money. Unfortunately for them, they can only lend Gold money up to the quantity on hand; either in the form of their own capital, or deposits.

To lend what does not exist takes some ingenuity, or perhaps fraud. Banks discovered they can lend far more 'money' in the form of paper bank notes, of promises of Gold, then Gold itself. To lend more, just print more. The act of printing bank notes as substitutes for real money bypasses a vital market mechanism; the feedback loop that controls credit by naturally setting interest rates.

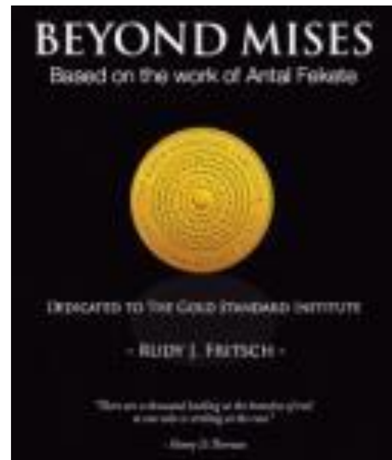
Bank notes make up the fiduciary component of the nineteenth century Gold standard; a component based not on Gold, but on promises... thus the name, which comes from fiducia meaning trust... 'trust me, I will pay you back'... even though I have lent you something that I do not have!

The panics went something like this; the bankers, working to maximize profits, lent more and more bank notes into circulation; at some point there were too many notes... and the process suddenly reversed. Borrowing collapsed, and the boom built on false indications also collapsed. Credit was reduced to reasonable levels, and the economy could start to grow again. These panics resolved rather quickly, and none of them were called 'Great'... what turned the 'Panic of 1929' into the Great Depression?

[Editor: This fascinating piece from Rudy Fritsch had to be broken into two parts and will conclude in July's issue.]

Rudy Fritsch

Rudy's book *Beyond Mises* was written to make Professor Fekete's work and Austrian economics accessible. To bring his wisdom to the majority who are not economists by training or inclination and to show that at the root, economics is actually simple and understandable. It can be ordered directly from http://www.beyondmises.com/



Are Real Bills Real Money?

Rothbard, Mises, and most other economists of the Austrian school claim that real bills of exchange are not money in the true sense, i.e., they are not true money substitutes. "The endorsement of the bill is in fact not a final payment; it liberates the debtor to a limited degree only. If the bill is not paid, then his liability revived in a greater degree than before."[1]

A bill of exchange is similar to a check except that one private individual draws it on another private individual rather than himself, or, more correctly, the bank that holds his checking account. Checkbook money, which most economists recognize as money in the true sense, has the same feature as bills of exchange. If the person who signs the check fails to honor it after the endorser cashes or deposits it at a bank, the bank comes after the endorser to refund the money. If the check bounces, the liability of the debtor, i.e., the signer, is "revived in a greater degree than before." The two differ only in degree.

Bills of exchange are a spontaneous creation of markets to facilitate the movement of goods. Under the real bills doctrine, a real bill of exchange is

created when the retailer (drawee or acceptor) accepts a bill exchange drawn by the supplier (drawer). When the retailer accepts the bill, he creates commercial money. The bill now functions as money similar to the way that a check functions as money. Commercial money can be, and frequently is or was, used to pay debt and buy goods. It serves as a highly marketable store of value until it matures.

As a store of value, it is superior to a check because its value increases daily. Moreover, it is usually more liquid than a check. Whereas a check seldom passes through more than one or two hands before it is returned for payment in gold, a bill may pass through several hands before payment in gold. Like a check, it can be used as a medium of exchange. However, its use as a medium of exchange is limited because bills are written in irregular amounts and generally for large sums. Commercial money (real bills of exchanges) is money in the same sense that bank money (bank notes and checkbook money) is money.

Unlike checks, bills of exchange often circulate especially in the arena of foreign exchange involving different currencies.

Although bills of exchange are used as money, their use is cumbersome. Bank notes come in convenient denominations and are more versatile. They can easily convert bills of exchange into smaller pieces. Unlike bills, which have expiration dates, bank notes do not. Bank notes can circulate indefinitely. People accept bank notes more readily than commercial money, i.e., bills of exchange. Therefore, bills are usually sold to banks and converted into bank money, bank notes and checkbook money, which functions as money in the sense that most people generally accept bank money as final payment.

