PFP
Wealth Management

3 Windsor Court
Clarence Drive
Harrogate, HG1 2PE
01423 523311

Lion House
72-75 Red Lion Street
London, WC1R 4FP
020 7400 1860

www.pfpg.co.uk

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Gold-shouldered

"Give me control of a nation's money and I care not who makes her laws."

- Mayer Amschel Rothschild.

Alan Greenspan was one of the most over-rated Fed chairmen in history. (This coinage is admittedly akin to the phrase "one of the greediest bankers"; Bob Woodward even titled his biography of Greenspan 'Maestro' – one eagerly awaits his biography of Hitler, which will presumably be titled 'Pacifist'.) But even Alan Greenspan was capable, very occasionally, of speaking like an honest human being, as opposed to a machine for uttering gibberish. Replying to a question about social security funding in 2005, Greenspan inadvertently nailed the fundamental problem of an inflationist welfare state:

"We can guarantee cash benefits as far out and at whatever size you like, ***but we cannot guarantee their purchasing power."*** [Emphasis ours.]

In other words, the central bank can always create money – but there's no guarantee it will be worth anything. Another quotation is equally astonishing in its candour. Years before he sold his soul and credibility to become a stooge for Wall Street, he wrote, in 1967, that

"In the absence of the gold standard, there is no way to protect savings from confiscation through inflation. There is no safe store of value. If there were, the government would have to make its holding illegal, as was done in the case of gold.. The financial policy of the welfare state requires that there be no way for the owners of wealth to protect themselves.

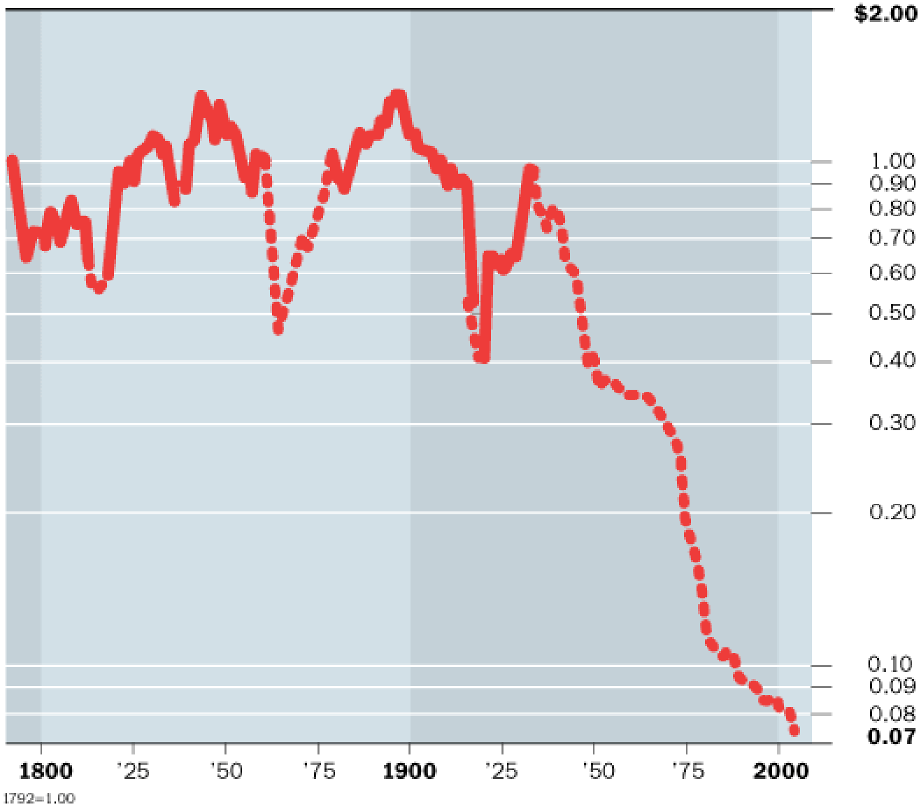
"This is the shabby secret of the welfare statists' tirades against gold. Deficit spending is simply a scheme for the confiscation of wealth. Gold stands in the way of this insidious process. It stands as a protector of property rights. If one grasps this, one has no difficulty in understanding the statists' antagonism toward the gold standard."

