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Without a doubt

"If we begin with certainties, we shall end in doubts; but if we begin with doubts, and are patient in them, we shall end in certainties."

- Francis Bacon.

"A good man always knows his limitations."

- Dirty Harry.

The next commentary will be out on Monday 5th July.

If there is just one reason to be wary of the advice of economists, it is the invariable presumption of certainty. Just do X, we are told, and Y will be the outcome. The most influential economic thinker of the 20th Century, John Maynard Keynes, left us with the now hugely ironic observation that

"Practical men, who believe themselves to be quite exempt from any intellectual influences, are usually the slaves of some defunct economist."

Ironic because Keynes, or his ghost, is now the defunct economist-in-chief. Governments throughout the industrialised world have been brought to the brink of insolvency through an unswerving commitment to deficit spending that could be broadly described as Keynesian. For one sovereign entity within a much larger economic system, the approach to insolvency is troubling but can be managed. But when the system itself approaches collective insolvency, the outlook has the whiff of chaos about it. Global banking crisis begets deflationary recession which begets further deficit spending which begets sovereign debt crisis which begets global currency crisis which begets.. ? The government debt and currency markets are not really so different from the banks. They depend upon a critical mass of inherent confidence.

As Liaquat Ahamed cogently but ominously points out in 'Lords of Finance: 1929, the Great Depression, and the Bankers who Broke the World' (Windmill Books, 2010), we have been here before. The financial crisis today has a mirror image formed in the 1930s. A vast pile of government debt had been allowed to accumulate (then: as a result of the costs of war; now: as a result of slavish attachment to defunct economics. The mutual characteristic is the malign influence of politicians). The problems of the 1930s were born during the Paris peace conference that ended the First World War. France was determined to make Germany pay. France, for her part, owed

money to Britain and the United States. Britain, in her turn, owed money to North America. The global trade system was balanced precariously upon thin strands of interlinked indebtedness. When a banking crisis severed those strands, the global trade system collapsed upon itself.

"In December 1930, the Bank of United States, which despite its name was a private bank with no official status, went down in the largest single bank failure in US history, leaving frozen some $200 million in depositors' funds.

"In May 1931, the biggest bank in Austria, the Creditanstalt, owned by the Rothschilds no less, with $250 million in assets, closed its doors. On June 20, President Herbert Hoover announced a one-year moritorium on all payments of debts and reparations stemming from the war.

"In July, the German chancellor, Heinrich Brüning, declared a bank holiday, restricted how much German citizens could withdraw from their bank accounts, and suspended payments on Germany's short-term foreign debt. Later that month the crisis spread to the City of London, which, having lent heavily to Germany, found these claims now frozen. Suddenly, faced with the previously unthinkable prospect that Britain itself might be unable to meet its obligations, investors around the world started withdrawing funds from London."

The Euro today is playing the part of the gold standard in the 1930s. Britain, then as now playing a pivotal role in the world monetary system, was hamstrung in that its ability to devalue Sterling was constrained by its membership of the gold standard, by which Sterling was pegged to gold in the ratio of 113 grains of the metal. Since all the major currencies were interlinked, Sterling was essentially pegged to the US Dollar, at a rate of $4.86 to the pound.

The gold standard ultimately collapsed, but not before it had wrecked the economies of those countries that determinedly clung to it, at punitively high exchange rates, for the sake of world monetary order. This is where the likes of Greece and Portugal are today. The Euro for them has become a doomsday machine; their membership of the Euro zone allows them no room for manoeuvre to depreciate their currency and remain competitive given their high labour costs.

Overnight bank deposits held within the European Central Bank have risen to record levels. In an uneasy echo of Lehman Brothers, banks throughout Europe – holding vast amounts of government debt of questionable value – are no longer sufficiently trusting to lend to each other. The ECB in turn has done itself no favours, having back-tracked grotesquely over its treatment of (toxic) Greek debt. Governments, having spent all their ammunition bailing out ungrateful banks, have nothing left in their armouries. The cupboard, as the UK electorate will have confirmed for them this week, is bare.