The above discussion assumes the true gold-coin standard accompanied by a decentralized competitive banking system without special privileges.

1. Ludwig von Mises, Theory of Money and Credit, new ed., tr. H.E. Batson (Irvington-on-Hudson, New York: The Foundation for Economic Education, Inc., 1971), p. 285.

Thomas Allen

New Austrian School of Economics

Announcing the third session of Professor Antal E. Fekete's New Austrian School in Munich, Germany.

Dates: 20-29th August, 2011
Venue: Maria-Theresia-Str. 20, Munich
Speakers: Prof A.E. Fekete (Hungary)
Sandeep Jaitly (UK)
Keith Weiner (USA).

Subjects to be covered include:

- The unadulterated gold standard.
- Inflation versus deflation – simple terms for non-simple action.
- The gold/silver market & gold/silver basis.
- The creation of the interest rate spread.
- Gold against other assets.
- The future of the bond market.

For further information regarding this event, please contact the organiser Mr. Ludwig Karl at NASOE@kt-solutions.de

Protection of Savings Against Inflation in Malaysia

Inflation! Inflation Everywhere!

Over the years, many in Malaysia have experienced continuous surges in the prices of food, energy and houses. Based on data in the official website of the Department of Statistics, Malaysia, the average inflation rate is 2.2% p.a. or a total inflation of 24.4% compounded over ten years from 2000 to 2010.

In the first quarter of 2011, inflation rate was 2.8% y.o.y. and in March 2011, 4.7% y.o.y. for food. Many Malaysians doubt the official inflation figures, as their personal experience indicates much higher rates of increase for grocery energy and housing bills.

As a result, many young people complained rapid inflation has put house ownership beyond them.

According to the National House Buyers Association, the property prices in urban areas in Penang and Kuala Lumpur rose by up to 40% last year, mainly fuelled by low interest rates and a surge

by speculative buying. The average price of a Kuala Lumpur house is now about RM485,000 or roughly 9 times the average urban household annual income of RM54,000.

The Demographia International Housing Affordability Survey rates property prices of 5.1 times or more on median income, as "severely unaffordable".

Many with savings feel that their money is buying less and less. Many Malaysians have used a number of ways to protect their savings against inflation. The following are some common and popular methods.

Note: As the effect of debasement of currency on prices is not always immediate, we should not be distracted by short term volatility of rates and prices, hence only the long term average rates (compounded) over the last 10 years are used to discuss their effectiveness.

1. Buying houses

Many in Malaysia have bought houses to live in as well as for investment. One can put down 10% deposit, and gets a housing loan if one's income qualifies for it. The current mortgage interest rate is about 5% per annum. The rental yield ranges from 4% to 7% p.a. which is sufficient to cover interest payment.

Over the decade (2000-2010) the average rise in price of houses is 3.5% p.a. (Data source: Valuation and Property Services Department, Malaysia-JPPH). This rate is slightly higher than the average official inflation rate of 2.2% p.a.

In the last 12 months, the price of houses have surged, with Kuala Lumpur house price index Surging by 9.9% y.o.y. in Q3 2010.

Many speculators have bought houses using flexible housing loan requiring only minimum monthly repayment of interest), resulting in a levered gain of 10 times in a rising market over last 10 years.

On average, an investment of RM100,000 in a million Ringgit house in Malaysia in 2000 will yield a gain of RM410,000 in the year 2010 (compounding effect). This figure does not take into account the maintenance cost of the house and local taxes such as quit rent and assessment.

2. Bank fixed deposit

The bank fixed deposit is currently paying less than 3% interest p.a. which hardly covers the price surge of essential goods and housing. Many still put money in fixed deposit for liquidity purpose, as it takes only 5 minutes to get cash from them compared to 4-10 months required to liquidate a house.

3. Stock Market

Many investors also put some savings in stocks and shares in Malaysia, and over 10 years, (2000-2010), the Kuala Lumpur Composite Index rose an average rate of 3.2% p.a. (compounded and without taking dividend into account), which is only slightly above the official inflation rate.

4. Gold

In order to encourage local Malaysians to save in gold, the Malaysian Government started, in July 2001, to issue the locally minted coins in pure gold (9999) called Kijang Emas (The golden Mouse Deer).