Greenspan may have – at least once – understood and articulated the attractions of gold when the monetary authorities go mad. His successor, the Ben Bernank (caution: parental advisory), shows not even this tenuous grasp of market realities. Hopelessly intellectually outmatched by congressman Ron Paul (caution: parental advisory), the current Fed chairman claims, amongst other things, that consumers don't want to buy gold. US consumers may not want to buy gold, but somebody does, unless the gold price rose last week to a record nominal high by osmosis alone. And we think the reason that a growing constituency of investors want to hold gold is because

Bernanke, and others, are busily destroying the purchasing power of paper money. Of course, when Ron Paul grills Bernanke on what defines and supports the dollar as a store of value and a unit of account – given that it no longer has metallic backing – he disingenuously replies: its purchasing power. The chart below would tend to suggest that Ben Bernanke is both a liar and an idiot – and we don't even feel particularly strongly about him.

The Greenback's Purchasing Power

This log scale chart of the purchasing power of the dollar begins with an index value of 100 at the passage of the Mint Act of 1792. The solid lines present periods when the dollar was convertible into a specific quantity of gold, and the fluctuations represent changes in the purchasing power of gold. The dotted lines present periods when the dollar was not pegged to gold, during and after the War of 1812, the Civil War, World War I and World War II. There was limited convertibility from 1945 to 1971, but the dollar lost purchasing power during the period. The last link between the U.S. currency and gold was cut in 1971 and the loss of purchasing power accelerated. By 2004, the dollar had lost more than 92% of its original purchasing power.

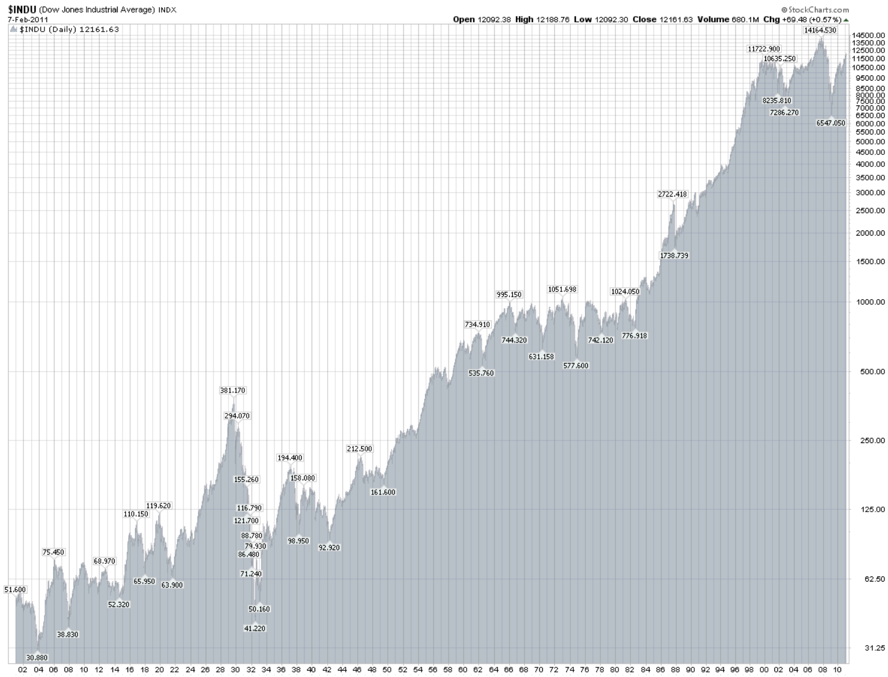


Source: Chart by American Institute for Economic Research, from the Wholesale Price Index compiled by the Bureau of Labor Statistics

As a tool of the banking cartel, Bernanke of course is not entirely free to articulate an honest attitude towards gold as opposed to paper money, but otherwise intelligent asset managers are, and for reasons known only to them, choose not to. Robert Blumen ("Why value investors hate gold") highlights two of them: Jeremy Grantham ("I hate gold. It does not pay a dividend, it has no value, and you can't work out what it should or shouldn't be worth.. It is the last refuge of the desperate"), and Warren Buffett ("I have no views as to where it [the price of gold] will be, but the one thing I can tell you is it won't do anything between now and then except look at you. Whereas, you know, Coca-Cola will be making money, and I think Wells Fargo will be making a lot of money.. The idea of digging something up out of the ground, you know, in South Africa or someplace and then transporting it to the United States and putting it into the ground, you know, in the Federal Reserve of New York, does not strike me as a terrific asset.")