Meanwhile, academic debates among the economic classes continue to oscillate wildly between deflation and inflation. In pure and classical economic terms, we already have both: a deflation in the prices of leveraged assets, and an inflation in the money supply, as governments succumb to the path of least resistance during a debt crisis, namely money-printing. Federal Reserve Chairman Ben Bernanke – who has specialised in study of the Great Depression, not that you could necessarily tell – claims to be puzzled by the rise in the price of gold. Taking him at face value, as opposed to thinking he is being disingenuous, there is no puzzle. Investors are losing faith in fiat currency (fiat: from the Latin "let it be done"; hence a currency given apparent value solely by government decree) and are voting in favour of real money (gold, which has served as a store of value for thousands of years, and which owes whatever its value to a free market, as opposed to arbitrary government sanction).

It is by no means clear where, as investors, we will end up. There is little point adopting a hardline, dogmatic economic stance: that would be beginning with certainties. There is surely more value in keeping a mind open to both financial and political uncertainty. Traditional gatekeepers of value are no longer fit for purpose. Take the ratings agencies (please !) – the website Hedged.biz has "downgraded Fitch, Moody's and Standard & Poor's from AAA directly to junk.

"For downgrading (upgrading) issuers only after price discovery has occurred and being reactive rather than proactive. For downgrading (upgrading) issuers only after bad (good) stuff has happened and been priced in. Downgrading BP over a month after their rig in the Gulf blew up is not very useful.

"For operating a conflicted model whereby the issuers pays the credit ratings agency to provide a rating. For the audacity to rate instruments which they did not fully understand. [Most damningly] For being part of a feedback mechanism of automatic leverage and deleverage."

Governments are doing their best to muddy the financial waters. It is impossible to assess values for financial instruments when the risk-free rate (whether defined as something approximating to cash or the interest rate payable on short-term government bonds) sits at zero due to administrative manipulation. Since governments are widely also attempting to depreciate their currencies in the (probably futile) cause of driving exports – we cannot all take in each other's washing – there is a wholesale and growing flight from fiat. This is still, we would argue, being misunderstood. Dr. Paul Kedrosky on Seeking Alpha suggests that either gold is overvalued or everything else is undervalued. (The binary structure of this expression is not helpful.) Gold is certainly not "(newly) part currency" – it has always been currency. Or as one respondent ironically observed:

"For any author to suggest that gold or other "hard assets" could possibly be "over-valued" versus worthless paper proves that this "doctor's" degree is ALSO just more worthless paper."

And as another even more ironically observes,

"Right. Gold is in a 4,000 year bubble, and we should accept this. Fiat currencies are far more stable than that."

It would be madness, when faced with such massive and systemic uncertainties, not to have an element of portfolio or wealth insurance. Gold in its various forms (physical / ETF / mining companies) goes some way to providing that insurance.

And as we shepherd our assets through this period of acute uncertainty, we should try and learn to live with our limitations, rather than seek the certainty of being wholly and unchallengeably right. As Kathryn Schultz says, in discussion of her book "Being Wrong: Adventures in the Margin of Error" (Portobello Books, 2010):

"Recognizing that error is an inevitable part of our lives frees us from despising ourselves — and forbids us from looking down on others — for getting things wrong. Once we recognize that we do not err out of laziness, stupidity, or evil intent, we can liberate ourselves from the impossible burden of trying to be permanently right. We can take seriously the proposition that we could be in error, without deeming ourselves idiotic or unworthy. We can respond to the mistakes (or putative mistakes) of those around us with empathy and generosity. We can demand that our business and political leaders acknowledge and redress their errors rather than ignoring or

denying them. In short, a better relationship with wrongness can lead to better relationships in general — whether between family members, colleagues, neighbors, or nations.

"Embracing fallibility to prevent catastrophic error, embracing fallibility to prevent conflict: These are two hugely worthy goals. But learning to do either one consistently is close to impossible as long as we insist that mistakes are made only by morons, and that an intelligent, principled, hard-working mind is the only backup we need. This is the deep meaning behind the pat cliché "to err is human." Take away the ability of an intelligent, principled, hard-working mind to get it wrong, and you take away the whole thing."

Buy a copy for a politician you know.

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