These coins in ¼ oz, ½ oz and 1oz are minted by Bank Negara Malaysia and made available throughout Malaysia at the Malayan Banking (Maybank) branches which sell the gold coins in Ringgit at rates published daily.

In July 2001, the price of a 1oz Kijang Emas was RM1082 and by Dec 2010, it was selling at RM4,624. Using the average yearly price over the last ten years (2001-2011), the price of local gold coins have risen at an average compounding rate of 15.7% p.a.

Coins bought in 2001 and sold them in 2010 would get a good appreciation of of 15.2% p.a. or total gain of 258% in Ringgit value (taking into account the 4% spread).This rate is definitely higher than the official inflation rate.

A history of 1oz Kijang Emas Gold Coin Selling Price in Ringgit Malaysia can be found on the following page.

Year	RM Yearly Average	% Yearly change
2001	1,121	
2002	1,253	11.8
2003	1,467	17.1
2004	1,653	12.7
2005	1,788	8.2
2006	2,344	31.1
2007	2,533	8.1
2008	3,070	21.2
2009	3,599	17.2
2010	4,177	16.1
2011(Apr)	4,555	9.0

(Data Source: Bank Negara Malaysia Official Website)

Preferred Method by Malaysians

From the amount of money invested, it is obvious most Malaysians with high savings prefer to invest in houses over the hoarding of gold as a method to protect their savings from losing their purchasing power. The main reasons are:

1. Banks are keen to make housing loans to Malaysians to invest in houses, and will never lend money to people to buy gold. Hence house buyers get leverage in the return on their investment in a rising house market.

2. Most people do not understand how the fiat monetary system functions, and they do not understand the importance role of gold in the monetary system.

Many Malaysians are influenced by Warren Buffett and his most famous quote about gold:

"Gold gets dug out of the ground in Africa, or somewhere. Then we melt it down, dig another hole, bury it again and pay people to stand around guarding it. It has no utility. Anyone watching from Mars would be scratching their head."

Note: on a yearly average basis, Berkshire Hathaway appreciated in USD value of 22% p.a. over the last 44 years (1966 – 2010), and Warren Buffett was voted by money managers as the greatest investor of the last century. However, over the last 9 years (2001 to 2010) his average yearly performance of 5.3% p.a. was consistently beaten by gold's 15.7% p.a. appreciation in Ringgit value.

When confronted with the above quotation of Warren Buffett (WB), my friend Mr.GB would always reply with the following story:

> One day, two aliens from the Planet A.S. (All Saints) visited Earth, and they met Earthling GB.
>
> Alien WB said, "I am amazed by the practice of you Earthlings. Why would you use locks to lock your doors? Why do you use gold as money?"
>
> Earthling GB: "We use locks to keep thieves out."
>
> Alien WB: "In Planet A.S. throughout all generations, people are honest and we have the DNA of the Saints. The A.S. people including our leaders are honest, and always have the interest of their people in their hearts.
>
> There is no crime or thief in A.S., hence no locks, no policeman or security guards. They have no utility in our Planet A.S.
>
> We do not need to elect our leaders. It is a waste of time & resources, and we definitely do not use the gold standard, as our leaders are perfectly honest and have infinite wisdom; they know how much money to print and will not steal the savings of the people via the stealth tax or printing of more fiat money than necessary."
>
> Alien CM said: "You can't eat locks! In Planet A.S. those who bought locks are irrational and immoral. These lock bugs are jerks."
>
> Earthling GB: "But here on Earth, we need locks, policeman, security guards, and gold to prevent theft of our properties including our savings. Only the thieves and crooks in disguise always discourage us to invest in locks.
>
> We have very few Mother Teresas on Earth. We must have frequent elections of leaders. We use gold standard as a fair accounting tool, and I can tell you these activities are not a waste of time or resources as they improve the quality of life and productivity of society."

Conclusion

In the last 10 years it appears that a good way to protect savings against inflation in Malaysia is by converting saving into gold coins or investing in houses by taking a mortgage.

Using leverage of a housing loan, one can gain wealth faster in a rising housing market, but then history tells us all bubbles will pop one day.

With the house price affordability of 9 times over the median household income, we in Malaysia may run out of buyers one day and when the housing bubble pops, many leveraged investors will find their wealth shrinking faster than it rose in the last decade.