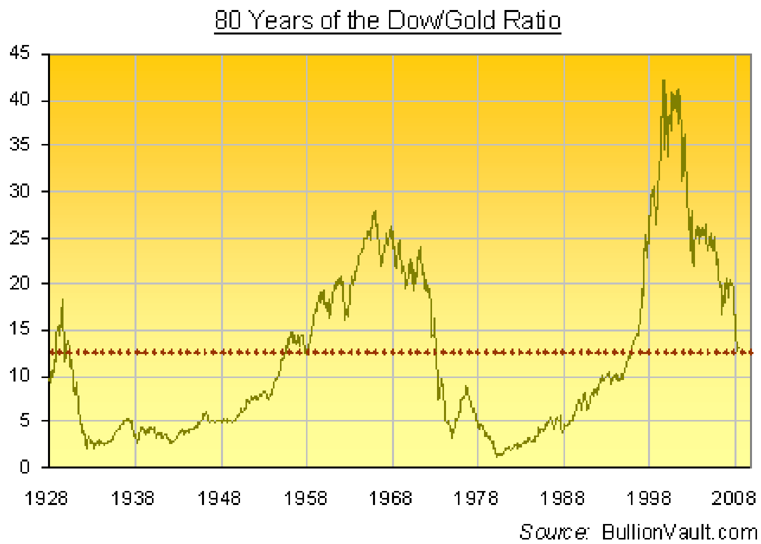
Of course, Buffett, with his preferential access to investments in the likes of Goldman Sachs, has recently migrated toward the dark side, and toward the forces of Wall Street, as opposed to Main Street. Either way, and not for the first time, Buffett is being a trifle disingenuous. It is also impossible to "value" silver in the same way as stocks or bonds, and that didn't stop him from acquiring a significant holding in the metal between 1997 and 2006. What is more disconcerting in Buffett's tired and hypocritical disdain for the monetary metals is his apparent confusion of nominal returns with real ones. In nominal terms, the Dow Jones Industrial Average had a good twentieth century:

Dow Jones Industrial Average, 1900 – 2000 (log scale)



Starting point: 51. End point: 11,497.

But express those returns in a proper store of value and unit of account, i.e. gold, and the returns look more modest:



Since 1928, on average, the Dow has sold for around 13 ounces of gold. It reached an all time high of c. 42 ounces of gold in 2000, and is currently at around 9. Note that in 1980, it traded for around 1 ounce. As the chart shows, since 2000, the Dow Jones in terms of gold has already suffered a monumental crash. If the Dow were to match its previous lows (1932; 1980), in terms of gold, it would be trading at around 1500 (it is currently around 12,200). Suffice to say: in real terms, adjusted for an endlessly depreciating currency, stock market returns have been uninspiring. In the words of Rod Rojas, the rise in stock prices or any other good denominated in paper currency may not say much about the real value of your investments.

“The point that is being missed is that gold is a commodity as well as a monetary metal. There is a market for gold outside the monetary realm, and this is an additional component to its value that modern paper currencies do not have. In that sense one could say that gold’s value as a commodity gives it that ‘price floor’, or downside protection.

“But above all, gold has value because [*pace* Ben Bernanke] people want it and because it is scarce. It is that simple.”

As befits a mouthpiece for ‘conventional finance as usual’, Lex asked last week why investors want safety but were not finding it in the dollar. To which the appropriate response has to be: if the dollar, and all it represents, is not the solution, it is surely part of the problem.

We conclude this week with some timeless quotes.

“Whoever controls the volume of money in our country is absolute master of all industry and commerce.. when you realise that the entire system is very easily controlled, one way or another, by a few powerful men at the top, you will not have to be told how periods of inflation and depression originate.”

- James Garfield, 20th US President, assassinated two weeks later.

In a letter attributed to the Rothschilds:

“The few who can understand the [banking] system will be either so interested in its profits, or so dependent on its favours, that there will be no opposition from that class, while, on the other hand, that great body of people, mentally incapable of comprehending the tremendous advantage that Capital derives from the system, will bear its burden without complaint and, perhaps, without even suspecting that the system is inimical to their interests.”

Most ominously, in the context of the current spirit of denial against gold and its legitimate, free market monetary history by comparison with unbacked, government-coerced and disintegrating fiat:

“A great deal of intelligence can be invested in ignorance when the need for illusion is deep.”

- Saul Bellow.

Be careful what you believe, because it may not be true. Illusion in money terms is an extraordinarily dangerous thing. If the prices of gold and silver are any guide, the monetary illusionists are slowly – perhaps not so slowly – losing their grasp on the crowd. As the Wizard of Oz said, in something of a panic: pay no attention to that man behind the curtain.

Tim Price
Director of Investment
PFP Wealth Management
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Email: tim.price@pfpg.co.uk Weblog: http://thepriceofeverything.typepad.com

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