Philip T

Should the Silver Standard Accompany the Gold Standard?

Several important reasons exist to have the silver standard accompanying the gold standard. However, the old bimetallic standard with a legally fixed ratio or exchange rate between the two metals should not exist. The markets should determine the exchange rate between the two.

A silver standard easily accomplishes what gold cannot. Precious metal coins should be in a convent denomination sufficiently small enough to pay the daily wage of a common labor or migrant field worker with one or more coins.

The daily wage of a common laborer is less than a pennyweight of gold. Two pennyweights is about the practical limit of the minimum size of a gold coin. A two-pennyweight coin is about the size of a dime.

Silver coins can easily fill this void. In silver, a day's wage for a common laborer would be a little more than 20 pennyweights (one ounce) of silver.

A common laborer should be paid in true, full-bodied money, and not in token coins or credit money, which is what he would receive under the gold standard. He should be able to carry true, full-bodied money in his pocket and have true money to spend if he so desires, and not just token coins or credit money. A silver standard provides him this service.

Another advantage of having both standards is that one metal, silver, provides convent coins for small value. The other, gold, provides coins for large value. The tendency would be to price cheap items in silver and expensive items in gold. Sliver coins are likely to circulate more than gold coins.

Historically, silver has been better suited for trade (buying and selling of goods and services), and gold, for commerce (large scale exchanges of goods). Silver seems more suited for industrial and agricultural areas, and gold, for the commercial and financial arenas. However, the markets should determine which products and services are priced in terms of silver and which in terms of gold. To allow coins of both metals to circulate freely gives the people the advantage inherent in both metals.

If only gold were money, then token and paper money would be needed to buy most items. Most common items are priced below two pennyweights of gold. Gold coins could not be used to buy these items individually, or if used, the change would not be in gold coins. However, if silver were money, silver coins (as silver money and not as subsidiary coins for gold) could be used to buy most of these items. Some items would be priced below two pennyweights of silver, and token coins would be needed to buy then individually.

Perhaps the most important reason for having both the gold and silver standards is that together they make replacing commodity money with fiat money more difficult. When the silver standard accompanies the gold standard, it protects the gold standard from deteriorating into fiat currency. "Gold must be priced in something other than gold, otherwise every sale of gold would have to end up as exchange of amounts of gold..."[1]

To maintain an honest monetary system, this something has to be a monetary metal in its own right. Silver is the most appropriate commodity money for this purpose. When both metals are money, each metal in the form of bullion can be priced in terms of the other metal. Otherwise, under a monometallic standard, the monetary metal in

bullion form is priced in paper notes or token coins, which introduces a fiat unit of accounts. The gold and silver standard is much more effective at protecting the integrity of the money than either standard alone.

A historical example of a dual monetary system occurred in the United States between 1862 and 1879. During this era both U.S. note (greenback) dollars and gold dollars circulated as money. Both were used for purchases and wages. Because U.S. notes were not redeemable in gold, no fixed exchange rate existed between fiat U.S. notes and gold coins. However, in most of the United States, U.S. notes were used for the payment of debt because they had legal tender status and were less valuable than gold.

Moreover, many third world countries operate with a dual monetary system. Many use the U.S. dollar and a local currency; sometimes a relatively strong regional currency is also used. They function with little difficulty going between currencies even without modern technology. Also, stores along the U.S.-Mexican border accept both Mexican pesos and U.S. dollars. With today's technology, conversion between gold and silver should be without difficulty. If an item were priced in silver, it could easily be bought with gold and vice versa.

[Editor: This is the second in an excellent and comprehensive, twelve part series by Thomas Allen on Real Bills. Each issue of The Gold Standard will contain one of these original pieces until we run out in April 2012.]

Thomas Allen

Thomas Allen has been a student and adherent supporter of the gold standard and the real bills doctrine since 1972. In 2009, he wrote and published Reconstruction of America's Monetary and Banking System: A Return to Constitutional Money. Many of his writings on money and other subjects can be found at http://tcallenco.blogspot.com/ and an index to these blogs is at http://tcallenco.weebly.com/

Notes:

1. J.N. Tlaga, "Gold Standard = Fiat in Disguise," Jan. 19, 2002, http://www.goldeagle.com/editorials_02/tlaga011902pv.html, Aug. 8, 2007.